



Middletown Small Business Development Center



Fundamentals of Planning Your Business

Paul M. Hughes
Middlesex County Chamber of Commerce
393 Main Street, Middletown, CT 06457
860 - 347-6924 x228
phughes@middlesexchamber.com

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<p>Tax, reporting and regulatory requirements are subject to change. Such information is presented here as example. Always secure current information from any authority having jurisdiction.</p>

Are you Entrepreneur Material?

Do you have what it takes?

An entrepreneur is one who organizes, operates and assumes the risk of a business venture. That takes some special skills, resources and traits that not everybody has. The entrepreneur is no better than those who are better off working for someone else, just different. To be a successful entrepreneur, you must have:

- **Vision.** This is the first thing you need and you cannot proceed without it. The type of vision needed is not a dream, but a realistic idea of what your business is going to be. This is not just the product or service, but a complete, integrated system for doing business. If you want your business to last, you have to pay attention to the future – where you will spend the rest of your life. You must always have a goal and a plan to get there!
- **Time.** Running your business will take much more of your time than working for someone else, especially at the beginning. Are you prepared to work an eight to ten hour day or more *and then* do the paperwork – accounting, billing and record keeping? If you often found yourself taking time from your job to do other things, you may not have the time. If you have a list of activities – like sports, classes, crafts or social events – that you are not willing to give up for your business, than you definitely don't have the time.
- **Ability to Prioritize.** The largest corporations do not have unlimited resources, neither will you. No matter how much time and other resources you put into your business, it will never be enough to accomplish everything you want to. You will have to be able to set priorities for the best long-term outcome for the business. The choices will not be clear and you may not know if you made the right choices for months, if ever. There is little instant gratification in owning a business.
- **Ability to Multi-Task.** The business owner has to handle operations, financial, sales, staff, purchasing, legal and more – all at the same time! Interruptions are more common than not and most days don't go as planned. Your business may need you at any time. You may have an employee no-show on your day off. If you have a store or office, it could

have a robbery or fire in the middle of the night. Your customers will call at their convenience, not yours. If you can't tolerate interruptions, if you are not willing to let your business schedule you as opposed to you trying to schedule your business, than you may not be flexible enough.

- **Ability to partner.** Running a business goes beyond just working with people. You will have highly important relationships with your customers, suppliers, employees, contractors and the government agencies that regulate or tax you. If any of these relationships is adversarial, your business will suffer. In many ways you will not be your own boss, but have lots of bosses.
- **Negotiating Skills.** Americans get so little experience in negotiation until they go into business, then they need to negotiate almost every day. The goal in negotiation is not to come out ahead of the other side but to find something to offer, to trade that is of value for the other side.
- **Discipline.** There will be a lot of temptation to divert your attention and resources from your business. As a matter of fact, your employees will probably encourage you to goof off because it makes work easier for them. Do you have the discipline to resist temptation and focus on your business? That means setting goals and sticking with them until they are accomplished or you make a sound business decision to change them.
- **Responsibility.** You will also be responsible for anything the business does, even if your employees or agents do it. You will be responsible for any reporting requirements. There will be no boss to handle problems; you are the boss. You will have to handle the customer with a complaint, the fire marshal with a demand and the letter from the Internal Revenue Service – maybe on the same day! There is no place to hide. Are you willing to be “where the buck stops?”
- **Patience.** As time goes on, you will find yourself doing much the same thing and handling the same problems over and over. Employee related problems are especially repetitive. Your business will be no less tedious than working for someone else. If you want to go into business for yourself for adventure, think again. Most of the excitement is going to come in the form of the problems we brought up in the previous paragraph.
- **Willingness to take risk.** As you create your business, and as long as you operate it, you will be continually faced with decisions that involve risk. Worse, most of the time you will have to make those decisions with incomplete facts and uncertain outcomes. You have to be tolerant of risk,

but not a fool. A fool shoots from the hip, ignoring the facts that are available. Honestly, are you the type of person who is willing to make such decisions?

In addition to those traits and resources, the entrepreneur must have three distinct skill sets:

- **Industry-specific skills.** It may be obvious that you have to know something about a business before you go into it, but how much is enough? You need to know enough to compete in the marketplace. It is very difficult to assess how ready you are for that. Study and training will go a long way, but there is no substitute for experience – especially to find out if you actually *like* the business.
- **Marketing skills.** No matter what you do, you are going to have to sell. You will have to step outside of your business and look at it from your customer's perspective to create effective marketing plans. This is very difficult for the business owner who is so close to the core of his or her business.
- **Business Systems skills.** If you are going to have employees, you must have Human Resources systems. No matter what your business, you must have recordkeeping and accounting systems. These systems are the foundation for organization and management.

Ask yourself

- What are specific skills, knowledge and experience do I have? Is it enough to handle this business?
- What are my weaknesses and what can I do to overcome them?
- Am I comfortable with math and finance? Working with all kinds of people? Selling?
- Why am I considering this?
- Is my family going to support this endeavor? Do they realistically understand the sacrifices we may have to make?
- Have I been successful planning and managing things without supervision?
- Can I ask for help or take complaints and criticism without becoming defensive or offended?

- Am I willing to spend the time, give up vacations, holidays and personal time to get this going?
- Do I have the courage and conviction to give up dependable income, relative security and peace of mind and become entirely self-reliant?
- And most important: **What is my plan to open and grow this business?**

Why Businesses Fail

About two of three new small businesses fail in their first year and only one in six are still in business five years later. How it happens is almost always the same, the business simply runs out of money. The reasons why that happens, in order of frequency, high to low, are:

1. Lack of management experience or capability;
2. Insufficient starting (working) capital;
3. Wrong location;
4. Poor or no systems, policy and procedure;
5. Excessive debt at start-up;
6. Poor supply chain/credit arrangements;
7. Personal use of business funds;
8. Unexpected customer behavior;
9. Competition;
10. Overestimated sales/underestimated expenses.

The Entrepreneurial Lifestyle

Is it worth it?

If you are asking yourself that question after reading the previous chapters, then consider what you gain in return for all that work, discipline, responsibility and patience. Going into business for yourself will change your life in a profound way. Nothing will be quite the same.

- Although you cannot just do as you please, you will be in control of your destiny as never before. That can be very fulfilling.

- Earning potential is far less limited. Hard work has its reward and all of yours will directly benefit you.
- You can be creative in the business solutions you execute and take pride when they work.
- Because of your direct contact with customers, suppliers, employees and others, your identity and that of your business will merge. Your business will become a passion and you will not be able to imagine yourself without it. Others will identify you, and probably your family, with that business.
- If you become successful managing your business, you will eventually have more freedom than you can imagine – but you will probably chose to spend time with the business you love.
- You can build something substantial for your children to take over or execute a “windfall” exit.

Although owning your own business is not easy, it is not impossible either. One in six Americans owns a business! You will not be alone and you will have the support of the business community you will be part of, and economic development agencies, like MSBDC.

As an exercise, list the advantages of going into business specific to your personal situation. Make another list of the risks and sacrifices specific to you going into business. Be honest; this is only for you. Study these before you commit to starting a business.

Choosing a Business

Do what you love doing and stick with it.

Most MSBDC clients don't need this chapter. They are either already in business or have a pretty good idea of what business they want to open when we first meet them.

There are a few, however, who have evaluated all of the sacrifices and rewards, decided they want to be entrepreneurs, but haven't decided on what business to be in. Many of those will be very successful once they make that decision.

This is one decision MSBDC cannot help you with, because it has everything to do with you on a very personal level. It must be based on a thorough self-examination that only you can do. We suggest you start by making a list of everything you enjoy doing or think you would. Include

everything without thinking about it – crafts, hobbies and academic pursuits as well as jobs.

Next, place a star on those items on the list you, and especially others, consider you skilled or experienced at. Rank those in order of your preference. Now you have an area to focus your research on:

- Basic research – books, trade magazines, websites;
- Observation of operating businesses (be especially sensitive to the working dynamic);
- Hands-on – working, interning, partnering (remember there is no substitute for experience).

Sometimes people decide the best business for them to operate categorically. They may know they want to be in sales, but selling what? Or they want to get into computers, but doing exactly what? The same exercise works to narrowing down what to sell or what niche of the computer business to research.

Too Many Choices

The most common problem for those choosing a business is too many choices. The client has the entrepreneurial skills necessary but can't choose among several possible businesses. The fear of not picking the best makes the client hesitant to pick at all. Some people just hate to exclude any opportunity from the list, even though some directly conflict with others.

The way to sort this out is to outline a vision and very basic business plan for each choice. Don't let easier start up or immediate opportunity make the decision. Think long term: What would your life be like in five, ten or fifteen years for each alternative?

Once You Decide on a Business

No matter if you knew what business you wanted to be in from the start or you decided among many possibilities, once you know what business you want to go into, your research is just beginning. The more you know about business, the more likely you will succeed and the more successfully you can compete.

Even if you worked in the industry for years, you need to do some research to fill the gaps. It takes a broader skill set to own and manage a business than to work in one.

Areas of focus are:

- Industry Research – What are the trends, the opportunities and threats? Where do the insiders think it is going?
- Market research – Which are the customers you plan to serve and how can you get your message to them. How can you differentiate your business from the competition?
- Location Research – Where will you operate your business and how do customers find you? What are the zoning and use issues?
- Resource Research – Where will you get product, supplies, employees, utilities and equipment?

It is important that you keep the data and materials you collect in your research organized. You will be using it and building on it as you progress towards opening and operating your business. The last section of this booklet gives you lots of research sources to start with.

Exit Strategy

It may seem strange to consider how to get out of a business even before you get into it, but eventually, everyone has to leave his or her business. If you don't have a plan for an exit, you could be trapped working in a business that can't run without you, is your sole source of income, with nothing set aside for retirement. Worse, after working your business for decades, you may not be qualified to do anything else.

Whether you want to sell the business, pass it on to family members or simply wind it down, you must have a plan to not only get that done, but also provide for yourself afterwards. Think about it before it is too late and plan your exit strategy. Your choice of exit will affect many of the decisions you will make even before you start the business, including...

Choosing a Legal Form

You have a business in mind and want to take the big step. Before you develop your plan, you need to pick a legal form for your business. They fall into two categories: Owner Entity and Separate Entity. Sole proprietorship and partnership are owner entities, where the owners and the business are legally the same. Corporation and Limited Liability Company (LLC) are

separate legal entities from the owners and have much the same rights and duties under the law as a living person.

Sometimes external requirements will determine what form your business takes. Your customers or suppliers may force you to adopt a business form as a condition of doing business with you. This is very rare though and usually the choice is yours.

You make that choice based on several characteristics that differentiate the forms of business, based on what is most advantageous for you and your business. Those characteristics include organizational and reporting requirements, treatment of earnings and taxes, and liability. Factors such as license and other regulatory requirements affect all forms of business the same and are not a factor in choosing a business form.

Sole Proprietorship

This is the simplest form of business – you are the business entity. A sole proprietorship may have employees, but it may not have co-owners, so raising equity capital is impractical (you can't sell "a piece of the action"). Financing is pretty much restricted to debt.

Organizational and Reporting Requirements.

A sole proprietorship does not have to register with any authority. While most businesses do not require a license to operate, certain trades, such as home remodeling, must be licensed and certain trades' people, such as electricians, must have licenses.

Trade Name Certificate

If you use your own name for the business ("Jack Smith Plumbing"), you do not have to register the business. If you use a fictitious name, like "Quality Painting", you must register that name with the town clerk where you live, or where your business operates. There is a \$500 fine and up to a year in jail for failure to register a fictitious trade name, usually because of a complaint based on fraud or confusion.

Pursuant to the Patriot Act, banks cannot open a business account unless there is a Trade Name Certificate on file, even if the business is operated under the owner's legal name. You can use a personal account for your business, but the checks you deposit must be made out to you, not the business ("Jack Smith", not "Jack Smith Plumbing").

No reports are required from sole proprietorships.

Owners of sole proprietorships who work in the business may want to, or even be required to carry workers compensation insurance on themselves. If they do not, the owner has no coverage for a work-related injury.

Earnings and Taxes

The state or federal government does not tax the sole proprietorship itself. All income and expense from a sole proprietorship is reported on the owner's personal tax return, on Schedule C. The net income on Schedule C is added to the business owner's income, on line 12 of his or her tax return, form 1040. The business owner then pays all federal and state income tax at his or her personal tax rates. In addition, Schedule C net income is subject to self-employment tax. Losses from a sole proprietorship are deductible only to the extent of the owner's "basis" which is the sum of the owner's investment (monetary and asset value, not work¹), plus any *taxed* profits from prior years, minus any *deducted* losses from prior years. Losses in excess of the basis may be carried forward to offset future profits.

Self-Employment Tax

While it sounds like a special tax or maybe even a penalty for the self-employed, it is actually the owner's Social Security. When you work for an employer, the employer deducts 7.65% of your pay for Social Security in addition to any income tax withholding. The employer pays the same amount for your Social Security. When you are self-employed, you are both employer and employee, so you pay 15.3% of your net (Schedule C) earnings² for social security. Because most self-employed do not treat themselves as employees, they do not get a paycheck with social security deducted, so they pay the tax annually by attaching Schedule SE to their income tax return and adding the self employment tax with their personal income tax payment.

Sole proprietors do not pay unemployment tax on their non-employee earnings and are not eligible for unemployment benefits to replace that income.

¹ "Sweat Equity" does not count towards basis, nor will banks count it as an owner contribution.

² For the purpose of calculating Self-Employment Tax, the net Schedule C earnings is multiplied by 92.35% to reflect the tax advantage that would have offered when the employer paid it's half as a tax-deductible business expense.

Liability

The owner/operator of a sole proprietorship is personally liable for the debts of the business, including judgments from lawsuits. From the standpoint of responsibility and liability, the owner is the business.

General Partnership

If there is more than one owner, the business cannot operate as a sole proprietorship. A partnership must have two or more owners, called “Partners”. Their partnership interest (percent ownership) need not be equal. Each partner in a general partnership contributes money or time with the expectation of sharing in the profits and losses of the business. Each partner is an agent of the partnership, making his or her actions binding on the whole business.

A partnership is legally the Partners and has no life on its own. A partnership ceases to exist upon any change in the partnership interest of any of the individual partners. In that case the business need not close. A new sole proprietorship or partnership of the remaining partner(s) can be created.

Organizational and Reporting Requirements.

Partnerships need not be registered with anyone. The same rules for Trade Name Certificate apply, so having the legal name of at least one partner in the business name satisfies the law.

Although a written partnership agreement is not required, most partners enter into such an agreement to define their individual rights and obligations. If there is no written agreement, the state partnership law governs the terms of the partnership. Partnership agreements address a lot of *what ifs* that may occur, such as a partner wanting to leave the business or dying. It is wise to work these out before they happen. *Hire an attorney to draw up, or at least review, the partnership agreement.*

Earnings and Taxes

The partnership itself pays no tax on its earnings. The partnership must file an informational tax return: Federal form 1065 and Connecticut form CT-1065. These forms show the partnership profit and loss statement and the portion of the net profit and loss that accrues to each partner. Each partner’s identity and share of the profit or loss is then shown on a separate page, called Form K-1.

Each partner must attach a copy of the K-1 to his or her personal tax (1040) return, add the partnership profit to income and pay income tax on it at

the appropriate personal tax rate. K-1 income is also subject to Self-Employment Tax, unless it is from a “Passive” source, such as rental income. Losses are only deductible to the extent of the partners “basis”.

Partners do not pay unemployment tax on their non-employee earnings and are not eligible for unemployment benefits to replace that income.

Liability

Partnerships may own real property and may sue and be sued in the partnership name. ***The partners are subject to unlimited personal liability.*** The liability is joint and several, meaning that any of the partners could be held responsible for the entire debt of the business, if the other partners have insufficient assets to cover their share of the loss.

Limited Partnership

A limited partnership is designed to attract investors. It includes at least one general partner and one or more limited partners. The limited partners are passive participants. They invest capital into the partnership, but do not and cannot take part in management or operations.

Organizational and Reporting Requirements.

Limited partnerships are required by statute to file with the Secretary of the State a Certificate of Limited Partnership, which has been signed by all general partners, or by their attorneys. It is an investment vehicle and there are laws to protect investors from fraud.

Earnings and Taxes

Earnings and taxes for both General and Limited Partners are handled the same as regular partnerships, proportional to the partnership interests.

Liability

The general partner(s) have unlimited personal liability, the same as in a regular partnership

A limited partner has no liability for the debts of, or judgments against, the Limited Partnership. The most they have to lose is the amount of their investment in the partnership. Under federal tax laws, limited partners may deduct the limited partnership losses, or the loss of their investments in limited partnerships, from other passive (but not active) income.

Corporation

A corporation is a state chartered legal entity that exists separate from its owners. It can outlive an owner and be passed from owner to owner without having to be re-formed. One or more shareholders own it, whose loss exposure is limited to the amount of their respective investments. Corporate shareholders generally will not be held liable for the corporate entity's debts or liabilities, unless they have personally guaranteed them. Likewise, corporate assets are protected against liabilities incurred by the shareholders, as individuals.

Officers Liability

While the owners of a corporation or LLC can not be held liable for the debts of the business, including those arising from court judgments (lawsuits), the officers of a corporation or LLC can be held personally liable for illegal or negligent acts or omissions.

Because the owners and officers of a small business are usually the same, the corporate or LLC form does not provide the small business owner the same isolation from liability as it does the non-managing shareholder of a larger corporation. The corporate or LLC form does not decrease the need for adequate liability insurance.

Small business owners are also frequently required to personally guarantee the debts of the business to creditors and lenders. In the case of a default, that guarantee places the business owner's personal assets at risk.

While a separate entity form will not fully protect an officer from most lawsuits or an owner from debts he or she has personally guaranteed, it may provide some defense, especially if the business is adequately insured. Such protection can be severely compromised if the business fails to act and appear as a corporation or LLC. Failure to properly identify the business, as a corporation or LLC, in all uses of the business name, failure to keep required records and reports current, or co-mingling business and personal funds can render legal protection void.

Organizational and Reporting Requirements.

To incorporate a business, you will need to file a Certificate of Incorporation and Organization and Report with the Secretary of the State's

Office. Every two years, the Corporation must file a Biennial Report naming all Directors and Officers.

Owners of a corporation are called stockholders. Generally, the only managing decision stockholders can make is to elect the board of directors. The board of directors do not run the company, but make the policy decisions for the corporation, including the appointment of officers and top management. A corporation must have a president, treasurer and secretary and the identity of those officers must be reported to the Secretary of the State whenever there is a change or not less than biannually. In Connecticut, one person may be the sole stockholder, sole director and serve as president, treasure and secretary of a business organized as a corporation.

President – Chief executive officer, runs the business.

Treasurer - Controls financial matters, the only one who can sign checks (can be delegated).

Secretary – Records and reports the acts of the board of directors.

A Corporation must maintain on the premises of its home office a Stock Book and Minute Book. The Stock Book is a record of ownership of the shares in the corporation. The Minute Book has records of the meetings of the board of directors, which must meet at least annually to elect the officers of the company.

A corporation can only enter into a contract signed by an officer duly authorized by the board of directors, usually the treasurer. Some acts, such as opening a bank account, will require a Corporate Resolution by the board of directors, signed by the secretary.

Corporations may own real property, and may sue and be sued in the corporate name. A corporation does not terminate unless termination is provided for in the Certificate of Incorporation or if a Certificate of Dissolution is duly filed with the Secretary of the State. A shareholder's transfer of stock will not affect the existence of the Corporation.

Earnings and Taxes

For tax purposes, there are two types of corporations, “C” and “S”. There is no difference as to the organizational form with the Secretary of the State. The difference is in the filing status with the federal Internal Revenue Service.

C-Corporation

A “C” corporation is taxed as a separate legal entity, paying tax on its income at the corporate federal and state tax rates. C-Corporations file federal taxes on form 1120 and pay quarterly estimated taxes with form 1120-W. While corporate tax rates are generally lower than personal rates, the profits of a corporation are paid to the stockholders as dividends. Dividends paid by a corporation are after tax income to the corporation and taxable income to the stockholders (what is frequently called ‘double taxation’).

S-Corporation

An S-Corporation is a corporation that is taxed as a partnership for federal tax purposes. Income and deductions “flow through” the corporation to the individual shareholders. It has the advantage of avoiding the double taxation and still offers the legal status of a corporation.

S-Corporations are treated identically as C-corporations in all matters other than federal income taxes. In addition to the federal and state income taxes, the State of Connecticut imposes an additional tax on the S-Corporation (currently \$25.00 per year), which it does *not* impose on a partnership or a limited liability company.

S-Corporation Election

To elect S-corporation tax status the corporation must be domestic (formed in one of the United States) with not more than 35 qualified shareholders. Qualified shareholders mean only individuals, estates, trusts and partnerships. If a corporation of any type or a non-resident alien owns a corporation in any part, it may not elect s-corporation tax status. An S-corporation is permitted to have only one class of stock, and it may not be a member of an affiliated group of corporations. S-Corporations are required to use the calendar year, as their fiscal year.

In order for a corporation to elect to be taxed as an S-corporation, Internal Revenue Form 2553 must be filed by the 15th day of the third month of the year during which S-corporation status is elected. All stockholders must sign the form.

Changing a corporation from “S” to “C,” or vice-versa, may have tax consequences based on prior earnings treatment. Simply put, one cannot avoid taxes by changing the form. It is thus best to make the decision early in the corporation’s life.

Limited Liability Company

A Limited Liability Company (LLC) is similar to a corporation in that it is a separate legal entity from the owners. It is a “pass through” tax entity for both state and federal income tax. Unlike an S-corporation, there is no limit on the number of members of an LLC or on who can be a member. A Limited Liability Company requires only **one** person in the State of Connecticut. Different rules may apply in other states.

Organizational and Reporting Requirements.

Articles of Organization are filed with the Connecticut Secretary of the State. An LLC is required to file an annual report naming the members with the Secretary of the State. In addition to filing the Articles of Organization, the member(s) of the LLC should adopt an LLC Operating Agreement, similar to a partnership agreement. While the Articles of Organization are easy to fill out, it is recommended that the members consult a lawyer to draft the Operating Agreement.

LLC’s are much simpler than corporations. The owners of an LLC are called “members”. The LLC can be operated by its members or by a manager, appointed by the members. The Operating Agreement details the rights and responsibilities of the members or managers and the rules governing the management and operations of the LLC.

Earnings and Taxes

As a ‘pass-through’ tax entity the earnings of an LLC are normally treated similar to a partnership, for tax purposes. If the LLC has only a single member, the entity is treated similar to a sole proprietorship, for tax purposes. Under the rules, a member pays tax on his or her share of the net profit of the business, regardless of the amount of money he or she draws out of the business.

Members of an LLC cannot be employees of the business. They do not pay unemployment tax on their income. They are not eligible for unemployment benefits. The money a member draws out of the business has no tax withheld. The tax report that a member of an LLC that is taxed as a partnership gets at the end of the year is K-1, not a W-2. The member is subject to the Quarterly Estimated Tax rules.

An LLC must have at least two or more of the below corporate characteristics to be treated as a partnership for tax purposes and for its members to be entitled to pass-through tax treatment:

1. Continuity of life;
2. Centralization of management;
3. Limited liability;
4. Free transferability of interests.

Business Entity Tax

Connecticut levies a tax of \$250.00 each year on any registered business, foreign or domestic, organized as a corporation or LLC, even if the organization is not operating or transacting business. This tax is owed every year until the organization is legally dissolved, which requires tax clearance certificates. The dissolution process can be difficult. Forming a corporation or LLC without sound reason can be a costly mistake.

Foreign or Domestic?

With respect to Connecticut, a corporation or LLC is considered “foreign” if it is organized under the laws of another state or a foreign country. In federal legislation, a distinction is made between “foreign” corporations (those organized outside of the territorial limits of the United States), and “domestic” corporations (those organized within the United States).

Certificate of Authority for Foreign Business Entities

To transact business in Connecticut, a foreign corporation, limited partnership or LLC must obtain a Certificate of Authority from the Secretary of the State. This requires the filing of a registration form together with a filing fee. Those forms and fees are much the same as the registration forms for a domestic corporation or LLC. A Connecticut Agent for Service, who is a Connecticut resident authorized to receive legal notices on behalf of the foreign business entity, must be designated on the registration form.

Every other year a biennial report must be submitted, together with a fee, to the Secretary of the State. Failure to file this report can result in the revocation of the Certificate of Authority.

If a foreign business entity conducts affairs in CT **without** a Certificate of Authority, then it is liable to the State, for each year or part thereof that it transacted business without the certificate, for an amount equal to two thousand dollars plus all the fees and taxes it would have owed had it applied for and received the certificate and any interest or penalties for failing to pay

those fees and taxes. If the entity is not-for-profit then it will not be liable for penalties, but will still be liable for any fees, taxes owed, and interest thereon.

Regulation and Taxation

Licenses and Permits

While every business is subject to local, state and federal regulation and taxation, few require licenses. While the two principal departments in Connecticut licensing business are the Department of Consumer Protection and the Department of Public Health, other departments including Agriculture, Banking, Environmental Protection and Insurance require certain businesses under their jurisdiction to be licensed. People who engage in certain trades, such as hairdressers or electricians, have to be licensed, as well as the business. The Smart Start program is a free service of the Connecticut Economic Resource Center (www.cerc.com) that assists businesses in licensing compliance. If you are unsure if you need a license for your business or need help obtaining it, contact CERC.

Local Regulation

Land use (zoning), building codes, fire safety codes and health codes are enforced at the local level by employees or agents of the municipality. For assistance with any of these, always start with the economic development coordinator your friend at Town Hall. That person's job is to attract new business to the town and assists with site selection, zoning issues, permitting and code compliance.

Every municipality governs land use by designating one or more zones in the categories residential, commercial and industrial. The first step in considering a business site is to find it on the town zoning map to see what zone it is in and then checking the zoning regulations to see if the business is allowed in that zone and under what conditions. There may also be requirements in the zoning regulations, such as on-site parking and restrictions on signs. Failure to comply with local zoning regulations may lead to the issuance of a cease and desist order by the local zoning enforcement officer that could put you out of business.

Anything more than cosmetic renovations, such as painting and carpeting may require the business owner to get a building permit. Renovations done under a permit must be done by licensed contractors and meet building codes. Plans for substantial renovations must be done by a

licensed architect and/or engineer and approved by the building official prior to the issue of a permit. You may also be required to cure existing violations that are not your fault.

Businesses that have customers or employees coming to their premises are subject to the fire safety code, enforced by the local fire marshal. That code can affect the floor plan of the business; materials used in building it, and may require fire suppression and/or detection systems in places of public assembly, such as restaurants.

Beauty salons and businesses that produce food for human consumption are regulated by the local health official, called a sanitarian. Plans for such facilities must be approved by the sanitarian and the facilities must be periodically inspected to be sure health safety is practiced.

Local Taxation

Other than nominal permit fees, municipalities in Connecticut can only raise revenues by property taxes. Business pay tax not only on their real property (land and buildings), but personal property: equipment, inventory, and supplies, even livestock. Like any tax, good planning and strategy will save money.

Every business in town must file a Declaration of Personal Property with the Assessor by the end of October each year to itemize the value of all personal property. Failure to file empowers the Assessor by law to place a “fair market value” on the business property and the business cannot appeal. By failure to file, it has waived that right. You can file a zero balance declaration, but you must not fail to file.

Employer Requirements

The State of Connecticut has significant jurisdiction over employers. Becoming an employer is a big step. There is a substantial body of state and federal labor law and a great deal of tax law and regulations regarding employee benefits.

While the regulations covering employees may at times be complex, they are not impossible and millions of employers handle the requirements. There is also a great deal of help available to employers.

The legal steps to become an employer are:

1. Apply for an Employer Identification Number (EIN) with the US Internal Revenue Service.

2. Register with the Connecticut Department of Revenue Services.
3. Register as an employer with the Connecticut Labor Department.

Federal Employer Registration

Employers must file income and employment tax forms under an Employer Identification Number (EIN). While a sole proprietor may file income tax forms under his or her social security number, it is *strongly recommended* that all sole proprietorships obtain an EIN, whether or not it has any employees. Most banks require an EIN in order to open a business checking account.

Because corporations and LLC's are legal entities separate from their owners, they must always file tax returns under an EIN. Partnerships need an EIN to keep filings discrete from those of the owners.

You can apply for an EIN with form SS-4 at any Internal Revenue Service office, by mail or online. Immediate issue of EIN numbers is available at their office or online (www.irs.gov). Do not apply for an EIN before you need it or you will be expected to file unnecessary tax returns.

Employers should get a copy of Publication 15 (Circular E) Employers Tax Guide from the Internal Revenue Service and a supply of Form W-4. Employers must withhold federal income and social security tax from employees, pay employer social security tax and federal unemployment tax, all in accordance with Circular E, based on the allowance claims made by each employee on his or her federal W-4 form and report total earnings and deductions to the employee and the Social Security Administration annually on form W-2.

Connecticut Employer Registration

Employers must register with the Connecticut Department of Revenue Services on form REG-1. They should get IP 2004(8), Circular CT, Employers Tax Guide and a supply of form CT-W4. Employers must withhold Connecticut Income Tax according to Circular CT in accordance with the employee's CT-W4 form.

State Labor Department Registration

The Connecticut Department of Labor requires all businesses employing workers to obtain a state unemployment tax number and to register with the Department's Employment Security Division. Any business employing

workers in a manufacturing operation must also register with the Labor Commission.

The publication *Wage and Workplace Standards* is available on the Connecticut Labor Department website as well as at local Labor Department Offices. Information on handling specific employer responsibilities, such as unemployment insurance, is also available as is employer training.

Employers should also get a copy of the *Employer's Guide to Unemployment Compensation*. Employers must pay Connecticut Unemployment Tax in accordance with that guide.

Connecticut Law also requires employers to send a copy of a newly hired employee's CT-W4 to the state labor department within 20 days of hire, by fax or mail. Contact information is in the Reference section at the end of this booklet.

Using a Payroll Service

Employers have the option of paying a payroll service to handle their payroll – print the paychecks, file all of those forms and pay the taxes. Payroll services can also provide workers compensation insurance and employee benefit management. Typically, the payroll service deducts both the employee and employer taxes from the business's checking account when the paychecks are issued. Even if he or she uses a payroll service, the employer must still track employee hours, compile them and submit them to the payroll company. While handling your own payroll can be a simple, repetitive task once you get started, the cost of having a payroll service do your payroll has to be weighed against the benefit – how much time will it save you, the business owner in preparation, required filings and keeping current with changes in payroll tax requirements and what can you do with that time.

Summary of Employment Taxes

Tax	Employer Cost	Depositing	Reporting	Reference
Social Security (employer tax is paid with employee withheld taxes)	7.65% on the first \$87,000 of each employee's wages 1.45% on all wages above.	Form 945: Annually if less than \$2,500/year, monthly up to \$2,500 per month. Biweekly if over (combined remittance).	Form 941, quarterly, with true-up	IRS Circular E (Publication 15), Social Security Administration Employers Guide
Federal Withholding	None, paid by employee through withholding from each paycheck	With Form 941 quarterly if less than \$500/ quarter, if over Form WH: monthly up to \$2,500 per month. Biweekly if over	Form 941, quarterly, with true-up	IRS Circular E (Publication 15)
Federal unemployment	6.2% on the first \$7,000 in annual earnings for each employee	Quarterly with Form 940 or 940 EZ	Form 940 or 940 EZ, quarterly	IRS Circular E (Publication 15)
Connecticut Withholding	None, paid by employee through withholding from each paycheck	With Form CT-941 quarterly if less than \$500/ quarter, if over Form CT-WH: monthly up to \$2,500 per month. Biweekly if over	Form CT-941, quarterly, with true-up	Connecticut Circular CT
Connecticut Unemployment	Based on experience, 2-6% of the first \$15,000 in annual earnings for each employee	Quarterly with Form UC-2	Wage data on Form UC-5A Quarterly (with UC-2)	Employer's Guide to Unemployment Compensation (CT Dept. of Labor)

Overtime Exempt or Not?

Many small businesses get into trouble for failure to pay overtime. Just because someone's title includes the word "Manager" does not make that

person overtime exempt. There are several important tests that a job must pass to be overtime exempt:

- The employee must be able to use his or her independent judgment in performing the work. Work requiring advanced knowledge; defined as work that is predominantly intellectual in character, such as engineering or computer networking, generally satisfies this requirement.
- Duties must be truly supervisory, for example, hiring and firing, setting policy, scheduling workers, making company investment decisions or reviewing performance of other employees. The employee must spend less than 20% of his time on non-supervisory duties (40% for retail and service businesses).
- Salary must be fixed and not reduced by lack of work, jury duty, or partial days off (employee not held to fixed hours)
- Salary must exceed certain levels – currently \$455-475 per week, depending on circumstances.

Professional qualifications, such as advanced degrees or licenses are further factors leading to classifying employee overtime exempt, so long as the above criteria are met. In summary, every case is judged individually and, if there is a doubt, the employee is entitled to overtime.

Employee or Contractor?

It may be easier for a small business to have contractors instead of employees, but calling someone a contractor does not make him one. If a labor or tax authority determines that your contractor is really an employee, you can be responsible for paying back payroll and unemployment taxes, unemployment insurance, and even benefits, with penalty and interest. A contractor must satisfy a majority of the following criteria:

Criteria	Employee	Contractor
Instructions	Told when, how, who does a job and in what sequence. Continuously instructed.	Told what the end result is and sometimes by when it must be complete.
Supplies	Purchased by employer	Purchased by contractor, except business may make available supplies it <i>normally</i> has on hand.
Tools	Provided by employer	Provided by contractor, except business may make available tools it <i>normally</i> has on hand.
Training	By employer	Uses his or her own methods
Incidental expenses	Paid by employer	Paid by contractor - not reimbursed unless specifically covered in the contract
Investment	None	Tools, equipment, vehicle, etc.
Risk	None	Profit & Loss
Payment	Hourly	By job, but can be time and materials
Relationship	Exclusive	Has or seeks other customers
Time	Generally permanent	Generally temporary or periodical
Employee Benefits	Yes	None
Type of work	Close to employer's regular business	Unrelated services
Tax Document	W-2	1099 if total annual payments exceed \$600.00

One of the big things that separate contractors from employees is the contract. A written agreement as to scope of work, payment and addressing several of the aspects above makes this issue much easier for the small business.

State Taxation

All business doing business in the State of Connecticut are required to file a form REG-1 with the Department of Revenue Services within six months of their organization, or before they start operations in the state. The REG-1 is a single registration form that sets up the business for any taxes it may be liable to the state for, such as business, taxi and limousine, sales, cabaret, admissions and sales taxes. Please note that REG-1 is a multi-purpose form and many sections may not apply to your specific business.

Any business selling goods at retail or wholesale in the State of Connecticut must have a sales tax permit, and collect and send applicable sales tax to the state. This requirement is for all businesses regardless of the business form or its federal or state income tax status.

Federal Regulation

Immigration

Employers are required to have proof at the workplace, or a central office, that all employees are eligible to work in the United States. Only U.S. citizens and foreign nationals with work authorization are eligible.

The only acceptable proof is a properly filled out U.S. Citizenship and Immigration Service Form I-9. That form records the employee's identification and work authorization paper numbers. Employers must have on file and available for inspection a Form I-9 for each employee for the longer of three years after hire or one year after separation.

Federal Taxes

Federal income tax is paid by a business based on its legal form and was discussed in that section previously. Tax strategy is specific to the business and circumstances. A tax professional, such as an accountant, is invaluable in forming tax strategy.

Excise Taxes

The federal government imposes a number of excise taxes on certain interstate business activities. These include production of motor fuel, telecommunications, air or sea travel, importing ozone depleting agents, manufacturing hunting or sport fishing equipment, mining coal, manufacturing tires, vaccines, or heavy trucks. IRS Publication 510 discusses specific details about which excise taxes your business may be subject to. These are reported on Form 720.

Record Keeping

WHY ARE RECORDS NECESSARY?

“Why do I need to keep records?” There are two basic reasons:

1. Every business must file tax and information returns with local, state and federal authorities. Organized, accurate records make this easier and save taxes, fines and penalties.
2. Even more important, well-maintained records help the owner control and manage the business. Good records are the foundation of a profitable business.

The last thing your lender or the IRS wants to hear is how you really haven't had time to keep track of those details and all of those numbers, or that you have a bookkeeper who should have taken care of it. Yes, you may hire a bookkeeper, but you, as the owner, are accountable and must be intimately knowledgeable of what the numbers consist of and what they mean to your bottom line.

Remember the list of common reasons for business failure on page 4? Good records and accounting can help prevent eight out of ten of those difficulties! Accurate and organized records are also essential to business best practices, such as:

- Customer relationship management;
- “Just in time” inventory;
- Optimal purchasing control;
- Fixed asset management.

What if I don't understand financial matters?

Then work for someone who does! If you are going to own and operate a business, it is not an option, but a basic necessity. The time to learn accounting and recordkeeping is before you open the business.

It is really simple and anybody with a checkbook has been doing a form of accounting already – you just had only one account for income, salary and one account for expenses, personal expenses. The basic difference with a business is that you will want more accounts to properly manage, to separate expenses into meaningful categories so you can quickly see which expenses are causing a problem or presenting an opportunity.

Accounting is the language of business. It is how businesses communicate as to their condition. It is the language your business will speak to you, your lenders and investors. You must be able to speak that language. It is really easy. **Accounting is simply placing money coming in and money going out into proper accounts to measure the activity.**

Accounting Systems

You may not think you need an accounting system yet, but you probably do.

- You will be incurring tax-deductible start-up expenses and an accounting system is the best way to track them.
- By developing an accounting system along with the financial projections in your business plan, they will be in the same format, making it easier for you and your lender to track goal attainment.

We are often asked if an accounting system should be manual or computerized. By far, a computerized accounting system is less work and far more useful in managing a business. You must, however, know enough basic accounting to understand what is going on behind the pretty screens, or you will be downright dangerous.

One of the services MSBDC provides is basic accounting training as an introduction to computerized systems. Most people can get going on their own accounting system after a single two-hour class.

The Chart of Accounts

In order to do the projections for your business plan, you need use the account categories on a chart of accounts according to Generally Accepted Accounting Principals (GAAP). Otherwise others, such as lenders, will not be able to follow the projections, without you there to explain them.

Sample Chart of Accounts

Category (GAAP)	Accounts (examples)
<i>Balance Sheet Accounts</i>	
Assets	
Current Assets	Cash in Checking Account Cash in Savings Accounts Accounts Receivable Inventory Cash Value of Life Insurance
Fixed Assets	Land Buildings Accumulated Depreciation, Buildings Equipment Accumulated Depreciation, Equipment Leasehold Improvements Accumulated Depreciation, Leasehold Improvements
Other Assets	Notes Receivable Due From Affiliates
Liabilities	
Current Liabilities	Accounts Payable Short-Term Loan Sales Tax Collected Current Portion of Long Term Loan
Long Term Liabilities	Bank Loan Loan from Officers
Equity	Owners Equity (depends on business form)
<i>Income Statement Accounts</i>	
Income	Sales & Sales Tax Collected
Cost of Goods Sold	Purchased Product Direct Labor (manufacturing)
Expenses	Salaries & Wages Owner's Salary Operating Supplies Utilities Repairs & Maintenance Auto & Truck Expense Office Supplies

It is important that you create only accounts you need and accounts that track significant activity. It is best to start with a minimum number of accounts and add them, only if additional detail is worth tracking. Once you use an account, it is difficult to delete it if it turns out to be insignificant because the record must be preserved.

Remember that accounts are types of asset, liability capital, income, cost or expense. Vendors, customers and products are not accounts.

Keep Business and Personal Records Separate

Whether the owner operates the business as a sole proprietorship, a partnership, a limited liability company, or a corporation, the same rule applies: Keep personal finances separate from business finances. **Never co-mingle personal and business funds in the same bank account.**

When an owner pays personal items with business checks or deposits business income directly into a personal checking account it gives the appearance of tax evasion. Such behavior is a common audit trigger. During such an audit, it is up to the taxpayer to sort business and personal transactions and prove there was nothing done wrong. Mixing business with personal finances can also void the separate legal entity status of corporations and LLC's.

Mixing business and personal finances makes control and measurement of the business difficult. That is an invitation to employees, suppliers and customers to steal.

Building Your Advisory Team

While many entrepreneurs may believe they have to go it alone, that is a dangerous misconception. A wise businessperson builds a network of advisors from the moment he or she contemplates going into business and continues to develop that network for the life of the business. These advisors should include as many of the following categories as possible:

- **The trade** –While you may not think you will get much help from the competition, many will consider you a colleague, not a threat. Trade associations are a great place to find mentors in your trade.
- **The Chamber of Commerce** – Most hold social and educational gatherings open to non-members, so you can go and assess the benefits before you join.

- **Your supply chain** – They sell to a lot of businesses like yours and may well be aware of trends and innovations.
- **Your customers** – Cultivate some “regulars” who can give you feedback on your business and the competition.
- **Economic Development Agencies** – In addition to MSBDC, there are a host of agencies offering free assistance to help with your success. They are discussed throughout this booklet.
- **Your Lenders and Investors** – Lenders and investors have a stake in your success and lots of contacts.
- **Professional Specialists** – Your insurance agent, accountant and attorney. Some businesses may have need for an engineer or other technical specialist.
- **Regulators** – The zoning board, fire marshal, building inspector or health inspector are a great free resource.
- **Friends and Family** – They may not be experts, but they care more about your success than anyone else.

Hiring a Lawyer

A lawyer’s best contributions are preventive so don’t wait until you are in trouble to get a lawyer.

Find a lawyer who does small business practice, fills your anticipated need and is willing to work with you at your level of legal ability. Your advisory group can be very helpful in finding the right lawyer.



Some attorneys offer a free initial consultation to new clients. That is not for you to get free legal advice – although you may get a little – it is your opportunity to shop. Interview the attorney to see if he or she is right for you and your business.

Properly preparing for a meeting with a professional – attorney, accountant, engineer, or other – will save you substantially. They charge by the hour and it takes a lot longer to handle something for a disorganized client than for one who is prepared. Do as much of the work yourself, as you can. It takes far less time for a professional to review something than to create it from scratch.

It is recommended that you seek the advice of a lawyer on what form of organization is best for you and your business. Although it is less expensive to fill out and file your own papers for organization, it is best to have any complex filings reviewed by an experienced attorney to:

- Help you understand the long term implications of the legal alternatives;
- Assist you in setting up the articles of organization and other legal requirements for the particular form of business entity;
- Create or review the agreement among the owners (very important);
- Recommend provisions for methods of dissolution or sale of the business;
- Advise you on tax and regulatory implications;
- Greatly reduce liability risks - if you don't complete the forms accurately, you could expose your personal assets in the event of a liability suit.

You have the right to expect your lawyer to preserve your secrets and confidences. It is called Attorney-Client Privilege. Anything said is in confidence and may not be revealed even, if subpoenaed by a court of law. If you decided to terminate the relationship, the lawyer will be required to respect your confidences and to transfer your file to your new lawyer.

Be aware that anyone you bring with you to a meeting with your lawyer is not subject to Attorney-Client Privilege unless they are also fellow clients for the issues at hand, such as partners or other fellow owners of your business. Other "guests" at a meeting with an attorney, such as consultants and accountants, can be made to testify against you on matters discussed with your lawyer.

Fee Options:

Never hesitate to discuss fees and prices. Remember, you are the customer. You should understand, however, that the cost of using an attorney is almost entirely dependant on the scope of services. The client adding work to the original understanding causes many fee misunderstandings.

Be a smart shopper. Before you make the first call, prepare a written list of what services you will need and, just as importantly, what legal work you are comfortable handling yourself. Based on the discussion, you may need to

amend the list during the call or at your first meeting. You may write the quoted fees on your list and ask the attorney to initial it.

There are several fee structures that are commonly used. You will probably be subject to more than one over time.

- A **retainer** is a periodic, fixed payment. This fee is no longer commonly used because it is not clear what the client is entitled to. Unless the scope of services and the client's expectations is clear, it invites dispute. It is unlikely a new client would be offered a retainer fee arrangement.
- An **hourly rate** is the most common method of payment. You may compare hourly rates between attorneys, but remember the number of hours affects the final cost just as much. You should ask the lawyer to estimate the number of hours needed to perform the work you are requesting, so that you will have an idea of the total expense. Under an hourly fee agreement all work the lawyer does for you, including phone conversations, will be billed to you. Chat will be very expensive, so organize your thoughts before you pick up the phone and call your lawyer.
- A **flat rate** may be used for some routine matters. Instead of charging by the hour, your lawyer may charge a fixed amount for a specific task, such as filing for a permit. This fee is fixed only because they know how much time the task normally takes.
- A **contingent fee** is only offered to plaintiffs in lawsuits. It is a negotiated percentage of any amounts the lawyer recovers for you through settlement or at trial. If there is no recovery, or settlement, there is no fee. However, in contingent fee situations, the lawyer usually requires you to cover expenses, such as court fees, copying, travel expenses, and telephone calls, regardless of who wins the case. In large lawsuits the expenses can build up to such an extent that they may exceed the contingent fee.
- In some cases the fee agreement will combine two or more of these options. This will depend on the type of matter, the lawyer, and the client (you), and it should be the result of realistic discussions between you and your chosen lawyer.

Selecting an Accountant

IS AN ACCOUNTANT NECESSARY?

An accountant is recommended for all small businesses and is required if a lender requires *audited* financial statements. Only a Certified Public Accountant (CPA) can certify audited statements.



The accounting system you choose should be designed to provide timely reports and information necessary to keep you on top of the financial condition of the business. It must also be simple and manageable, so you actually use it to its full potential. The more accounting work you do, the less you have to pay an accountant to do. The closer you are to your accounting system, the closer you are to your business.

Your accountant should also serve as part of your advisory team. An experienced accountant can point out risks and opportunities revealed by your financial data. Selecting the ‘right’ accountant for your business is critical. Accountants are not all equal, with or without a CPA designation. Some things you should consider:

- The accountant should be able to work with you at *your* level of bookkeeping capability and be willing to help you to improve your accounting skills.
- The accountant should be able to spend time on your work, as necessary.
- The accountant should be experienced in small business, ideally in your industry. An experienced accountant can advise you on the latest tax incentives available to you.
- The accountant’s fees must be affordable. As with an attorney, work out the scope of services and fee schedule before you make a commitment.

Should you shop around for an accountant? By all means, ask pertinent questions. Ask for referrals – then call the referrals. Ask those in your advisory group who they recommend.

Your accountant may advise you as to what accounting software to use for your specific business. Perhaps initially you will not use software, but will

purchase a one-write carbonized bookkeeping system. In either case your accountant may help you set up your chart of accounts, if you need guidance.

It is **your** responsibility to get the business transactions into the accounting system, in other words, bookkeeping (by you or a bookkeeper hired or contracted by you). Bookkeeping is the daily recording of all transactions.

It is your accountant's responsibility to question your management of the income and expenses. Do not take offense of any criticism. It's an accountant's job to point out deficient bookkeeping or control practices. Some advice you may get from your accountant includes:

- Suggesting financial procedures and practices to maintain control of the business and yield meaningful information for management;
- Examining financial strength or weakness of the business and suggesting ways to improve things;
- Advising Tax strategies;
- Analyzing leasing verses buying equipment, which may involve complex financing and depreciation trade-offs;
- Pointing out changes in financial performance and analyzing trends and cycles. A good accountant may recommend remedies and alternative strategies.

Who Runs the Business?

You do! Always remember that you have the ultimate responsibility for running your business. Professionals and advisors only offer guidance and the final decisions are always yours. Compliance with laws, including tax and employment, are your responsibility. It is up to you to monitor the condition of the business and its assets. It is up to you to maintain sales.

Insurance

Many of the risks small business owner face might cause considerable financial loss. These risks, called "perils" in insurance terminology, include flood, fire, breakage, theft, and negligence. Negligence that results in personal injury or property damage leaves the business and/or owner liable for

monetary damages. Most of these perils can be protected against with insurance.

It is important to avoid being underinsured and exposed to devastating perils. It is also foolish to be over-insured and waste money on insurance premiums for protection that costs more than the likely losses. To avoid both of these, you need to know how insurance really works.

Insurance companies do not pay for such losses; they pool similar risks in a risk class and calculate the likely (actuarial) total loss in the pool. Each individual risk in the pool pays a proportion of the estimated loss, plus the insurance company's overhead and profit, as an insurance premium.

That means you insure for the perils you cannot afford and not for minor risks. Not buying insurance for minor risks is called "self-insurance". As your company grows, it will be able to afford larger and larger risks and save money by self-insurance.

Other characteristics of business insurance that are not typical of personal lines (what the insurance industry call products such as homeowners and auto insurance) are:

Loss Control Programs – Business risk pools are smaller than those for individuals (such as homeowners insurance) and businesses within those pools are rated based on their individual loss experience. That means safety programs; loss prevention programs and loss investigation programs pay for themselves many times over in premium savings. Your insurance carrier has professionals who can assist with setting up your loss control programs at no charge.

Higher Deductibles – Businesses evaluate the trade-off between premium and deductible and usually find that the premium saved justifies self-insuring the higher deductible.

Co-Insurance – Common business property insurance covers 80-90% of replacement value up to a stop-loss, usually \$5,000. Liability coverage never has co-insurance so the insurance carrier can defend the claim exclusively and has sole determination regarding settlement.

Minimum Coverage – Generally, if a business does not cover property by at least 80% of replacement value, the insurance will only pay losses proportionate to the percent of the value insured.

Disaster Management and Recovery – If your home burns down, you rebuild or get a new home. Your business has a life of its own that requires continuity. Insurance may pay for certain losses, but it will be up to you to start the business up again after that loss. Plans for disasters from fire to computer crash should be worked out before the disaster or it is unlikely your business will survive.

In general, insurance for the business owner falls into six categories:

Liability Insurance:

- Liability Insurance will cover your business for negligent acts or failures to act responsibly resulting in personal injury or property damage. The insurance carrier will defend the business against lawsuits for public and *product* liability. In order to reduce potential liability, most policies cover the first \$5,000.00 or so of medical expense for any injury related to the business, regardless of fault.
- Liability is usually the highest potential monetary risk for business dealing directly with the public. The absolute minimum limit such businesses should have is \$1,000,000 per occurrence. Most landlords will require you to have public liability coverage and probably at a higher limit. Most large business customers will require you to have at least \$5,000,000 in product liability coverage. The assets of the business and its officers are at risk for any judgment or settlement that exceeds the policy limit.
- In any small business, the owner/officer(s) should be listed on the policy, as additional insured(s). Most lawsuits will name the owner/officer(s) as additional defendants. Insurance carriers usually do this at no additional cost.

Premiums for liability coverage are not fixed. They are based on sales. At the end of each policy year, the carrier will audit your sales and adjust the premium, billing additional or refunding unapplied premium.

Property Insurance:

- Property insurance covers losses due to fire and other perils such as windstorms, explosions, smoke, and water damage. Perils covered or excluded differ between carriers and policies. Common exclusions are acts of war, riot, flood and radioactive release. It is wise to compare and shop for more than price.

- Additional coverage may be available for perils specific to your industry, such as burglary and shoplifting for retailers. Fire insurance policies are available for real property (buildings) and for business property (contents).

Business Interruption Insurance:

- If your business is damaged by a covered peril and you cannot operate, business interruption insurance will pay for certain ongoing expenses, but generally not owner's salary and profit. Since coverage differs between carriers and policies, it is wise to shop.

Bonds:

- Performance Bonds may be required by a customer to protect him if you fail to perform under a contract.
- Fidelity Bonds will protect you against financial loss due to dishonest employees.
- Janitorial Bond protects customers from loss of property through theft or breakage.

Business Life Insurance:

- May be required by a lender or investor to reduce the loss of investment in the event of the death of a manager or employee whose contribution to the success of the business is essential. Often partners get life insurance on each other. Family businesses often use business life insurance as part of their estate and succession plan. This insurance is referred to as Key-Person Insurance.

Worker's Compensation Insurance

- Worker's Compensation Insurance is *mandatory in Connecticut* for all businesses that employ workers, whether full or part time. Under workers compensation law, the employer takes the responsibility for the financial loss of any work related injury and the employee waives the right to sue for additional damages. Financial loss can include compensation for scarring, partial disability and lost wages. Work related has been interpreted to include commuting to work and doing work for the employer off premises, including the employee's home.
- The potential losses under worker's compensation are much greater than most employers think. Policy premiums are based on the employer's loss history. An "accidents will happen" attitude can result

in very high premiums. Worker's compensation expense has closed many businesses. Loss control and back to work programs are highly effective in reducing the cost of this insurance.

Additional insurance is available covering the risk or loss from such diverse events as poor weather, fire sprinkler leakage, goods damaged in transit, glass breakage, damage to neon signs, and loss of accounts receivable. These may be packaged into your main policy, or be covered on a separate policy. It is usually less expensive to package these as additional coverage. An insurance agent experienced in business insurance can analyze the insurance needs of your business and discuss the costs and benefits of different policies with you. Always evaluate the cost of the coverage against the financial risk.

Business insurance is a specialty. The agent who sells you auto or homeowners insurance may not even offer business insurance. An experienced business insurance agent can save you money by getting more than one carrier (insurance company) to quote the policies. The agent can get your business placed in the risk class with the lowest premiums

Most business qualifies for coverage in more than one class. A dance studio, for example may be insured as an educational or a fitness facility, with very different rates. Once a carrier accepts a risk (your business) in a class, it is bound to the coverage.

Some agents and many insurance carriers offer loss control services. Effective loss control programs benefit businesses greatly because loss experience is figured into future premiums. Premiums can easily double with poor loss experience. Since loss records are available to all carriers, a business cannot escape a bad history, by simply switching carriers.

Goodwill and Intellectual Property

The value of a business is not just in the hard assets on its balance sheet. A good part of it is intangible property. Intangibles, such as reputation or the value of a business name or trademark are called goodwill. An original recorded work or a proprietary idea, whether it is a patented, secret or neither is called intellectual property. These soft assets can be worth much more than the plant and equipment.

Trademarks

The name of a successful business has great value and should be protected from use by others. Registering a trade name with the municipality (Trade Name Certificate) was discussed previously.

Trademark rights to your business, name, trade name, product name or logo (design used to identify the business or product) are automatic for the business or person who first uses it. To claim them, it is wise to place the word “trademark” or TM after the name or mark each time it is used. This avoids confusion as to exactly what your trade name is.

In addition, a trademark can be registered with the Secretary of the State of Connecticut or U.S. Patent and Trademark Office. The registrant must satisfy that the trademark is and has been in commercial use. A Registered Trademark must be identified each time it is used by the symbol ®. Many businesses get several registrations for the same name or logo, using different colors and registering it in parts. as well as whole.

A trademark holder cannot only stop others from using the trademark, but can stop the importation of goods from abroad bearing the trademark. Information on trademarks is available on the website of the Patent and Trademark Office (www.uspto.gov).

A business selling goods or services abroad may need trademark protection in every country it markets to. Many countries do not grant automatic protection, so registration is required. Protecting a trademark internationally became easier in 2003 with the adoption of the Madrid Protocol. One application to the U.S. Patent and Trademark Office for international registration, once examined and approved, will provide protection in all countries that adopted the protocol.

Copyrights

You do not have to register with anyone to claim copyrights to original written, graphic, or audible work. You have that right the moment the work is created. You should make that claim clear by stating three things prominently on the work:

1. The words “copyright”, “Copr.” Or the symbol ©
2. The date of creation
3. The name of the person or business claiming the right

Example: © 2006, Jones Company

You may register a copyright with the U.S. Copyright office to make a public record of your claim or to gain international protection. Information on copyrights is available on their website, which is listed in the reference section at the end of this booklet. Copyright protection extends seventy years following the death of the copyright holder.

Businesses frequently claim copyrights on many of the original documents they create, such as training manuals, procedures, contracts, advertising and policies. While copyrights do not give the protection of a patent, they will stop the competition, and ex-employees, from duplicating your hard work.

Patents

The inventor of a process or object does not have automatic protection like the author of a book. He or she can get exclusive rights for a limited time by obtaining a patent. Obtaining a patent is more complex than a trademark so a patent attorney is recommended.

The period of exclusive use is usually 17 years, after which the invention is in the public domain, meaning anyone can copy it. Information on patents is available on the website of the U.S. Patent and Trademark Office (www.uspto.gov).

Trade Secrets

Many businesses protect their inventions and “know-how” by keeping it a secret. Secrets can outlast a patent. The formula for Coca-Cola has been a trade secret for over a century.

There is some legal protection for trade secrets under the Uniform Trade Secrets Act, which protects secrets from theft, but not careless divulgence. That means that you have to take measures to keep your secrets confidential and make every employee who has to know even part of the secret execute an acknowledgement that the secret is the intellectual property of the business and agreement not to disclose the secret or utilize it for personal gain.

Covenant not to Compete

Businesses that have to disclose confidential information or trade secrets to employees or other businesses should require a covenant not to compete, a non-disclosure agreement, or both. These are common in joint ventures.

To be enforceable, a covenant not to compete must cover only sensitive information and not be overly restrictive. A worker who must be taught a

proprietary technique to make tires, for example, could not be restricted from working in the entire automotive industry for fifty years after he leaves the employer. Unless the confidential material is of a very enduring nature, the enforceable term of a non-compete agreement is two to five years.

Non-disclosure agreements may be enforceable longer than a non-compete, if there is reasonable expectation that damages may occur if the information is disclosed. A non-disclosure agreement on the formula for Coca-Cola could go past the life of the employee and be effective on his estate.

Non-disclosure agreements cease to protect confidential material that is made available to the general public voluntarily by its owner. The owner must take reasonable measures to protect confidential information for a non-disclosure agreement to be enforceable.

The Business Plan

Why do you need a business plan?

- Internally, to set goals and measure achievement. Tracking your business against the plan is a highly effective management tool. It is your vision, the path to it and benchmarks (budgets) to measure progress along the way. Business requires different plans through its life cycle, from the feasibility study before start-up to the expansion plan at rapid growth stage to the reorganization plan for a business at decline.
- Internally, the plan keeps everyone working towards the same goals. Without a plan, you can expect only chaos.
- Externally, a comprehensive plan for lenders and/or investors to show that you and your business can provide a return worthy of the risk of providing you with start-up or expansion capital. Lenders and investors will expect reports on your progress on the plan and the plan to be updated on a timely basis during their relationship with your company.
- Externally, a summary plan for suppliers and other related persons and entities, to motivate or enable them to help you achieve your goals.

Obviously, to meet any of those purposes, the plan has to be based on reality, not a work of fiction or fantasy. You will have to live that plan, so it is no place for “guesstimates”.

Where to begin?

There are three parts of the business plan. You should work on all at the same time so they are in agreement and support each other. A contradiction will cause automatic rejection.

1. **Narrative** – The narrative is the story of your business and how you will make it succeed. Start with your vision and proceed to what you love about the business, what got you excited enough to begin this process – be it the product, marketing, your experience, whatever. The rest will grow from there. *Remember, this is a plan, not a promotion.* Don't tell how great you and the business are; tell how you are going to get it done.
2. **Financials** – These are detailed financial projections. Start with the Sources and Uses statement. That is easiest to do and all other financials flow from that.
3. **Exhibits** – Things that support the plan and financials. Some are required and anything else that supports the plan should be included. Start with what you have – articles, patents, leases and information on competitors. The need for other exhibits, and many of the exhibits themselves, will be developed along the way.

Business Plan Outline

There is no set order to a business plan, but it must be in order. The plan should flow smoothly from concept to concept and make a clear conclusion – that it is a good, complete plan. Your MSBDC Counselor can provide you with detailed instructions and templates to help you create your plan. It follows the outline below:

Narrative

Warning: If you do not have a workable answer to <u>all</u> of the questions in this outline, you are not ready to start your business.

Mission and Vision

Mission: What do you intend to accomplish? What are your objectives?

Vision: What will the business be at opening, and then end of the first year and ultimately?

Keep these conceptual and brief; details go in the next section.

Description of the Business

What is the operating history of the business, if any?

What legal form was chosen for the business and why?

What are the operating hours and why?

What do you intend to accomplish over the next 1, 3, 5 and ten years (or whatever time horizon you envision)?

Keep this brief and simple, details follow in later sections.

Products and Services

Just what do you intend to sell (list all products, by category if there are more than 20, describe examples of services)?

What needs do you intend to satisfy?

On what basis do you think these products or services meet those needs?

The Industry

What is the business environment - industry history and trends, recent history of the industry (both in your market and nationally/globally)?

Who are the other players in the industry (just list the names of your competition)?

You don't need to write a book. The purpose is to (1) show you know the business, and (2) point out what aspects of the industry and/or its trends favor your business.

Target Market

What market you propose to serve?

Define your target market – your potential customers in terms of demographics - geographic area, socio-economic status, gender, occupation age group, etc.

Market Size and Trends

What is the approximate size of your target market?

What is its growth rate?

Use real statistics, not guesstimates!

Marketing Plan

Overview: What makes your products or services attractive to the target market (on their own, not relative to the competition)?

Pricing

What is the price structure?

How does that pricing compare to the industry and why is it different or the same?

Why will that price structure appeal to the target market?

Location

Where will you place your business or what is your means of distribution?

Why will that appeal to the target market?

Promotion

How will you get your message to the target market?

What differentiates your products or services; what are your Unique Selling Points?

Competitive Analysis

What are the basic offerings and operations of each of your competitors?

What are your advantages over the competition?

How are you going to maintain any advantage you claim, or do you plan to add advantages as time goes on?

Do you have any patents, copyrights, trademarks, trade secrets, and contracts that give you a competitive edge?

Do not knock the competition, they are successful or they would not have survived. Stick to hard facts that give you an entry/edge for your target market.

Management and Organization

Overview: In summary, how will your business be organized?

Management Team

What is the staffing requirement, by job title (include an organization chart, if more than three)?

What are the job duties of each title (in brief)?

Who does each person report to and who reports to him/her?

What are the qualifications of the key people, in detail?

Advisory Network

What advisors and professionals have you secured relationships with that will assist with the business and what are their qualifications?

You want to show you have capable support and are not going it alone.

Principals

Include the bios of all principals. You must demonstrate management capability and capability in your specific industry. This is not your resume, although you may include it, as a supporting exhibit. You should include any life experience that helps qualify, including military and volunteer service.

The most important factor to lenders and investors is management capability. Deals are made or lost on that alone.

Operations

How will the company operate, get the mission done?

What resources will be utilized?

Business Systems

How will you do accounting?

How will you maintain financial control?

If you will be an employer, how will you manage human resources (recruitment, salary structure, vacations, discipline, etc.)?

Supply Chain

Where you are going to get materials and services and why?

What arrangements have you made, including credit terms?

What are your alternative or backup sources?

Insurance Plan

What are the insurable risks specific to your business and will you get coverage, why/why not?

Where will you place coverage and at what cost and payment terms?

Compliance Plan

What permits and licenses are required for this business and how do you plan to procure them?

Include your plan to comply with environmental, taxation, and regulatory requirements

Risk Analysis

What assumptions did you make in the plan and financials and how may they be wrong?

Include any external possibilities – What can go wrong and what would you do?

In each case what would you do, what have you done to protect against those contingencies?

Disaster Recovery Plan: How would you manage through and recover from a natural disaster, prolonged power failure, data loss, death of a principal, shutdown of a major customer, etc?

Exit Strategy

How do you plan to get out of this business?

What steps will be necessary to accomplish that and when/how will you take them?

This section is usually not necessary for plans written for lenders.

Notes to Financial Statements

How did you arrive at your of sales projections?

What resources did you use to get prices/bids for your start-up needs and ongoing costs and expenses?

How did you arrive at the amount of necessary working capital?

Explain anything that is not immediately clear from the financials.

Financial Data

Sources & Uses of Funds

Projections

- Profit & Loss (by month and summarized by operating year)
- Cash Flow (may be part of Profit & Loss)

- Sales Projections Detail
- Staffing Detail
- Balance Sheet (at beginning and end of projections)
- Amortization Schedule(s) of loan(s)
- Depreciation Schedule (showing equipment purchased over the span of the projections)

You must provide a detailed profit and loss statement and cash flow projections for at least the initial 3 years of loan repayment and justify the numbers with fact. "Guestimates" are not allowed.

Historical Financials (if any)

- Profit & Loss (2-4 years), audited or supported by tax returns
- Balance Sheet (current)

Supporting Documents

Required:

- Resumes of all principals (owners and directors)
- Personal tax returns (3 years) of all principals
- Personal Financial Statement of all principals
- Loan application

Required if Applicable:

- Business tax returns (for existing businesses - 3 years)
- Leases
- Contracts
- Patents
- Agreements
- Business real estate appraisals or independent valuation
- Cosigners' income and financial statement
- Legal (any judgments, liabilities, pending litigation)
- Commitments: subcontractors, distributors, leases, suppliers, etc.
- Franchise: all documentation, legal and financial obligations

Optional to support the plan:

- Independent articles on the industry, local market, etc.
- Supporting statistics from any independent, reliable source
- List of Distributors
- Policy and Procedure Manuals
- Information about Competitors
- Photos of your selected site
- Copy of form of organization document
- Licenses, permits, registrations
- Equipment: serial numbers, purchase dates, and accumulated depreciation
- Listing of aging accounts receivables/payables
- Just about anything that credibly supports the plan

Capital Sources

It takes money to start a business. How much depends on the type of business and the scale the business starts at. It is less expensive and far less risky to start small and grow the business from the income it generates.

The table below shows what sources small businesses have used for start-up capital and how frequently³:

- **88% (440) - Founder's Personal Assets**
- **39% (195) - Partner's Personal Assets**
- **30% (150) - Family and Friends**
- **11% (55) - Bank Loans**
- **3% (15) - Investors**

Obviously, lender and investor financing are not easy to get and there is a lot of competition for them. You must have a very sound plan to get such funding.

The basic difference between a lender and an investor is that an investor gets a “piece of the action” – either a part ownership of the business or a part of

³ *Inc. Magazine*, 2000

the profits. This can be a burdensome relationship for most small businesses so financing from lenders is more common.

That does not mean that lenders have no say in the operation of the business. Common loan covenants and conditions include minimum cash balances, coverage and current ratios. In all cases, a personal guarantee from the business owner is required as a condition for a business loan. That means the owner's personal; assets are at risk, including his or her house.

Before you look outside for funds, look to your own resources. Savings, home equity, friends, family and liquidating (selling) assets should be carefully considered.

Grants

There are no grants available for the purpose of starting or expanding a small business. Grants are given to achieve something good for humanity and buying someone a business may be good for him or her, but not for humanity as a whole. Grants are given to rescue people from a hardship and not owning a business is not a hardship. Nobody is entitled to or deserves to own a business.

All grants have conditions. They require specific performance and all granted funds must be spent as proscribed in the grant. Simply put, there is no such thing as free money.

Beware! Con artists who led them to believe it is otherwise have swindled many people. You can buy books, join organizations or pay for grant writing services, but we are not aware of one grant for the purpose of starting a business that resulted from those expenses.

There are certain loan programs that target specific groups. The SBA prequalification loan program, for example, is open to women, minorities and veterans. Like any other loan, the applicant must show that he or she can pay back the loan and it must be paid back.

There are grant programs for people with disabilities. The Veterans Administration will provide grants, generally less than \$35,000 to disabled veterans and the Connecticut Bureau of Rehabilitation Services can provide up to \$10,000 to their clients to start a business. In both cases a Connecticut Small Business Development Center counselor must approve the business plan and in both cases the applicant must be otherwise unemployable. The goal of these programs is to get people off of public assistance.

There are grants available from time to time for economic development purposes. These are conditional grants in that the business must do something

that helps the economy. States or municipalities through their economic development offices generally run them. Examples are:

- Brownfield grants offset the cost of environmental clean-up necessary for a new business to build on a polluted site. These cover only the clean-up costs. The State Department of Economic and Community Development runs this program in cooperation with the municipality.
- Training grants to offset the cost of training skilled workers. These grants usually require the creation of several new jobs and cover only a part of the training cost. These are common for manufacturing companies in cities such as Bridgeport.
- Tax abatements (reductions in state income or local property tax) to encourage the new construction or jobs.
- Façade grants of up to \$2,000 for exterior improvements to buildings in targeted areas.
- Disaster recovery grants. For example, after the World Trade Center disaster, New York City offered \$50,000 to any business willing to locate in lower Manhattan. Disaster recovery grants are not a good idea for small business as operating in areas recovering from a disaster can easily result in significant financial losses in the first years.
- State economic development grants to attract large employers to economically depressed areas. These cover only part of the cost of the project and are administered in partnership with the municipality. As an example, Pfizer received state grants that covered approximately 4% of its development costs as an incentive to locate its global research headquarters in New London.

Small businesses rarely qualify for grants and no grants cover more than a small fraction of expenses. For the truth about grants, please visit <http://www.sba.gov/expanding/grants.html>. For a complete listing of federal grant programs, visit www.firstgov.gov

How to Get a Business Loan

Of all the requests for assistance received at the Middletown Small Business Development Center, the



majority seeks assistance in securing loan financing. Borrowing money is something nearly every small business must do at some time. Most entrepreneurs do not really know how to go about that because it is a once in a lifetime ordeal – they have no experience to draw on. The MSBDC has helped secure financing by putting together “loan packages” for lenders to evaluate.

Lenders want to make loans; that’s how they make their money. However, lenders cannot afford to make bad loans – one bad one takes the profit from forty equal good ones to break even. Bankers have a responsibility to preserve their depositor’s money, so they are not risk takers. You must prove that your plan is low risk.

There is no substitute for a comprehensive business plan. You need to provide your Lender with the proper information needed to evaluate your request. You must clearly show what the loan will be used for, that it is necessary and that it is the right amount. That information must be stated in writing, in a logical, concise, well-designed business plan. Remember that you or the management team you are part of is the most important factor to lenders and investors and deals are made or lost on that issue alone. You must qualify in two areas:

1. **Business Management Capability:** The plan must demonstrate that you have the ability to execute it. You must show that you can manage a business, market your products, generate and interpret financial reports. Describe business systems and show training and policy manuals
2. **Industry Capability.** Closely related to management capability is how it relates to what you plan to do. Demonstrate that ability by providing a complete description of the industry, your company, product(s), market, competition, marketing plan, and location. Even more important is the details of your experience and training in the industry. Evaluate your position in industry and relative to the competition realistically and factually. Do not knock the competition; they must be doing something right. Invite the lender to meet you where your business is being created or already exists. This establishes credibility.

In addition, you should understand how lenders operate. Ask your MSBDC counselor, accountant, attorney, or business associate to recommend a bank or loan officer who has granted loans to others in your situation and

industry. Banks have different underwriting requirements and familiarity with certain types of business.

Understand the lender. Like you, he or she has many customers and may not be as familiar with any one (you!) as you would like. The loan officer may ask questions that are clearly answered in the materials you already submitted. Be patient. What may seem like silly questions is only the banker trying to get to know you.

Finally, be patient: Do not expect the lender to review your proposal and make a decision overnight. The longer you have to wait, the better, because you have not been rejected. You want the lender to view you as someone with a vision and ability to achieve it, rather than someone who has an immediate crisis and is running out of money. Do not rush the decision or you will look desperate.

The Six C's

Lenders evaluate loan applications on the following factors. Your application must satisfy all of them.

CHARACTER – Your credit history, community and business reputation. They are lending the money to you and depending on you to make the payments.

CAPACITY – Your source to repay the loan must be the business' cash flow or you should not be taking out a business loan. This must be proven in the business plan.

CAPITAL – You must invest in your own proposal before you can expect anyone else to back it. Your financial commitment is the business' starting net worth. Generally, you must provide 20-25% of the start-up capital. This can be material as well as money, but not “sweat equity”.

COLLATERAL – There must be a significant part of that net worth that has market value if the business fails. Your loan officer must always consider the worst-case scenario. Sometimes a co-signer with sufficient assets will fulfill the collateral requirement. A co-signer, however, will not make up for a flawed business plan.

CAPABILITY – Is there sufficient management skill and industry expertise?

COVERAGE – Your income projections must cover the debt comfortably (at least twice).

Credit Reports

Credit history is underlined above because that is one of the first things a lender will check and anything other than a good credit report (a credit score of at least 700) will cause your loan application to be rejected. Bankers rightfully believe that, if you don't pay your bills on time, you will not pay a business loan on time either.

You can owe money to several creditors, such as credit cards, and still have good credit. You must only not exceed the credit limit on the card and make the minimum payments, on time. A late payment has the same effect on your credit rating as not making the payment at all.

There is no way you can hide any payment problems in your past. They were all reported to the credit bureaus as they happened. The MSBDC can still work with you, but you should be honest about your credit history with your counselor. There are many ways to launch a business in spite of bad credit, but a bank loan is not one of them.

If you have corrected any credit problems and paid the debts as agreed, you should make sure that your credit report reflects that. You can get a copy of your credit report from any or all of the three credit bureaus listed in the reference section of this booklet. We recommend that everyone check his or her credit report and get their credit score before they apply for a loan.

Buying a Business

Many people become entrepreneurs by purchasing a business instead of starting one. A smart buyer puts the business through a careful examination before making an offer and an even more detailed examination before the sale closing.

Sellers are rightfully unwilling to disclose the confidential details of their business to anyone but a serious, qualified buyer. An interested buyer will be allowed to tour the premises and will be provided with whatever financial figures the seller is comfortable disclosing. At the very least, the seller will have to reveal three years of summary profit and loss data, the amount of business debt the buyer is expected to assume and the existence of pending events that may adversely affect the business.

If the buyer wishes to proceed with a purchase, he or she must make an offer for a certain purchase price and then provide the seller with some proof of qualification – that is the buyer’s financial capability to make good on the offer. This offer should be conditional and is sometimes called a “Letter of Intent” and must be countersigned by the seller for the deal to proceed.

The Letter of Intent should stipulate the buyer’s conditions in as broad a statement as possible. These conditions should include:

- Subject to buyer’s ability to secure suitable financing at no higher than a specified rate of interest. Seller may insist on a time limit of this or not agree to the Letter of Intent until financing is arranged so the seller is free to sell the business to other prospects.
- Subject to verification of income and expense. This requires the seller to provide audited statements and tax returns.
- That there are no outstanding debts or judgments other than those in the normal and customary course of business.
- That the business is in good legal standing and regulatory compliance.
- That the equipment, building and other assets of the business are in good, serviceable condition.
- That the business is not in default of any leases and contracts and that the leases and contracts are assignable to the buyer. This requires that the buyer is allowed to examine all leases and contracts.
- That the seller has the right and title necessary to make the sale.
- That the Buyer will execute a confidentiality agreement and then seller will make available to the buyer all business records for examination and provide releases for any professionals used by the business, such as accountants.

If the seller accepts the offer, the buyer is given a time before the deal closes to do a thorough examination of the business and all of its records. This is called “Due Diligence”. The purpose of this investigation is to discover any deal-breakers and to become familiar with the business the buyer is going to operate.

The final step is the closing. The parties execute a Purchase and Sale Agreement. That agreement should hold both buyer and seller to written warranties of all of the material representations they have made during the acquisition process.

Franchises

At some point, you may consider buying a franchise as an alternative. Buying a franchised business is a special case of starting your own business. It has some of the advantages and disadvantages of both owning your own business and of working for someone else.

The company that sells you the franchise is called the Franchisor and you become one of their franchisees. You do not have to create the business, they already have. You follow their business plan and operating procedures. The only planning you do is usually the weekly ordering and staffing. For all of the thinking they do for you, the Franchisor will get 5-10% of your sales plus other fees, such as marketing.

Purchasing, marketing promotions, record keeping and accounting systems are determined by the Franchisor. In many cases, the Franchisor provides a good part of the financing of starting your business, but you still will have to put up \$5-100,000, depending on the business.

All you really get with a franchise is a license to use their systems. You may have little actual control over the destiny of the business, so it's a lot like buying a job. On the other hand, you may make a lot of money without all of the hard work of creating a business.

To properly evaluate a franchise opportunity, you should do a thorough investigation, including:

- Examine the Uniform Franchise Offering Circular. This is the actual deal and the Franchisor is required to provide it to you.
- Look at all other contracts. Verbal statements the Franchisor makes at meetings are not binding, contracts are.
- Talk with existing Franchisees to confirm sales projections and the trustworthiness of the franchisor. Be warned that they do not have to tell you the truth and may be contracted against saying anything disparaging, so call several and listen to what is not said as well as what is.
- Ask for sales, costs and expenses. Do not expect any projections; franchisors are prohibited from providing them.
- Observe the operation of an existing franchise. Is that what you want to do and the way you want to do it? You have little chance

to change things once you buy the franchise and will be doing it their way for a long time.

- Remember that the products or services are not as important as the integrated business system, which is all that differentiates the franchise from its competition. Just how good is this system you are licensing at running a business?

Starting a Business Checklist

Don't quit your day job until you....

- Complete the vision into a complete, integrated system for doing business.
- Do a personal need assessment. Just how much money do you need to live on each month?
- Find a source for health insurance on you and your dependants, include the cost in your personal needs.
- Compile a complete list of what you need to start the business, accurately priced.
- Come up with a marketing plan.
- Design systems to run the business so it does not run your life.
- Based on solid fact and research, compile the income, cost and expense projections for the business, month-by-month, for at least three years.
- Have a solid plan to secure all operating licenses and permits. **But** do not get sales or income tax accounts until you need them.
- Understand and be prepared to handle taxes and regulations that apply to your business. Check with Zoning, Building, Fire Marshal and Health Department.
- Compile a list of contacts and advisors. Include the ones you have at work if that does not violate a non-compete agreement.
- Finish a business plan. It must include all of the above.
- Get a lawyer and an accountant

- File Necessary Papers to create the business with Town Clerk or Secretary of State.
- Establish a line of credit. You will not get a home equity loan after you quit your day job. Likewise, apply for necessary credit cards before you quit.
- Get legal with your software. You will need technical support.
- If you can, start your business part time, after hours to test the concept.
- Plan your exit from your job. You may need to work just a little longer to qualify for benefits. Do not burn your bridges. Everyone you work with is a potential customer or referral agent. Telling your boss to shove it is a bad idea.

References & Resources

AT THE LIBRARY

Search the materials file by subject, such as business, management, marketing or small business. You can also search the directories at bookstores and online vendors, such as Amazon, for books to buy or request from your library.

Among the facilities at the reference desk, you will find:

A Professional Reference Guide - An excellent starting point, providing a list of trade associations and organizations. Those organizations are a great source of information on your industry.

Data Sources for Business and Market Analysis – Sources of market data

Encyclopedia of Business Information Sources – Lists handbooks, periodicals, directories, and trade associations on more than 1200 specific industries and business subjects. It is a good starting point to search for information on a particular business.

Small Business Sourcebook – Guide to the informational services and sources for over 100 different types of small businesses.

Encyclopedia of Associations – Trade and professional associations throughout the United States that can help existing business owners keep abreast of industry developments, and provide start-up business owners

with valuable market information. Most associations will readily work with start-up business owners.

National Trade & Professional Associations of the United States – Similar to the Encyclopedia of Associations, this lists trade and professional associations throughout the United States.

Simmons Study of Media and Markets – A comprehensive market survey of media audiences and product use in the United States. It provides detailed information on over 100 products categorized by different demographic criteria.

Acorn Consumer Classification System – Segments potential customers by consumer type based on many criteria including age, wealth, location, and spending habits.

Demographics USA – Provides information on population, ethnicity, age/sex groupings, household related data, consumer expenditure, employment, and occupation data.

Standard Industrial Classification Manual – This lists the SIC numbers issued to major areas of business. These numbers are the key to unlocking census data and are used as the basis to determine workman's compensation pricing category.

Business and Industrial Financial Ratios – Updated yearly, it contains IRS data on 37 million United States corporations. The data is organized by industrial groups and provides comparative historical information on key financial criteria. Other publications that provide the same type of information are the *RMA (Robert Morris Associates) Annual Statement Studies*, the *FRA Financial Studies of the Small Business*, and the *Industry Norms and Key Business Ratios*.

Standard & Poor Industry Surveys – Updated industry statistics and analysis

U.S. Industrial Outlook – Provides overview, forecasts, and short profiles for 200 American industries including recent trends and a five-year outlook.

Statistical Abstract of the United States – Updated annually, provides demographic, economic, and social information.

City and County Data Book – Updated every three years and contains statistical information on population, education, employment, income, housing, and retail sales.

American Business Climate & Economic Profiles – A concise compilation of facts, rankings, incentives, and resource listings for all 319 Metropolitan Statistical Areas (MSA) in the 50 states.

Dun and Bradstreet Directories – List companies alphabetically, geographically, and by product classification. Good for researching competitors and potential consumers.

The Thomas Register – Detailed information under more than 52,000 separate product and service headings. This manual lists capabilities and contact headings on more than 148,000 U.S. companies.

Predicasts F&S Index – Short abstracts on U.S. companies, products, and industries. Indexes trade associations, government, and specialized business service publications.

Marketing Information Guide – Provides a monthly-annotated bibliography of marketing information.

Seasons of Business: The Marketer's Guide to Consumer Behavior (1992) – Helps companies to understand what seasoned factors shape customers buying decisions.

The Green Book – International directory of marketing research companies and services.

On CD-ROM:

American Business Disc - Basic information on U.S. companies of all sizes. The CD allows you to search by different criteria, such as: SIC code, geographic location, company name, company sales volume, and number of employees.

ABI/Inform - Business periodical references with abstracts searchable by industry, subject, and keyword. Contains articles from 1971 to present.

Business Dateline - Contains the full text of articles from nearly 180 regional business magazines, daily newspapers, and wire services.

National Trade Data Bank- Operated by the U.S. Department of Commerce Economic and Statistics Administration. The data bank contains trade promotion information, investment statistics, and international economic data from approximately 20 federal agencies.

CREDIT BUREAUS

Equifax: 1-800-525-6285

www.equifax.com

Experian (formerly TRW): 1-888-397-3742

www.experian.com

Trans Union: 1-800-680-7289

www.transunion.com

www.myfico.com – One credit report, credit score and credit tips for \$14.95

There may be a fee for these reports. You will also have to provide positive identification, which may include the amount of your last payment to one of your creditors, so have your checkbook handy.

If you discover credit problems on your report that are not your doing, you may be a victim of identity theft. Notify the credit bureau immediately. If you confirm that you are a victim of identity theft, notify the Social Security Administration Fraud Unit at 1-800-269-0271.

To prevent identity theft, never give personal identification information, such as your social security number, to anyone unless you know who they are and that they have a valid reason to ask for it. Never put such information on an email.

FEDERAL RESOURCES

U.S. Citizenship and Immigration Service (division of Homeland Security)

Employer Information

<http://uscis.gov/graphics/services/employerinfo/index.htm>

I-9 Form <http://uscis.gov/graphics/formsfee/forms/files/i-9.pdf>

Internal Revenue Service

Home Page: www.irs.gov

An easy to use site with downloadable guides, forms and instructions. To view or print the files, you need Adobe Acrobat. You can download it free at <http://www.adobe.com/products/acrobat/readstep2.html>

Useful Internal Revenue Service Materials

Available on line or at the local office

Small Business	Publication 583 <i>Starting a Business and Keeping Records</i> Publication 17 <i>Your Federal Income Tax</i> Form SS-4 <i>Application for Employer Identification Number</i> Circular E <i>Employer Tax Guide</i> Publication 533 <i>Self Employment Tax</i> Publication 587 <i>Business Use of your Home</i> Publication 3702 <i>Small Business resource Guide</i> (CD/ROM)
Sole Proprietorship	Publication 334 <i>Tax Guide for Small Business</i> Schedule C and Instruction
Partnership	Publication 541 <i>Partnerships</i> Form 1041 and Instructions
Corporations (C)	Publication 542 <i>Corporations</i> Form 1120 and Instructions
S Corporations	Publication 542 <i>Corporations</i> Publication 2553 and Instructions Form 1120S and Instructions

TATE RESOURCES

Connecticut Department of Labor

www.ctdol.state.ct.us

State Office (new hire reporting)

Connecticut Department of Labor
Office of Research, Attn: CT-W4
200 Folly Brook Boulevard
Wethersfield, CT 06109
Fax: 1-800-816-1108

Department of Revenue Services

25 Sigoney Street
Hartford, CT 06105

www.drs.state.ct.us

Useful Department of Revenue Services Materials

Available on line or at the local office

REG-1 Business Taxes registration Application

QS-114 Sales tax Return

0-88 Instructions for Sales Tax Return

IP2000 Getting Started In Business

Connecticut Circular CT, Employers Tax Guide

IP 99(19), Building Contractors' Guide to Sales and Use Taxes

Informational Publication 2003(15) Q & A on Business Entity Tax

Connecticut Economic Resource Center, Inc.

1-800-392-2122 www.cerc.com *Note:* some services are fee-based

- **Smart Start** Licensing Assistance (www.ct-clic.com or www.CTSmartStart.com)
- **Site Finder:** Database of Connecticut's available commercial and industrial properties. www.CTSiteFinder.com
- **Geographic Information System:** demographic and business information through maps
- **Demographics:** census data including county, zip code, and census tract
- **Economic and Demographic Analysis:** industry profiles, competitive intelligence, survey research, benchmarking, and evaluation
- **Business Lists:** lists of foreign-businesses
- **Business Resource Index:** federal, state, local, and private resources

ConnStep – Lean Manufacturing Training (fee) www.connstep.org

Other Connecticut Agencies

WBDC (Women's Business Development Center, Stamford 203-353-1750

CEDF (Community Economic Development Fund)800-656-4613

ACCESS Entrepreneurial Center, Willimantic.....860-450-7146

Gateway Entrepreneurial Training Prgm, Gateway Community College,

New Haven RBDC (Regional Business Resource Center).....203-624-1493
Hartford Economic Development Corp.860-527-1301
Mile Program, New London860-482-1136
SECTOR (Southeastern CT Enterprise Region), New London888-673-2867
CT Innovations (high-tech), Rocky Hill.....860-563-5851
Child Care Facilities Microloan Program, New Haven.....203-776-6172

ASSOCIATIONS

American Marketing Association www.marketingpower.com
250 Wacker Drive, Suite 200
Chicago, IL 60606

Publishes annotated bibliographies on marketing topics and has an alphabetically arranged directory of marketing research firms and services.

International Council for Small Business www.icsb.org
U.S. Association for Small Business and Entrepreneurs
905 University Avenue, Room 203
Madison, WI 53715

A Professional organization for educators and entrepreneurs interested in the development of a small business.

National Association of Women Business Owners (NAWBO) www.nawbo.org
1377 K Street NW, Suite 637
Washington, D.C. 20005

Helps broaden opportunities for women in business. Offers workshops and seminars providing information and referral services to members, and maintains a database of women-owned businesses.

National Federation of Independent Business www.nfib.com
600 Maryland Avenue SW, Suite 700
Washington, D.C. 20024

The country's largest small business association; it has more than 500,000 member business owners. In addition to representing small business interests to state and federal governments, it distributes educational information and publications, and holds conferences.

INTERNET SITES

Learning about the internet and how to use it:

Learning the Net: <http://www.learnthenet.com>

Internet Terms: <http://www.netlingo.com>

Internet Reference: <http://www.refdesk.com/>

Search The Web: <http://www.google.com>

E-Commerce: <http://www.sbasupport.org>

Internet Search Strategies

Noodle Tools:

<http://www.noodletools.com/debbie/literacies/information/5locate/adviceengine.html>

Georgetown University Library:

<http://www.library.georgetown.edu/internet/effectiv.htm>

Small Business Training

Workshops: <http://www.va-interactive.com/MSBDC/>

Business Legal Forms:

http://www.inc.com/guides/solo_business/20676.html

Start-Up Guide:

http://www.sba.gov/starting_business/startup/guide.html

Managing Cash

http://www.mastercardbusiness.com/assets/brochure/smallbiz/manage_cash_flow.pdf

Writing a Business Plan: http://www.inc.com/guides/write_biz_plan/

Sample Business Plans: <http://www.bplans.com> or

<http://www.businessplans.org/businessplans.html>

Business Plan Workbook:

http://www.mastercardbusiness.com/assets/brochure/smallbiz/develop_business_plan.pdf

Management and Franchise Info: www.entrepreneur.com

Small Business Resources: www.sbaer.uca.edu

Young Entrepreneur's Organization (under 40): www.yeo.org

Business Management

American Management Association: www.amanet.org

Global marketplace Risk Assessment:

www.assessyourinternationalrisk.org

Business Financial management: www.business-literacy.com

Woman owned Business: www.womensbusinessresearch.org

Best for Business: <http://www.bestforbusiness.com/>

Business Owner's Toolkit: <http://www.toolkit.cch.com/>

Commerce Clearinghouse (tax, human resources): <http://www.cch.com>

Federal Agencies (for information and to use their services)

U.S. Government Business resources: www.business.gov, or

Regulations and Directory: www.firstgov.gov

Export Assistance and Training: www.export.gov, or

International Trade & Technology: www.usgtn.net, or

International Trade Organization: <http://www.ita.doc.gov/>

The U.S. Census Bureau: www.census.gov/

Demographic Data: <http://homer.ssd.census.gov/cdrom/lookup>

Small Business Administration: www.sba.gov (resource listings for every state)

The SBA defines a Small business as one that is under:

- 500 employees for most manufacturing and mining industries
- 100 employees for all wholesale trade industries
- \$6 million for most retail and service industries
- \$28.5 million for most general & heavy construction industries
- \$12 million for all special trade contractors
- \$0.75 million for most agricultural industries

Office of the SBA Inspector General:

www.sbaonline.sba.gov/ignet/ig.html

U.S. Department of Labor (Labor Law Information):

www.dol.gov/elaws/firststep

The Bureau of Labor Statistics: <http://stats.bls.gov>

U.S. Department of Commerce: www.commerce.gov/

Office of Business Liaison: <http://www.osec.doc.gov/obl/>

United States Patent and Trademark office: www.uspto.gov

U.S. Copyright Office: www.copyright.gov

Selling to the Federal government: www.fedbizops.com

Connecticut Agencies

A complete listing of Connecticut agencies can be found at:

www.ct.gov

Company and Industry Information:

Hoovers: <http://www.hoovers.com>
Dun & Bradstreet: <http://www.dnb.com>
Industry Links: <http://www.industrylink.com/>
Associations Gateway:
<http://info.asaenet.org/gateway/OnlineAssocSlist.html>
Industrial Newsroom – Optics & Photonics:
http://www.industrialnewsroom.com/news/optics_photonics
Industry Links: <http://www.competia.com/express/right.html>
Public Records: <http://www.brpub.com/pubrecsites.asp>
Industrial Research Institute: <http://www.iriinc.org/webiri/index.cfm>
Web Page Change Monitoring: <http://www.WatchThatPage.com>
Interesting Company Analysis: <http://www.footnoted.org/index.html>
Business Research: <http://business-research.info/business-research-links.htm>
BizStats: <http://bizstats.com>

Financial Information Sources:

IPO Monitor: <http://www.ipomonitor.com/>
Ten K Wizard: <http://www.tenkwizard.com/>
SEC Edgar: <http://www.sec.gov/edaux/searches.htm>
FindArticles: <http://www.findarticles.com/PI/index.jhtml>
Yahoo Finance: <http://finance.yahoo.com/?u>
Quicken: <http://www.quicken.com/>
Morningstar: <http://www.morningstar.com/>
Bloomberg: <http://www.bloomberg.com/>
Financial Analysis and Spreadsheets:
<http://pages.stern.nyu.edu/~adamodar/>
Financial Data: <http://bigcharts.marketwatch.com/>
The Scannery: <http://www.thescannery.com/>

News Sources:

ABC News: <http://abcnews.go.com/>
Rocket News: <http://www.rocketnews.com/search/index.html>
Newspapers Online: <http://library.uncg.edu/news/>
The American City Business Journals: <http://www.amcity.com/>

New York Times: <http://www.nytimes.com/>

Newspaper Links: <http://www.newspaperlinks.com/>

Boston Globe: <http://www.boston.com/globe>

Forbes: <http://www.forbes.com>

Individual.com: <http://www.individual.com>

NewsAlerts:

<http://www.marketwatch.com/news/default.asp?siteid=mktw>

Feedster News Search: <http://www.feedster.com/>

Worldwide Newspaper links: <http://www.thepaperboy.com>

Blogs (a great source for inside information on the competition):

Blog Searches: <http://www.bloglines.com/> or

<http://www.technorati.com/index.html>

Search Engines:

AlltheWeb: <http://www.alltheweb.com/>

Google: <http://www.google.com/>

Alta Vista: <http://www.altavista.com/>

Vivisimo: <http://vivisimo.com/>

Gigablast: <http://www.gigablast.com>

Public Documents Search Engine: <http://www.searchsystems.net/>

Portico Industry Searches: <http://indorgs.virginia.edu/portico/>

General Reference and Directories:

Wikipedia global user-created encyclopedia:

http://en.wikipedia.org/wiki/Main_Page

Connecticut State Library: <http://www.iconn.org/>

Global Edge: <http://globaledge.msu.edu/ibrd/ibrd.asp>

Britannica Online: <http://www.eb.com/>

Columbia Concise Encyclopedia: www.encyclopedia.com/

Refdesk.com: <http://www.refdesk.com/>

UCSD Reference desk: <http://libraries.ucsd.edu/refshelf.html>

Corporate Library: <http://www.thecorporatelibrary.com/>

CEO Express: <http://www.ceoexpress.com/default.asp>

CI Seek: <http://ciseek.com>

Internet Public Library: <http://www.ipl.org/ref/index.text.html>

American Society of Executive Associations: <http://info.asaenet.org>

Librarian's Index to the Internet: <http://lii.org/>
Information on People: <http://www.ZoomInfo.com>
Melissa data (mailing lists, market statistics): <http://melissadata.com>
Zapdata (mailing lists, market statistics): <http://zapdata.com>
Information Please: <http://www.infoplease.com>
Miser: <http://www.umass.edu/miser>
ResearchBuzz (What's new on the net?): <http://www.researchbuzz.com/>

Government Information & Public Records:

US Government Portal: <http://www.FirstGov.gov>
Public Records: <http://www.searchsystems.net/>
State & Local Records: <http://www.StateLocalGov.net/index.cfm>
News About All the States: <http://www.stateline.org>
Reports from Government, Think Tanks and Non-Government
Organizations:
<http://www.Docuticker.com>
Non-Profit Organizations: <http://www.guidestar.org/>

Trade Shows:

Trade Show Database: <http://www.tradeshowdatabase.com/index>

Patent & Technology Resources:

Patent and Trademark Office: <http://www.uspto.gov>
Patent Café: <http://www.patentcafe.com/directory/directory.asp>
World Patents: <http://www.pcug.org.au/~arhen/>
European Patents: <http://www.espacenet.com>
Japanese Patents: <http://www.jpo.go.jp>
World Intellectual Property Organization: <http://www.wipo.int/>
Prior Art Database: <http://ip.com> -- or --
<http://www.priorartdatabase.com/>
National Science Foundation: <http://www.nsf.gov>
Science Central: <http://www.scicentral.com/>
Patent Alert: <http://www.patentalert.com/>
Business & Technology: <http://www.brint.com/links/>
Wiley Interscience: <http://www3.interscience.wiley.com/cgi-bin/home>
Metric Group Patent Citations Tool: <http://www.patentcitations.com/>
R&D Magazine: <http://www.rdmag.com/scripts/default.asp>

Competitive Intelligence:

Competitive Intelligence Sources:

<http://web.syr.edu/~jryan/infopro/intell.html#top>

Competitive Intelligence Information Sources:

<http://www.andrew.cmu.edu/user/adele/45790y.html>

Finding People:

Find People: <http://www.journalismnet.com/people/>

Phone numbers: <http://www.411locate.com/>

Phone Numbers: <http://www.anywho.com/>

Connecticut Capital Sources

www.ct-venture.org

www.ctinnovations.com

www.cda.state.ct.us

www.ace-net.sr.unh.edu

www.secter.org

www.cedf.com