HANDBOOK FOR SMALL BUSINESS

By SCORE Chapter 225
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Management and Planning Series

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Realizing that small business is the backbone of this country's competitive free enterprise system, Congress, in 1953, created the U.S. Small Business Administration. SBA defines a small business as one independently owned and operated, and not dominant in its field. SCORE is part of the SBA's business development program.

To start a new business and remain in business profitably, one must be able to adapt to changes in the population, work force and technology, and to the demands of a global marketplace. To address these changing conditions, sound management and organizational practices are more important than ever before. The necessity of increasing productivity of employees, the difficulties in recruiting qualified workers from a shrinking labor force and the importance of devising ways to meet workers' benefits will challenge managers of all small businesses.

America's future depends on the continued emergence of successful small businesses. To be successful, those who start a new business must be prepared. It is the purpose of this *Handbook for Small Business* to provide information in the simplest terms to help new and existing businesses to be successful. The mission of SCORE is to help people get into business, stay in business and make a profit.

More detailed information on the various facets of operating a business is available. Much is contained in the publications and video/audiotapes listed in the SBA booklet, *The Small Business Directory, available* from SCORE or the SBA.

Handbook for Small Business is designed as an extension of the SCORE concept of service to the small business community. It is a comprehensive presentation of general information. To a considerable extent, its contents reflect the personal and practical experience, which *is* the hallmark of the SCORE counseling procedure.

Handbook for Small Business is not offered as a substitute for in-person counseling, but rather as an enhancement of counseling. It is published with the understanding that the publisher is not engaged in rendering legal, accounting or other professional service.

Although this publication has been prepared by competent, knowledgeable and experienced contributors, it should not be used as a substitute for professional or other authentic sources in specific situations. As pointed out repeatedly in the book, legal or other expert assistance should be sought when required.

STARTING A BUSINESS

Some of the reasons people start new businesses are

For fmancial independence

To be one's own boss

For creative freedom

What equipment and supplies will I need?

What insurance will I need?

What skills or experience do I have?

What are my financial resources?

What finances are necessary to start and maintain the business?

How will I compensate myself?

How will the business be managed day to day?

How will I identify customers and how will I reach them?

How will I hire and pay employees?

How will I best serve the needs of my customers?

Because going into business is a risk, careful preparation is essential. A business plan is critical to determining if the risk of entering into a business is worth taking. Various chapters of this *Handbook* discuss preparation in much greater detail. Once the decision has been made to open the business, the remaining steps are quite simple.

If the business is to be operated as a sole proprietorship, and you use your name, it is usually unnecessary to register the business with your city, town or state. (See "Naming a Business"). If you do not use your own name, the business may need to be registered with the municipal or town clerk. Partnerships must be registered locally and corporations with the state.

If you are to have employees, or will be a partnership or corporation, you must obtain a business identification number from the Internal Revenue Service (IRS) by filing Form SS-4. Also, all businesses that have employees must register with their state division of employment and training, and must pay unemployment insurance taxes to the state as well as to the federal government.

NAMING A BUSINESS

Every business needs a name. Because a name is an important asset to a business, it should be selected carefully.

Before choosing a name, it is advisable to look at the types of names in use by businesses similar to yours. To prevent choosing a name already in use, check lists of business names available in telephone books, libraries, city and town halls, and trade journals. Names of corporations can also be checked at the corporate division of the office of the Secretary of State. To guarantee availability of your intended corporate name, contact your state's corporate division for an application and fee

Ease of Formation. A sole proprietorship is the easiest and least expensive form of a small business to begin, as well the one with the fewest legal restrictions. No government approval is needed to begin operation. If the business is in your own name, just open the door and start. If you have employees, the business must be registered with the federal government on Form SS-4. State and local government registration may also be necessary.

Sole Ownership. The proprietor shares the profits with no one, and the decision making is vested in one person.

Control. The sole proprietor is in complete control of his or her business.

Flexibility. Management can quickly respond to the needs of the business and can make the day-to-day decisions so often critical to a new business's success.

Freedom from Government Control. There are no special taxes for this form of business, including no state or federal taxes. Profits become the owner's personal income and are taxed as such.

Disadvantages

Unlimited Liability. The sole proprietor is responsible for the full amount of business debts. These could exceed the proprietor's total investment. Be aware that this liability extends to all the proprietor's assets, including his or her home.

Less Available Capital. Capital is limited to the owner's personal assets and the funds the owner can borrow. Hence, this form of business ordinarily has less capital available than the other forms. Also, it *is* usually more difficult for a sole proprietor to borrow money for the business.

Unstable Business Life. The business may be crippled or terminated upon the illness or death of the owner.

Experience Limitation. Single owners operating with no or few employees are often limited in experience and viewpoint compared to those in the other forms of business.

Limited Business Deductions. Certain types of business deductions are not available to the sole proprietor. These include workers' compensation insurance and a portion of personal health and injury insurance.

Partnership

A partnership is an association of two or more people as co-owners of a business for profit.

Although not required by law, written articles of partnership are customary and highly recommended. These articles of agreement state the financial, material and managerial contributions to the business by each owner. The articles should clearly spell out the role of each partner and the share of the profits each will receive. There should be provisions in the articles both for dissolving

A corporation is a legal entity distinct from the individuals who own it. It is the most complex of the three forms of business.

A corporation can only be formed by authority of a state government. Check with your attorney or your state's agency that supervises corporations for details of registering your business and information on the laws affecting corporations.

As soon as you are notified that your organization has been approved, you must file for a federal identification number using IRS Form SS-4. As noted earlier, check into licenses and permits before doing business.

Advantages

Separate Legal Existence. The corporation is distinct from the individuals who own it.

Limited Liability. Individual shareholders are not liable for debts of the corporation.

Ownership Readily Transferable. Owners invest in shares of the business, which can be bought and sold.

Stable and Relatively Permanent. Death of a shareholder does not end the business.

Relatively Easy to Secure Funds. The foundation of investors' stock purchases gives confidence to lenders of the corporation's stability.

Delegated Authority of Management. A board of directors and officers give structure to decision making.

Skills and Expertise Available from Many. Boards of directors usually are made up of members with a wide variety of perspectives, in addition to their interest in the specific corporation.

Disadvantages

Extensive Government Regulation. Corporations must be registered with state government and are subject to more extensive regulation by local and federal government than are solely owned businesses or partnerships.

Complicated Tax Reporting. Taxation of corporations *is* totally different from taxation of individuals. A corporation's dividends affect tax returns of individual shareholders.

Double Taxation. Profits are subject to corporate tax and, if distributed to the stockholders, are taxable as personal income.

Limited Incentive. If management does not share in the profits, there is usually less incentive.

Once you have determined the purpose, type, name and structure of your business, you must find out if a license or permit is required. Many businesses require one or the other. To operate without one may be illegal.

A license is a privilege granted by a legislative body at its discretion. A permit is a right that anyone can obtain if the requirements of the granting agency are met. Licenses and permits may be granted at the town, city, county or state level. Table 1 lists departments that issue licenses or permits at the local level.

Table 1 - License or permit issuing bodies

Department	Authority
Building	Construction, renovations, zoning, signs
Health	Food handling, rest rooms, sewer connections, septic systems
Council	Licenses and permits
Town Clerk	Business certificates
Police	Alarm & business registrations
Fire	Safety inspections, alarm registrations
Weights and Measures	Weighing and measuring, packaging and labeling
Conservation Commission	Wetland alterations, building and activity near wetlands
Historic	Signs, building and home alterations, business activities

Exhibits 1 and 2 list types of businesses, trades and professions that often require a license, permit or registration. These lists may not be complete. Check with your attorney or local government for requirements in your area.

Food or beverage service, sale or preparation

Fortune tellers

Hawkers and peddlers - balloons souvenirs arts and crafts, flowers, auctioneers

Hazardous chemicals or flammables

Insurance agents, adjusters, brokers, advisors

Junk dealers

Lodging - hotels, motels, inns, bed and breakfasts, guesthouses

Motion picture operators

Motor vehicle appraisers

Notaries public, justices of the peace

Nursing homes

Outdoor advertising

Painters, riggers

Pet shops, riding schools, cattle dealers, stables, riding instructors, guard and hearing dog businesses

Restricted pesticide dealers and applicators

Solid fuel burning, construction supervision

Exhibit 2 - Professions and Trades Frequently Requiring a License or Registration

Allied health professions
Architects
Athletic trainers
Attorneys
Audiology
Barbers

Landscape architects
Nursing
Occupational therapists
Optometry
Pharmacy
Physical therapists

An example of an objective might be "to increase my business from $24,000 to $36,000 in the next 12 months." Another might be "to prepare, have printed and distribute 1,000 flyers to shoppers in the local mall, all within two months." Others might be "to hire and train a new sales clerk before the end of the fiscal year" or "to telephone each account receivable at the end of each month and to personally visit accounts that are more than six weeks delinquent."

Objectives should be written for every phase of a business, such as sales, service, bookkeeping, advertising, employee relations and marketing. Note that objectives should be written and reviewed frequently.

Keeping Records

Know your figures and keep them up to date. Doing this is the only way you will know how the business is faring on a daily, weekly and monthly basis. Stationery and other stores have simplified bookkeeping systems available, or you can engage the services of an accountant or bookkeeper. Accurate records are needed by business owners and managers not only to make informed decisions, but also to support reports required by federal, state and local government agencies. (See the section on record keeping below.)

Reviewing Records

Keeping adequate, accurate records of your business permits you to use them in the daily management of the operation. At the end of each month you should compare the actual profit and loss and cash flow statements with the goals identified in your business plan. This way you can see your progress and take the proper action. You should not only review the financial area, but also evaluate marketing, sales, advertising and other operational goals.

Taking Action

Do not procrastinate! If something is not working as you planned, do something about it - now! Don't become paralyzed by inaction. Every well-developed business plan should detail how the following will be accomplished:

Deciding - Determining what must be done.

Planning and scheduling - Setting time tables.

Performing - Following through on decisions.

Controlling - Monitoring events as they occur.

Coordinating - Ensuring that each objective is in harmony and not at odds with the others.

Recording and documenting - Keeping accurate and complete records.

Join a trade association for your industry.

Read the same publications that your competitors and customers read.

Constantly scrutinize your competitors' advertisements and read their sales literature.

Ask yourself the following about your competition: Is their business increasing or decreasing? How do you compare as far as quality, price, product line, exclusivity, service, reliability, location, warranties, delivery and courtesy are concerned?

Talk regularly about business-related subjects with other small business owners.

Review financial and marketing strategies often.

Have regular training sessions for and regular motivation meetings with your employees.

Recognize your own weaknesses and get help in these areas.

Review the business plan monthly.

Tell everyone on the payroll exactly what his or her responsibilities are and what is expected.

Treat employees as individuals.

When an employee does a good job, tell him or her.

Keep as accurate a set of records as possible.

Analyze your records often and take any appropriate steps that may be indicated.

Take pride in your business.

FINANCING A BUSINESS

One of the leading causes of business failure is insufficient start-up capital. Therefore, a crucial element for business success is adequate financing. Not only are funds required for start up, but also to cover initial operating losses and provide for growth.

As a general guide, one should have sufficient cash to cover at least one year's operating expenses, which includes the owner's salary and money to make regular loan payments. Almost all business operators hope their business will grow, yet some fail because, after a successful start, additional

$65,000 to $75,000 from the bank. In the case of a restaurant, the bank may require the borrower to invest 50 percent of his or her own money.

Banks require that you have a good personal credit record and, in most cases, will require some form of collateral to secure the loan. Collateral can be in the form of assets used in the business or personal assets, including the unused equity in your home.

Credit Unions

Many companies, labor unions and government agencies have credit unions for their employees or members. Credit unions perform functions similar to banks, including making personal loans to their members. If you are a member of a credit union, check it out as a possible source of a business loan.

Loan and Finance Companies

These are companies that specialize in making personal loans for business purposes. Some of the larger companies make business loans as well as personal loans.

Life Insurance Companies

Many life insurance policies have provisions for the accumulation of a "cash value," against which funds may be borrowed. Some policies call it the "loan value." The interest rate, established in the policy, is usually less than the commercial rate. Check to see if you, parents or friends have life insurance with loan values as they can be an excellent source of fmancing.

Small Business Investment Companies

Small business investment companies (SBICs) are privately owned companies licensed by the SBA to provide capital to small businesses. SBICs look for businesses that have proprietary products with high growth potential. Young, lower-risk, aggressive companies are preferred. Usually, an SBIC wants a share in the business.

Community Development Companies

Many communities have established community development companies (CDCs) to help attract new business to their area. Frequently, they are used to develop commercial or industrial parks. Check to see if your community has a CDC. If so, you should talk to them.

Suppliers

In order to encourage sale of their products, many suppliers provide retailers with shelving, display cases, refrigeration units and so on at very favorable terms. Caution should be used when financing assets through a supplier; be sure you understand any commitment you have to make regarding purchasing the supplier's product in the future.

worthwhile. It indicates to a prospective lender or investor that you thoroughly understand your business and its financial demands. The proposal must be thorough, concise and neat. It may be submitted in longhand, but it is worth the money to have it typed. Cash flow charts may be submitted in writing.

The proposal should answer most of the questions that will be asked by a prospective lender and should present a convincing picture. Tell it like it is, being totally honest. Overstatements of facts and figures will not serve you well in the long run and will be challenged by an astute lender. If you cannot prepare this yourself, get help. It will pay off!

Exhibit 3 provides an outline of a typical loan proposal.

Exhibit 3 - Outline for a Loan Proposal

Cover Page
- A. Name, address and telephone number
- B. Name and title of principal(s)
- C. Amount of loan (investment) requested
- D. Purpose of the loan (investment)
- E. Repayment terms of the loan

II. Description and Summary of the Business
- A. Length of time the business has been operating
- B. The business's historical trend
- C. The nature of the business What does it do?
- D. What is unique about your product line or service?
- E. What or who is your **market?**
- F. The business's competition
- G. The business's long-term growth plan
- H. Trends in your industry

III. Management
- A. Your management experience
- B. Your management team
  - 1. Table of organization
  - 2. Brief resume of key individuals and their responsibilities
  - 3. Current staff or work force level and future needs
  - 4. Existing backup
- C. Your accountant and attorney

IV. The Loan (Investment) Request
- A. Justification of the loan
- B. Details of the loan request
  - 1. Amount needed

Provides financial forecasts based on your estimates of the future and your business experience.

Provides budget guidelines, including projected cash flow analysis and income statements.

Gives a break-even analysis of your business.

Helps determine the amount and kinds of financing best for your business.

Gives banks, investors and suppliers useful information they need to make fast and accurate decisions about your business.

Forces you to think through every aspect of your business and recognize opportunities for growth and profit.

Provides financial information so that the past can be compared to the present and future.

It is not possible in this *Handbook* to present an example of a completed business plan. Exhibit 4 contains an outline listing the contents of the plan.

Remember, a business plan is a dynamic, not a static, tool. After it is prepared it must be used often. It is flexible, not rigid, and should be altered as conditions change. Most important is that the owner(s)/manager(s) prepare the report.

If you have trouble understanding how to write a plan, be quick to get help. SCORE can be of great assistance. Also, an accountant can help in preparing the financial reports. However, only you can set the objectives of the business only you can decide where you want the business to go and what you want it to be. Do it!

RECORD KEEPING

Experience has clearly demonstrated that for a person about to start a business, an adequate record keeping system will increase the chance of survival and reduce the probability of failure. Similarly, for the established business, experience has shown that a good record-keeping system increases the chances of remaining in business and of earning larger profits. How? Because accounting records can furnish the following timely information:

Amount of business done in cash and credit.

Amount of business tied up in receivables.

Amount of collections and losses from credit sales.

B. Market
   1. Who buys your product or service
   2. Who needs it
   3. Size of the market
   4. Growth potential

C. Location of business
   1. Physical features of site
   2. Whether it is leased or owned
   3. Renovations needed
   4. Description of neighborhood
   5. Zoning restrictions, if any
   6. Other businesses in the area
   7. Advantages and disadvantages of the location
   8. Whether relocation is necessary and, if so, effect on operating costs

D. Competition
   1. Names and addresses of competitors
   2. Their share of market
   3. What you have that your competitors do not
   4. Future effects of competitors
   5. Comparison of your site inside and out to competitors'

E. Management
   1. Your background and experience
   2. Experience of management employees
   3. Analysis of strength and weaknesses of management, including your own
   4. Needs for the future and plans to hire
   5. Job descriptions and training program

F. Personnel
   1. Number of employees and experience
   2. Strengths and weaknesses
   3. Skills needed for future
   4. Plans to hire and training program

G. Application and effect of loan or personal funds
   1. How much is needed
   2. What for - inventory, equipment, renovations, etc.
   3. How funds will help business
   4. What happens if funds are not available in full

H. Objectives of business and plans to achieve them

Simple to use.

Easy to understand.

Reliable.

Accurate.

Consistent.

Able to give information on a timely basis.

The following information must be recorded:

Cash receipts.

Cash disbursements (expenditures).

Sales.

Purchases.

Equipment.

Inventory.

Accounts receivable (amount customers owe).

Accounts payable (what business owes).

From the record keeping system, the owner/manager must determine the following information:

Daily

Cash sales and cash receipts.

Cash on hand.

Bank balance of business.

Monies paid out -- both cash and check.

Weekly

Accounts receivable.

These are the early warning systems, the problem indicators and the solution indicators. If there is to be only a single statement available monthly, it should be the cash flow statement, because this will show how well cash is managed. Obviously, cash in must be greater than cash out.

Before you open the door of a new business, be certain a good record-keeping system is in place. If you do not understand the need for this, it indicates you do not have enough managerial know-how to run a business.

If possible, do the record keeping yourself. If not, hire a part-time bookkeeper, use a business service or public accountant. SCORE can help you set up a system.

In any case, be sure - absolutely sure - that you understand what records are required for your business. If a system is designed by someone else, understand the system. IRS Publication 583 is helpful for the beginner.

PRICING SERVICES PROFITABLY

Successful business owners know that the greatest opportunity for success and growth comes through quality of service and customer satisfaction. However, the service must be priced properly or there will be no profit.

Many small businesses do what they consider a good volume of business, but do not make any money. Why? Because of improperly priced services or products. Some make a profit on certain services, lose money on others and do not know which is which. Remember, the right to establish price is yours - 100 percent yours.

Types of Costs

For the purposes of this section, costs are defined as

> *Fixed costs* - Costs that remain the same in any time period despite changes in business activity. These include rent, insurance, utilities, office supplies, salaries, depreciation, legal services, accounting and property taxes. These expenses are usually called overhead.
>
> *Variable costs* - Costs that usually vary in proportion with business activity. These include materials used in manufacturing, goods purchased for resale, labor and commissions. In a service business, labor may not be variable.

Calculating the Cost of a Service

A simple, easy-to-understand method of calculating the cost of a service is by basing the cost on billable hours. Because services must be provided by people, begin by determining the number of hours available for billing in a year. Then calculate the break-even point by dividing the overhead and labor charges by the billable hours and adding the cost of any materials used. Your desired profit

To determine what rate to charge, the bookkeepers divide the desired revenue ($82,440) by the number of billable hours (2,944), resulting in an hourly rate of $28.00. Profit is then calculated by subtracting total overhead and salaries from the proposed revenue ($82,440 - $70,400 = $12,040). This is the profit to be realized, assuming the billable hours figure is realistic for the first year of operation.

Example 2

DWA Repair Service employs ten repair technicians, who are paid $18,000 each. Social Security tax, unemployment tax, workers' compensation insurance, health insurance and retirement benefits cost an additional $5,400 each, for a total cost of $23,400. Because there are ten technicians, the yearly labor charge is $234,000.

DWA Repair Service's overhead expenses are listed in Table 4.

Table 4 - DWA repair service's overhead expenses

Expense	Amount per year
Salaries (including owner)	$60,000
Payroll taxes and costs	3,700
Insurance	13,000
Utilities	2,600
Rent	10,000
Telephone	1,200
Depreciation	5,000
Miscellaneous	2,500
Total	$98,000

To break even, DWA Repair must have a total revenue of $234,000 (labor) plus $98,000 (overhead) = $332,000. All of it must come from the income of the repair service based on the hourly rate charged.

The owner of the business has calculated the billable hours as follows:

Work days per year = 52 weeks x 5 days = 260 days.
Subtracting 15 vacation days, 7 sick days and
8 holidays leaves 230 work days.

Work hours = 230 work days x 8 hours = 1,840 per year
for each repair technician.

service business, the elements are materials and supplies, labor and operating expenses, planned profit and competition. (See "Pricing Services Profitably.") In a retail business, the elements of price are costs of goods sold, overhead, sales volume, planned profit and, often, competition.

Types of Costs

In the retail business, there are two types of costs: the cost of acquiring the goods, called cost of goods, and the cost of operating the business, called operating expenses.

Cost of Goods (Variable Cost)

Cost of goods is known as a variable cost or expense because it varies depending upon the amount of goods purchased for resale and the price of the goods. Cost of goods includes the price paid for goods, freight charges, import duties, handling charges and any commissions.

Operating Expenses (Fixed Cost)

Operating expenses are a fixed cost because they usually do not vary with the volume of business. Operating expenses include wages, management salaries, rent, utilities, office supplies, insurance and any other costs attributed to the operation of the business.

Planned Profit

Planned profit is whatever the owner/manager calculates the business will generate. Usually, return on owner's investment, fruits of labor, plans for expansion or relocation, return to stockholders, demand for the product and competition are considered when calculating the amount of planned profit.

Competition

In setting prices, small businesses should consider prices charged by competitors for similar or comparable items. A small business should not try to compete pricewise with large stores, discount houses or supermarkets. This type of competitor can charge less because of buying power. Pricing should be based on the quality or type of service offered, as customers will pay higher prices for merchandise to obtain the services they want.

Pricing Below Competition

Beating the competitor's price is effective only if it greatly increases sales. This strategy reduces the profit margin. Consequently, cost of goods and/or operating expenses must be reduced and inventory must be closely controlled; the product line must be limited to fast moving items; and services must be limited or eliminated.

Pricing below competitors often backfires because every cost component must be constantly monitored and adjusted. Competitors can retaliate by matching the lower prices, at which point both businesses lose.

price.

Break-Even Analysis

A break-even analysis can be used by a new or old manufacturing or retail business. It indicates the amount of revenue at which a business will neither lose nor make money. For a retail business, the break-even point is when sales equal the cost of goods plus operating expenses, or

$$S = FC+VC$$

where	S	=	sales in dollars
	FC	=	fixed costs or operating expenses
	VC	=	variable costs or cost of goods.

From a strict accounting standpoint, cost of goods cannot be determined until an inventory has been taken, because cost of goods is determined as follows:

Inventory at beginning of a period +
Purchases during the period - Inventory at end
of period = Cost of goods sold

Thus, the break-even analysis involves a variation in the break-even formula because the total cost of goods is not known. First, gross profit (also known as the gross margin or contributing margin) on sales is determined as follows:

Cost of sales - cost of goods = gross profit

The break-even point is then calculated as

$$\frac{\text{FC (operating expenses)}}{\text{GM (gross margin)}}$$

Earlier, an example of a retailer buying shoes for $25 a pair and selling them for $40 a pair was used. The gross margin on each pair of shoes sold was

Selling price	=	$40.00 or 100%
Cost of shoes	=	$25.00 or 62.5%
Gross margin	=	$15.00 or 37.5%

Note that the gross margin and cost of goods (variable unit cost) are expressed as percentages of the sales price.

Let's assume the shoe retailer has operating expenses (fixed costs) of $75,000 per year. The break-

The unit selling price or price per pair of shoes at 55 percent gross margin is determined by dividing the unit cost by the percent of variable costs.

$$\begin{aligned} VC &= 100\% - GM \\ &= 100\% - 55\% \\ &= 45\% \end{aligned}$$

$$\frac{\text{Unit cost of shoes } (\$25)}{VC\% \ (.45)} = \$55.56 \text{ or } \$56 \text{ selling price}$$

As a check

Unit selling price =	100% =	$56
- Variable cost =	45% =	$25
Gross margin =	55% =	$31

Let us determine if $150,000 of sales at a gross margin of 55 percent will provide a profit of $7,500.

Today's sales	= $150,000 or 100%
- Cost of sales	= 67,500 or 45%
Gross margin	= 82,500 or 55%
- Fixed costs	= 75,000
Profit	$7,500

If a business manager calculates the gross margin for all merchandise sold, the price structure that will generate a level of revenue to purchase goods, pay operating expenses and make a profit can be determined.

The gross margin percentage can be used as a monitor of the sales/purchasing area of the business. The gross margin calculation allows the manager to buy goods that can be sold at or higher than the desired margin. Pricing policy should be based on gross margin.

If an item of merchandise has a low sales volume, it should have as high a gross margin as possible or else it will not be profitable. If a business does a high volume of sales, it may be possible to have a pricing policy based on a lower gross margin, subject to calculation.

In review, the break-even point is the level of sales that will just cover fixed plus variable expenses. By determining the gross margin for each item of goods sold, the level of sales needed to break even can be determined as follows:

Fixed cost

Objectives of Advertising

Objectives will vary with each type of business. Usually, one or two will be of most importance to a business. Some typical objectives are to

Increase store traffic.

Acquaint customers with new products.

Promote special events, such as a clearance sale, a new location or the opening of a new business.

Change the company image.

Keep the business name and location before the public.

Inform customers of special services available, such as delivery service, alterations or credit plans.

Introduce new employees to the public.

Tie in with a supplier's national promotions.

Capitalize on the seasonal nature of a product.

Offer get-acquainted incentives.

Emphasize quality of product and services.

The most important asset of a small business is quality, and advertising is the way to let potential customers know that it is the mainstay of your business.

Unfortunately, some small businesses underestimate the value of advertising or are basically uninformed about how to budget money for advertising, how much to spend and where to advertise. A new business should be prepared to spend about 5 percent of projected gross revenue on advertising. An established business should budget 2 to 3 percent of gross revenue.

Advertising Media

Once the advertising objectives have been established and written, the next step is to select the specific media in which the advertising will appear. Media costs vary from inexpensive, such as business cards, to very expensive, such as television. The selection should be based on cost effectiveness, scheduling, trading area, customer type and frequency of message.

The types of media available are as follows:

For help in planning, producing and measuring the effectiveness of advertising, consider an advertising agency. Often the services of an agency can be obtained at low cost because agencies earn commissions paid by the media (about 15 percent) and take a percentage of the cost of the material they design (also 15 to 20 percent). Before selecting an agency, be sure the agency knows the objectives of your advertising and the size of your budget. Then have the agency describe what it can and will do for you.

Advertising is not merely an item of business expense; rather, it is an investment in building your business. Its objective is to help you sell your product or service. The copy should attract attention, develop interest, describe the product or service, convince the reader or listener and get action.

Do not advertise something you are stuck with. Advertise what your customers want and like to buy. Show the benefit of your product or service. Attempt to tell your prospective customers what is in it for them.

Be sure to include the name and address of the business in all advertisements! Finally, be honest!

MARKETING

Business success ultimately comes from satisfying market needs. Therefore, it is essential that people in small business understand and develop marketing programs for their products and services. What is meant by market and what is marketing?

> *Market* - A body of existing or potential buyers for specific goods or services. It is the demand for a product.
>
> *Marketing* - The total of activities involved in the transfer of goods from the producer or seller to the consumer or buyer. Marketing activities include buying, storing, selling, advertising, pricing and promoting products as well as managing the business.

A business will not succeed just because the owner wants it to. There must be a market for the merchandise or service being offered or there is no chance of success.

Marketing Before Opening

Before opening a business, the following information must be obtained:

> Is the product or service to be offered one that people want? How do you know this?
>
> How many people want it?
>
> Who are the potential customers?

How they like the business.

Whether they would recommend the store, product or service.

Why they came to the business.

The products they would like that the business does not have.

Listed below are the logical steps in more formal market research:

Define the problem or area to be investigated.

Assess all available information.

Assess additional information if required by

Reviewing internal files and records.
Interviewing employees.
Interviewing customers and suppliers.

Organize and interpret information.

Make decisions.

Observe and evaluate results of the decision.

A good part of marketing research can be done with readily available information. Trade associations constantly report on and analyze pertinent marketing information. If your type of business has a trade association, the membership fee may be money well spent.

Market Strategy

Market strategy involves identifying customer groups that small businesses can serve better than larger competitors can, and tailoring products, services and promotional efforts to that particular market segment.

Ideally, this strategy should address the customers whose needs are not currently being met in the marketplace and whose needs are great enough to provide a profit. Small business should analyze its market and capabilities, and focus on that part of the market it can serve best.

Target Marketing

Because small business owners may have limited funds to spend on marketing activities, they should consider restricting their efforts to one or two key market segments by

Geographic targeting - Specializing in serving the needs of customers in a particular

The third business type is one in which the business comes to the customer, such as plumbers, electricians and landscapers. For this type of business, location is not of primary concern. The only caution that may apply is compliance with zoning laws regarding material storage and truck or other vehicle parking.

Three factors are involved in choosing a business location: selection of a city, town or municipality; choice of an area within a city or town; and choice of a specific site.

Selecting a City or Town

When selecting a city or town for your business, consider the following:

Size of the trading area within the city or town.

Population and population trends.

Total purchasing power and distribution of the locale.

Total retail potential within the city or town.

Number and size of competitors.

Aggressiveness of competitors.

Selecting an Area Within a City or Town

Once a city or town has been chosen, consider the following in selecting an area:

Power of the shopping district to attract customers.

Number and quality of competitive stores.

Availability of access routes to the store.

Nature of zoning regulations.

General appearance of the area.

Expansion and rebuilding of the area.

Selecting a Specific Site

In selecting a specific site for your business, consider the following:

Adequacy of parking.

away. Excellent products and services can be negated by a poor location.

INSURANCE

Going into business is a risk. To succeed in business, the many potential risks must be managed, i.e., reduced and controlled. One of the methods of controlling risks is with insurance.

For the small firm the most common risks are

- Business fraud and theft.
- Fire.
- Legal liability - injury to customers or employees, defective merchandise, etc.
- Business interruptions.
- Death or loss of key personnel.
- Death or loss of owner or partner.
- Violent weather -- hurricanes, floods, etc.
- Damage to or loss of vehicles.

If a business has even one employee, workers' compensation insurance is mandatory. In several states, if a business has five or more employees, health insurance is required. When applying for a loan, banks may require certain types of insurance, depending on the nature of the business and the type of loan.

Each business will have its own particular insurance needs. At business start-up, funds to purchase insurance may be limited. Nevertheless, insurance must be investigated and that which is essential must be purchased. For example, one can imagine a tree surgeon must carry liability insurance when felling a tree.

The general categories of insurance are

- Property.
- Automobile and vehicular.
- General liability.
- Product liability.

Help maintain good employee relations by eliminating uncertainties and hazards.

If the business is a partnership, provide a prearranged plan for the orderly and equitable dissolution of the partnership and the opportunity for surviving partners to buy out the heirs.

Provide funds to replace a key employee or train another if the key employee leaves, becomes ill or dies. This is called "Key Employee" insurance.

Insurance is one area of your business where professional help is strongly recommended to obtain proper coverage at the best price. Help is readily available from local insurance agents and brokers, the best choice being one who writes insurance for other small businesses.

One way to determine which insurance agent is best for you is to ask other small business owners whom they use and what kind of service they receive. Also, your banker, accountant or attorney may be able to recommend an agent or broker.

RETAILING TIPS

Image

Every retail and retail-service business has an image, which can be controlled by the operator. People's impression of a store, office, showroom, beauty shop is based initially on the appearance of the premises, both inside and out, and then by the type of merchandise and services offered. Therefore, each business operator must decide what image he or she wants and then take steps to develop it.

Creating the proper image and environment is particularly important to certain types of businesses and not as critical to others. For example, a junk yard may not be very attractive; but then its customers do not expect it to be. However, most business should create an atmosphere that corresponds to their product line or service. For example, people do not expect carpet in hardware stores; but they do expect clean, uncluttered aisles and easily accessed displays. In a store selling expensive clothing, people will expect carpeting and papered walls. There is no doubt that carpet leaves a different impression than vinyl tile or linoleum and costs more to install and maintain. In this case, the extra cost may be worth it.

Window Displays

A neat, eye-catching window display is an effective way to stop pedestrian traffic and entice people to enter the premises. It takes only two to four seconds to pass a six- or eight-foot window. Therefore the display not only has to be eye catching, but also must be well lighted day and night. (Good daytime lighting avoids shadows that dull a display.)

Change window displays periodically and keep windows clean. Window displays used for

Markdowns on certain items reduce profit margins but usually are an excellent way to sell unsalable or end-of-season goods. Markdowns, if properly done, clear out merchandise quickly, thereby increasing cash flow and reducing inventory.

Loss Leaders

Loss leaders are items sold at a lower price to attract people who will buy other regularly priced items or become regular customers. Loss leaders should have a lower wholesale price, look more expensive, sell at other stores at a higher price and be readily available from the supplier.

Loss leaders are more effective as a strategy when they are associated with another item at regular price and both items are sold together. An example is a shirt and tie, with the tie being the loss leader.

Sometimes loss leaders do not work. With experience, the successful leader will be selected and often can be used over and over again.

Pricing Policy

Pricing may depend on the following:

Location of the business.

Physical appearance of the premises.

Purchase of manufacturer's close outs.

Volume of sales.

Pricing must take into account fixed or operating costs, owner and manager salaries, variable costs (cost of goods) and profit. Buying practices affect the cost of goods. Attention must be given to quality as well as the quantity of goods purchased. Utilities, rent, services, salaries, employee benefits, etc., affect fixed costs. Unless prices are changed accordingly, increases in either variable or fixed costs will decrease profit.

Often, competition dictates pricing. Therefore, competitors' pricing must be constantly monitored. As pointed out in the section on pricing products, a pricing policy must be examined and reviewed frequently to be certain the desired profit level is maintained. Profit and loss or income statements are most helpful.

Leases

Landlords can be difficult; remember they are trying to make a profit, too. Cordial relationships make it easier to get improvements to the premises and to negotiate late rent payments.

Most important, get to know the credit manager of your supplier. If you need extra time to pay, extra credit or special terms, this is the person to contact. The credit manager can be a valuable ally to your business.

For special promotions, ask manufacturers and suppliers if they have a program to contribute to advertising costs. The way to learn about all the services a supplier offers is to spend time with the supplier and ask questions.

Be sure you know the availability of every item purchased and how long it will take to get to your store. This will help you place orders and keep you from running out of an item.

EMPLOYEES AND INDEPENDENT CONTRACTORS

Classes of Employees

For federal and state tax purposes, small business owners and operators must know who is an employee and who is not, and what their classification is. Employees may be classified as common law or statutory.

Common-Law Employees

Every individual who performs services that are subject to the will and control of an employer as to both what is to be done and how it is to be done is a common-law employee. Two of the usual characteristics of an employer-employee relationship are that the employer has the right to fire an employee and the employer supplies the tools and the place to work.

Employers must withhold federal income tax, Social Security tax and, where required, state and local income tax from common-law employees. Also, employers must pay their share of Social Security and federal and state unemployment tax for such employees.

Statutory Employees

In many states, a statutory employee is one who works for an employer in any one of the following four categories:

1. A driver who distributes meat, vegetables, fruit, bakery products or beverages (other than milk), or who picks up and delivers laundry or dry cleaning, if the driver is your agent or is paid on commission.

2. A full-time insurance salesperson.

3. An individual who works at home on materials or goods that you supply and that must be returned to you or to a person you name. You also furnish the specifications for the work to be done.

independent contractors, nor does the employer have to pay the unemployment taxes or workers' compensation insurance.

Because an employer who has hired an independent contractor must file form 1099-MISC with the Internal Revenue Service and, where applicable, state and local government, the independent contractor must provide the employer with an employee identification or a Social Security number. If the independent contractor fails to provide this number, the employer may have to withhold 20 percent of the amount paid as income tax.

Casual Labor

Many small businesses classify certain types of labor as casual labor. In these cases, the employer does not withhold income taxes or Social Security tax, does not pay employment taxes and usually does not cover the worker with any type of insurance.

If one asks either the IRS or a state department of revenue for a definition of casual labor none will be forthcoming. This means that the IRS and other agencies do not recognize the term and will not define it. Federal and state agencies reserve the right to judge each case as to whether or not a worker is a casual employee.

The issue at hand is whether or not an employer must withhold income and Social Security tax, pay unemployment taxes and provide workers' compensation insurance. In some cases, the IRS and other taxing agencies may recognize intermittent and temporary labor, such as in the following cases.

Case 1

Katie's Catering has two full-time employees. Katie contracts for a job for which she needs extra help, so she hires a person to work for one day for $50 with no withholdings of any kind. She does not intend to hire this person on a regular basis.

Case 2

Conwald Construction accepts a contract to frame two houses and agrees to finish both houses within one month. Conwald does not have enough regular full-time employees to accomplish this, so he hires two extra carpenters at an agreed-upon wage of $300 per week for three weeks. At the end of the job, Conwald pays each carpenter $900, but does not withhold taxes, etc. However, because the wages were over $600 to each person, Conwald must obtain the Social Security number of each carpenter and, at the end of the year, submit a 1099-MISC to the IRS, appropriate local agencies and to the carpenters.

Case 3

Russ's Restaurant has occasional need for an extra bartender during July and August. He hires a person to work one night a week for eight weeks at $45 per night, with no withholding. The total wages paid are $360. In this case, Russ does not report these wages because the amount is less than $600.

expertise, that may be another matter.

A prerequisite to hiring any worker is a well-written, thoroughly thought-out job description, describing the duties and responsibilities of the job. Such a description makes it easier for the employee and supervisor to work together.

Interviewing

An interview is a two-way communication, during which the participants find out about each other and assess competence and compatibility. The interviewer must guard against invading the legal right to privacy of the applicant, both on the application form and in direct questioning.

The primary concerns of the interview are the job description, working conditions, standards of performance and the applicant's ability to meet or exceed these standards. All these matters must be clearly understood and agreed upon before a final decision to hire is made. References must be checked, preferably by telephone.

Wages and Working Conditions

Wages and working conditions are controlled to some degree by labor laws and, to a greater extent, by local practice. The National Bureau of Labor Statistics can provide surveys of conditions in local markets.

Usually, it is wise to set wages at the midpoint of current practice to allow for incentive and future growth. Employee benefits will add from 20 to 40 percent to the cost of the payroll. Careful thought must be given to benefits when planning and budgeting. For businesses experiencing peaks and valleys in work flow, thought should be given to the use of temporary workers and agencies.

Training

An employee may be considered on probation for an agreed upon length of time -- usually three months. During this time, attention must be given to integrating the employee into the work force and bringing the employee's performance up to standard. This is best accomplished by explaining and demonstrating the task, having the employee perform the task and then giving constructive correction and reinforcement. Time spent in proper training will more than pay for itself in weeding out employees who lack the ability to perform or fit in. Training fosters the success and high performance of those retained.

Supervision

Both the supervisor and the employee have an interest in the successful performance and stability of the work force. The essence of good employee relations is to treat all equally, and to be fair and consistent in maintaining discipline. Be factual and not subjective. Always let the employee know what is expected and whether or not those expectations have been reached. Both correction and recognition should be given regularly to achieve a healthy and productive work force.

form letters, printing mailing labels, etc.

Keep transaction records, such as cash receipts, receivables ledger and a general ledger.

Prepare statements and reports such as cash flow sheets, income statements, balance sheets and inventory status reports.

Areas a Computer Can Improve

Accounts receivable.

Accounts payable.

Sales records.

Billing.

Order entry.

Inventory records.

Payroll.

Tax reporting.

Mass mailings.

Projections.

File management.

What a Computer Cannot Do

Correct errors in an existing manual system.

Save money by eliminating employees.

Make business judgments or create logic.

Solve poorly defined problems.

Define or describe jobs that should be done.

Generate information that is not in the system.

indicates that the computer applications most beneficial to a small business are accounts payable, order entry, accounts receivable, inventory control and general ledger.

Getting a computer into operation initially requires the full and total involvement of the owner/manager, which translates into many extra and sometimes frustrating hours. Meanwhile, the regular business functions must be continued. If an employee is to operate the computer, the employee will also have to devote extra hours, at the expense of the owner.

Computers do not save money by eliminating employees. Rather, computers facilitate and complement employees' work by performing certain functions rapidly and efficiently. This may be of great advantage in effecting other savings.

If the business owner/manager has his fingers on the pulse of his business, a computer may not be needed. In any event, the cost, efficiency and adequacy of a manual system should be evaluated before you consider buying a computer.

FRANCHISES

Franchising has a number of appealing features for prospective business owners. Primarily, the risks of opening a business are reduced because of easy access to an established product and a proven method of marketing.

Franchising has existed in one form or another for over a century; in recent years enormous growth has occurred in the number of franchises. Industries relying on franchised business to distribute their products and services touch every aspect of life, from automobile sales and real estate to fast foods and tax preparation.

As a matter of fact, franchises have the highest success rate of any type of business start-up, which adds to their appeal. However, buying a franchise does not in any way ensure instant success; unless you are prepared for total commitment of time, energy and financial resources, it is not for you.

Definition

A franchise is a legal and commercial relationship between the owner of a trademark, service mark, trade name or advertising symbol and an individual or group seeking the right to use that identification in a business. The franchise governs the method for conducting the business between the two parties.

In its simplest form, a franchisor owns the right to a name or trademark and sells that right to a franchisee. This is known as *product/trade name franchising.* In the more complex form, *business format franchising, a* broader, ongoing relationship exists between the parties. The franchisor provides a full range of services, including site selection, training, product supply, marketing plans and sometimes financing. Generally, a franchisee sells goods or services supplied by the franchisor or sells goods or services that meet the franchisor's quality standards.

A good franchisor usually encourages prospective franchisees to visit and talk to other owners of the franchise. This certainly should be done!

Other Considerations

An attorney should assist the prospective franchisee to evaluate the franchise package. An accountant may be needed to determine the full costs of purchasing and operating the business, as well as the potential profit to the franchisee.

Before purchasing a franchise, carefully consider the level of independence you will maintain, how comprehensive the operating controls are, and the full costs of purchasing the franchise. Also, be sure to ask about the terms and conditions for reselling your franchise.

Although the success rate of franchises is high, very independent people with their own concepts of operating a business may not be the type to open a franchise.

MANUFACTURING COST ACCOUNTING

Cost accounting, in a broad sense, means accumulating all the costs associated with an activity (manufacturing, retailing, providing a service, etc.) and organizing them in a meaningful way to (1) satisfy financial reporting requirements and (2) achieve understanding of the costs of the activity for control and optimization purposes.

There is a distinction between general accounting and cost accounting. Although costs are of primary concern in both, general accounting is concerned more with the total costs of a business. These costs are usually classified into well-established summary level accounts, such as cost of goods sold, selling expenses, administrative expenses, advertising and research. Cost accounting details costs of individual products by the types of costs (raw material, direct labor, etc.) and by the departments (cost centers) within each of the business functions (manufacturing, selling, administration, etc.). Cost accounting is used to

> Control business operations by detailing the important costs of the business, permitting analysis of these costs and indicating where corrective action is required if costs are not meeting expectations (budgets, standards, etc.).
>
> Optimize business performance by using cost details, along with sales revenue details (sales price received by product, customer, territory, etc.) to identify the most profitable areas of the business for further development, as well as to ferret out marginally profitable or unprofitable operations for elimination.
>
> Satisfy financial reporting requirements, particularly in the valuation of inventories in manufacturing businesses.

Although cost accounting is mainly used for manufacturing businesses, it is equally effective in that lot.

Continuous process manufacturing (such as many chemical operations) *is* a continuing manufacturing operation where costs are collected over time (such as a month) and quantities of materials consumed or produced are measured through inventory changes.

Typical manufacturing costs and their general classification are listed in Table 6.

Table 6 - Typical manufacturing costs and their classification

Cost element	Direct	Indirect	Variable	Fixed
	Classification			
Raw materials	X		X	
Labor	X	X	X	X
Salaries	X	X		X
Supplies	X	X	X	X
Payroll taxes	X	X	X	X
Medical insurance	X	X		X
Heat, light, power	X	X	X	X
Telephone		X		X
Rent	X	X		X
Insurance, property taxes		X		X
Depreciation		X		X
Other				

Manufacturing cost accounting is particularly effective when it includes a *budgeting/standard cost system*. A standard cost system develops a projected unit cost, achievable under controlled conditions, for each product. This unit cost is identified as the standard cost, and includes all the raw materials, labor and other costs incurred in producing the product plus an allocation of the support costs. A sample standard cost (summary) could be as follows:

Direct-variable	$2.00 per unit
Direct-fixed	1.00 per unit
Indirect-fixed	1.25 per unit
Total	$4.25 per unit

The standard cost originates from the manufacturing budget. This budget projects the production requirements (from sales and inventory projections), the costs of each of the departments within the plant, the costs of raw materials, the raw material and labor requirements for each product, the production rates and other considerations depending on the particular manufacturing operations.

A sample budget, simplified for illustration purposes, follows in Table 7.

Table 7 - Sample manufacturing budget

ZYX Company
Annual Budget, by Quarter

	1st qtr	2nd qtr	3rd qtr	4th qtr	Year
Production (units)	3,000	4,000	2,000	1,000	10,000
Raw materials ($)	18,000	24,000	12,000	6,000	60,000
Production department budget ($)					
Labor	180,000	240,000	120,000	60,000	600,000
Salaries	7,500	7,500	7,500	7,500	30,000
Rent	3,750	3,750	3,750	3,750	15,000
Utilities	11,000	13,000	9,000	7,000	40,000
Maintenance	12,500	12,500	12,500	12,500	50,000
Total	214,750	276,750	152,750	90,750	735,000
Administration department budget ($)					
Salaries	25,000	25,000	25,000	25,000	100,000
Rent	3,000	3,000	3,000	3,000	12,000
Utilities	750	750	750	750	3,000
Depreciation/Insur.	12,500	12,500	12,500	12,500	50,000
Total	41,250	41,250	41,250	41,250	165,000
*Total mfg costs	274,000	342,000	206,000	138,000	960,000

*Raw materials + production and administration department budgets.

A budget broken down by periods is extremely important in planning raw material purchases, arranging to have labor available during seasonally busy periods and particularly for ensuring that cash is available to fund the manufacturing operations. It is also essential to control operations during the course of the year. As the year progresses, actual costs are compared to budgeted costs and the variances analyzed. Table 9 shows the first quarter manufacturing cost (or variance) report for the ZYX Company. The manufacturing budget is adjusted for actual production volume. This permits a valid comparison of actual costs with allowable costs based on actual production volume.

The above first quarter report for the ZYX Company indicates that the plant exceeded allowable costs by $20,950. Higher volumes than budget would result in higher actual costs compared to budget. However, it is important to compare actual costs to allowable costs (budget adjusted for actual volume) to make a meaningful comparison and analysis. In this case, the analysis revealed that the unfavorable variance of $20,950 was due mainly to a surge in orders requiring considerable overtime for direct labor. This resulted in a substantial unfavorable labor variance, which could have been avoided by moving more quickly to hire additional labor to handle the increased orders. The variance report, with analysis, provides a much clearer understanding of costs so that actions can be taken when indicated.

Inventory Record Keeping

Inventory record keeping establishes and maintains information on current inventory, the additions and withdrawals to inventory and inventory balances at the end of specified periods (week, month, etc.). These records identify the products/materials, the quantities and the value (cost) of these products/materials. A simple inventory record could look like the one shown in Table 10.

Table 10 - Sample inventory record

Product code: 1020
Product description: 1 quart bottle, Hi Temp Oil

Period	Inventory activity			
Month: May	Beginning	Sales	Production	End
Quantity (units)	600	(200)	300	700
Value/cost ($)	300	(100)	150	350

The value is the cost of the product. This would be what a retailer paid for the product or what a manufacturer paid for materials plus labor and other charges applied in converting the materials into the finished product. In Table 10, the cost of goods sold would be $100 for this product for the month of May.

There are two different methods used in inventory record keeping: perpetual and periodic.

Perpetual Inventory

The perpetual inventory method starts with a physical inventory (actual count) and then adjusts this inventory for additions and withdrawals. The inventory at the end of the period is calculated by subtracting the number of units sold from the total of the beginning inventory plus the additional units produced. An example is furnished in Table 11.

Table 11 - Sample perpetual inventory

Activity	Value in units
Beginning inventory	100
Sales	(75)
Production	95
Ending inventory (calculated)	120

The perpetual inventory method is used when reliable sales and production information is readily available and the frequent taking of physical inventories would be burdensome. However, physical inventories must be periodically taken (e.g., quarterly or annually) to check the calculated define the role inventories will play in achieving the business objectives.

Inventory control consists of the following:

Setting objectives for inventory: the type, quantity, cost and order/production point (what quantity will initiate action for resupply) of products/materials.

Recording and reporting actual results (done by the inventory keeping system).

Comparing actual results with objectives and analyzing the differences.

Taking action to correct problems or improve business performance.

Inventory supports the sales activity. This means having what the customer is willing to buy, when he or she needs it, at a price that provides an acceptable profit to the business.

Inventory control is integrated with systems that track sales, production and purchasing activities. The following is a simple example.

The BAC Company plans to produce and sell three products: X, Y and Z as detailed in Table 14.

Table 14 - Proposed annual sales and production rates for BAC Company

Product	Annual sales (units)	Production rate (units/day)
X	26,000	200
Y	52,000	300
Z	13,000	100

The business operates five days per week, 52 weeks per year. The minimum economic production run is two weeks. It is planned to have a minimum inventory equivalent to four weeks of the planned sales rate to ensure having enough product for customer needs. The maximum inventory is to be eight weeks of the planned sales rate to limit the investment. The minimum and maximum inventories, based on these plan assumptions, would be as listed in Table 15.

Table 15 - Minimum and maximuminventory for BAC Company

Product	Daily sales rate (units/day)	Minimum inventory (units)	Maximum inventory (units)

Again, values (costs) could be used in calculating inventory turnover similar to that done above.

Although the time period of a year is used as the basis for calculating inventory turnover in most cases, a seasonal business (such as a store in a summer resort) would use the season as the basis. In this case, the business objective is to turn the inventory over as many times as possible and have little or no inventory by the end of the season.

Actual sales activity (sales rate, product preferences, selling prices) must be closely monitored with inventory (products, quantities, costs, resupply limits) to be sure that the inventory control system is properly supporting the sales activity.

Another important objective of inventory control is to keep the financial investment in inventories just sufficient to support the business. Inventory building converts cash into products that may or may not sell or may sell at a price less than cost. Inventories consume cash, increase the investment in the business and can bankrupt the business if not properly controlled.

Inventory Strategies

Every business competes within an industry and each industry has a life cycle. The strategies employed by the business depend on where in the life cycle the industry is. The management of inventories is influenced by this life cycle.

Generally, there are four stages in the life cycle of an industry. These are as follows:

> *Development* - Uniquely new products are being developed and market tested. Products must be available for market testing. There is little concern about inventory investment, other than to be sure products are available for market testing and development.
>
> *Growth* - The product has been demonstrated to have significant market potential and the business strives to gain a major market share. Investment in inventory is heavy to ensure product availability to gain significant market share.
>
> *Maturity* - Growth has leveled off Inventories are very closely controlled to keep investment in them just sufficient to maintain market share.
>
> *Aging* - A period of retrenchment as competitive industries take away or eliminate markets. Inventories decline as unprofitable and marginally profitable segments of the business are weeded out.

The proper control of inventories is essential to the success of any business in which investment in inventories is significant. Awareness of the competition and the state of new product development is just as important as a finely honed record-keeping system. While the record-keeping system is important, how it is applied will determine the success of the business.

Small Business Development Centers (SBDCs), sponsored by the SBA in partnership with state and local governments, the educational community and the private sector. They provide assistance, counseling and training to prospective and existing business people.

Small Business Institutes (SBIs), organized through SBA on more than 500 college campuses nationwide. The institutes provide counseling by students and faculty to small business clients.

For more information about SBA business development programs and services call the SBA Small Business Answer Desk at 1-800-U-ASK-SBA (827-5722).

Other U.S. Government Resources

Many publications on business management and other related topics are available from the Government Printing Office (GPO). GPO bookstores are located in 24 major cities and are listed in the Yellow Pages under the bookstore heading. You can request a Subject Bibliography by writing to Government Printing Office, Superintendent of Documents, Washington, DC 20402-9328.

Many federal agencies offer publications of interest to small businesses. There is a nominal fee for some, but most are free. Below is a selected list of government agencies that provide publications and other services targeted to small businesses. To get their publications, contact the regional offices listed in the telephone directory or write to the addresses below:

Consumer Information Center (CIC)
P.O. Box 100
Pueblo, CO 81002
The CIC offers a consumer information catalog of federal publications.

Consumer Product Safety Commission (CPSC)
Publications Request
Washington, DC 20207
The CPSC offers guidelines for product safety requirements.

U.S. Department of Agriculture (USDA)
12th Street and Independence Avenue, SW
Washington, DC 20250
The USDA offers publications on selling to the USDA. Publications and programs on entrepreneurship are also available through county extension offices nationwide.

U.S. Department of Commerce (DOC)
Office of Business Liaison
14th Street and Constitution Avenue, NW
Room 5898C
Washington, DC 20230
DOC's Business Assistance Center provides listings of business opportunities available in the federal

A librarian can help you locate the specific information you need in reference books. Most libraries have a variety of directories, indexes and encyclopedias that cover many business topics. They also have other resources, such as

Trade association information
Ask the librarian to show you a directory of trade associations. Associations provide a valuable network of resources to their members through publications and services such as newsletters, conferences and seminars.

Books -- Many guidebooks, textbooks and manuals on small business are published annually. To find the names of books not in your local library check Books In Print, a directory of books currently available from publishers.

Magazine and newspaper articles -- Business and professional magazines provide information that is more current than that found in books and textbooks. There are a number of indexes to help you find specific articles in periodicals.

In addition to books and magazines, many libraries offer free workshops, lend skill-building tapes and have catalogues and brochures describing continuing education opportunities.