

ENTP 6020: BUSINESS PLANS & SEED FINANCING

Bard Center for Entrepreneurship
University of Colorado Denver

Professor John Ruhnka

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Office Hours: Tues/Thurs 3:00-4:00 P.M., or we can meet at the Bard Center before or after class.

Required materials: (1) *The Successful Business Plan: Secrets & Strategies* by Rhonda Abrams, 4th Edition (the Planning shop, Palo Alto, CA; ISBN 0-9669635-6-3); (2) CD Rom "*Business Plan Pro 11.0*" (standard) by PaloAlto Software, order direct from www.paloalto.com/ and use your UCD student email address with an .edu ending for ordering. It is also available to students on the Bard Center computers. An optional but very useful resource is *Successful Business Research* by Rhonda Abrams (the Planning Shop, Palo Alto, CA; ISBN 13:978-0974-08013-0) which tells you how to use the web and available data bases to find target market and industry information for a wide variety of industry and service areas. I will bring my copy to class to loan out, but if you are serious about a business plan, you will want a copy for yourself. Also check out the website of the UCB entrepreneurship program at <http://Leeds.colorado.edu/BPlan> which has business plan templates, spreadsheets, sample plans, and lecture notes by Prof. Steve Lawrence and Frank Moyes for you to use. I use *Business Plan Pro* software because it is #1 rated and uses formats that most lenders, Angel investors and VC's expect. It operates in Word, Excel, and PowerPoint and will import Excel spreadsheet calculations (and even photos) into your business plans. I will post copies of many of the handouts in class as well as PowerPoints used in class on the **Blackboard** web site for this course.

Course Objectives

This course teaches the process and the key steps for preparing a business plan for a new (or existing) business venture. A business plan is an essential tool in planning an entrepreneurial venture and integrates an analysis of the potential demand for the product or service and the potential customers, identifying and generating critical competitive advantages, the proposed marketing, pricing and competitive strategy, how the product or service will be produced; the proposed legal structure and financing sources for the new venture, generates the projected financial results, and describes the team needed to manage the business. A business plan serves several different critical functions:

- 1) It serves as a feasibility assessment and a proof of concept for a potential business opportunity that can be used to pre-test and to avoid unprofitable/unworkable ideas, and to improve the commercial viability of a concept before it is launched.
- 2) It is an iterative process for testing an initial idea for a new business and developing a workable steps in an operational plan.
- 3) It is a financial plan that identifies the resources required to execute the concept, the projected sources, cost and timing of the funding required for the venture, and the projected profitability.
- 4) It identifies the specific management skills needed to execute the concept and when those skills will be needed; and it is also a sales tool for selling potential management team members on the business concept.
- 5) It is a sales document for the investors or lenders who will provide funding for the new venture, demonstrating the commercial feasibility and financial returns of the concept, and showing that due diligence and proof of concept has been performed by the venture team.

- 6) The business plan is also the first step in producing an annual plan of operations and a milestone plan and that will be used as the operational roadmap for the new enterprise.

How Objectives Will Be Met

The objective of this course is to learn the techniques for preparing a business plan for a new venture through sharing the experiences of entrepreneurs and investors who have been through the process; by analyses of new business opportunities and case studies; and, most importantly, by either writing your own business plan or assisting others in the preparation of a business plan for a proposed new or existing business.

Meeting Practitioners and Bard Center “Mentors”

I will invite a dozen founders, practitioners and investors in start-up businesses to share their experiences with us over the course of the semester (including former students in this course who have won the Bard Center Business Plan Competition and who have gone on to start their own business), so that we can compare their experience in starting-up a businesses, strategic planning and financing against our textbook models. The Bard Center can also pair you up with a "mentor" from the Bard Center Advisory Board with whom you can discuss your ideas for a new venture. If you are interested, please contact Cathy Kunst, Executive Director of the Bard Center.

Constructing a Business Plan and the Bard Center Business Plan Competition

The central element of this course is the preparation (and presentation) of a business plan for a new (or existing) venture; both a 15 minute PowerPoint presentation to the class and a formal written business plan. This may be done individually, or by teams of 2-4 students who collaborate on one idea. Students who do not wish to take the lead on a business plan may team up on the business plan of a classmate, or may help to develop a business plan for several entrepreneurs and non-profits who will present their ideas to the class to interest students in developing a business plan for them. A draft of the "target market and competitive analysis" section of your business plan is due mid-way through the course, to help focus your BP development and so that the instructor can assist you with feedback and suggestions. All Business Plan students are eligible to submit their business plans to the outside referees who will select six finalists for the Bard Center Business Plan Competition to take place on June 10, 2009, and which will feature more than \$27,000 in cash prizes. Students from this course have won many of the awards in past Bard Business Plan Competitions.

Class Schedule and Assignments

<u>Session</u>	<u>Topic/Class Activity</u>	<u>Assignments</u>
Jan 22	Overview and Introduction	
	What <u>is</u> a <i>successful business</i> ? Different types of entrepreneurial businesses “Stages of development” of new ventures, risk profiles, and new business survival rates. Guest speaker – Jung Park (2004 Business Plan Competition winner)	TSPB Ch.1 <i>The Successful Business</i>
Jan 29	The Business Plan and Its Functions	
	The different functions of a Business Plan	TSBP Ch. 2 <i>Getting Your Plan Started & Ch.3 Making Your Plan Compelling</i>

What are the functions of a Strategic Plan and do you need one?

- How do you perform a strategic analysis?

Guest speaker – Tiffany Espinosa (2005 Business Plan Competition winner)

**Feb 5 Desirable Characteristics for New Business Concepts;
Ideal “Model Business” Parameters**

Handout *Opportunity Recognition*

John Morse case handout

- Classifying new concepts by growth potential (differentiating "mom & pop businesses" from potential IPO's)
- Identifying key feasibility indicators for success - and “good-bad” ranges for them
- What are potential “fatal flaws” to watch out for in new business concepts?

Guest speaker – Dave O'Brien, The Business Catapult

Feb 12 Opportunity Screening and Evaluation

TSBP Ch. 6 *Industry Analysis & Trends*;

Ch. 7 *Target Market*

Handout *Screening Venture Opportunities*

1st case due: John Morse

Evaluating and developing the new venture idea:

- How do entrepreneurs “find” new venture ideas? The importance of personal “fit” and timing.
- New businesses that recognized a specific market need and filled it.
- The importance of identifying competitive strengths:
 - price
 - quality
 - service

Class discussion of John Morse case

Feb 19 Market Research and Competitive Strategy

Market Research

TSBP Ch. 8 *Competition*; Ch. 9 *Strategic Position & Risk Assessment*; Ch. 10 *Marketing Plan & Sales Strategy*; Handout: *Market and Competitive Analysis; Developing a Marketing Plan and Competitive Strategy*

Voice Concepts case handout

The critical importance of market/competitive analysis and how to use it to develop your competitive strategy

- What is your "target market"?
- What are the present market size and growth rates?
- What is the potential market size and potential market niches?
- Existing and potential competition (features, price, & your potential concept copycats)
- Sources of data and research methods for assessing market and competitive factors.
- How do you deal with undeveloped markets or with missing information?

Market Penetration and Competitive Strategy

- What does a "market share" map of your target market look like? Are your potential customers available, or are they locked up?
- How can you differentiate your product/service from the competition?
- Different market penetration strategies.
- Competitive strategies to deal with existing or projected competition.

Guest speaker:

Feb 26 Assembling the Venture Team & Producing the Product or Service

TSBP Ch. 11 Operations; Ch. 12 *Technology Plan*;
Ch. 13 Management & Organization
Handouts: *The New Venture Team*;
Advisory Boards
2nd case due: Voice Concepts

The critical importance of the management team and incentivizing the team:

- How to do a management skills requirements analysis for a new venture.
- What skills are needed and when; which management functions can wait until later?
- What skills do you need in-house and which can be contracted-out?
- Management styles and the importance of building a team.
- Performance incentives: management compensation & reward structures
- How can you assemble and use an "Advisory Board"?

Producing the product or service:

- What will customers actually pay for your product or service? How can you find out?
- Can you avoid multiple distribution layers with their added mark-ups?
- The critical importance of high Gross Profit Margins for financial viability.
- The need to deal with unanticipated problems: changing plans in mid-stream to adapt to unanticipated problems, or "repositioning" of a product or service to adapt to changed market or competitive conditions.

Guest speaker

Mar 5 Structuring a new venture and Legal Issues

Handouts: *New Venture Legal Issues*;
Obtaining Web Domain Names
**1ST Draft of Market & Competitive Analysis for
your Business Plan is due!**

- Identifying the key legal issues for the Entrepreneur
- Advantages and disadvantages of various legal entities for a business
 - Personal and investor liability issues
 - Ease of adding investors/raising equity capital/transfer of ownership
 - Tax consequences
 - Suitability for an eventual public offering of stock
- The critical importance of a "clear" product name, trade name & domain name
- Protecting intellectual property and trade secrets: confidentiality/nondisclosure agreements; non-compete agreements
- How to select and use a lawyer

Guest speaker: Sam Cheris

March 12 Resource Needs and Financial Projections

TSPB Ch. 16 *The Financials*

Handout: Resource Needs & Financial Projections

Article: *How much money does your new venture need?*

Article: *Look at the Cash*

Article: *How to Read a Financial Report*

- The function (and limitations) of financial projections in a business plan; and why it is important to *nail your costs*.
- How your market assumptions and operating assumptions drive the financial assumptions and resulting financial projections.
- How the income statement and balance sheet interrelate.
- The critical role of cash in new ventures and how to perform a cash flow analysis.
- The importance of break-even analysis.
- Importance of pricing a product or service and the dangers of underpricing.

Guest speaker:

March 19 Sources of Financing for New Ventures

TSPB Ch 15 *Development, Milestones & Exit Plan*

Handout: *Sources of Financing for New Ventures*

- The necessity of matching financing sources to the projected growth and resource needs of the venture, and the need for “exit vehicles” for your investors.
- Stages of development and risk profiles of new ventures and appropriate funding sources for each stage.
- An overview of potential funding sources for new ventures and the feasibility of each such source for specific types of ventures
 - Friends & Family investors
 - Reg. D “private placement” investors
 - “Angels”
 - Venture capital investors
 - Initial public offerings
 - SBIDC
 - Bank lending

Guest speaker

March 26 – No Class – UCD Spring Break!

April 2 Private Placements, Initial Public Offerings and Investor Exit Vehicles

Handout: *Reg. D & IPO offerings*

- How Private Placements are structured and sold
- How IPO's are structured and sold
- Advantages and disadvantages of each method of raising equity for new businesses
- The necessity of exit vehicles for private investors and the available options

Guest speaker:

April 9 Buying a Business and Valuing a Business

Article: Valuation Techniques

3rd Case assignment: Michigan Lighting, Inc. – (this case is due on April 23).

- How do VC firms value the new businesses that they invest in?
- The “deal structure” and dividing up the pie.
- Advantages & disadvantages of venture capital funding.
- You can run your business idea through <http://www.startupjournal.com/financing/> and get a “report card” on its attractiveness to VC investors from the Wall Street Journal with suggestions on how to improve it's appeal.
- Remember, buying an existing business is always an alternative to starting a new one; what are some advantages and disadvantages?
- Different methods for valuing a business, and their suitability.

Guest VC: Larry Fenster

April 16, April 23, April 28, April 30 Student PowerPoint Business Plan Presentations

Note: the April 28th Class is on a Tuesday Night at the Bard Center is an make-up class which we are required to have because I am ending the semester a week early. We need this session to cover all student business plan presentations, and I expect everyone to attend.

**** All written Business Plans are due by April 30! ** ***

The final part of the course will consist of 15 minute PowerPoint presentations by the BP teams of their business plans, with comments & suggestions by classmates, Bard Center faculty and Advisory Board “mentors”. This presentation is very helpful if you are thinking of entering the Business Plan Competition, and can produce some very useful last-minute ideas for improving your plan! A formal, written business plan with spreadsheets, exhibits, etc. is due by April 30th.

INSTRUCTIONS FOR PROJECTS & ASSIGNED CASES

Format: all cases should be 1.5 line spacing, in *memorandum form* (To: John Ruhnka, From: Bill Gates, Re: John Morse case) with underlined or bold-face headings and subheadings, and please *number* your pages. Your case analyses should each be 6-8 pages in length and should address each of the questions or issues identified for each case, below. Your business plan format should follow the *The Successful Business Plan: Secrets & Strategies* outline.

Case 1 - John Morse

All of the cases you will be considering are “real”, but several date back to the 1970’s or 1980’s so you need to keep the setting of the case in mind when thinking about the degree of technological advancement of an idea, or whether something is in the market yet. So make recommendations on a 1975 case as if you were in 1975, not in 2008! The John Morse case is set in 1975 and deals with the dilemma of whether an entrepreneur can “find” a new business idea or do they have to wait for the idea to “find” them? Which is more important: “Fit” with the entrepreneur’s abilities? His or her prior experience? Timing? In the John Morse case we find a “wanna-be” entrepreneur attempting to identify a new business to pursue through systematic searching procedures. Evaluate Morse’s approach - addressing the following questions:

- 1) Has Morse come up with too many new business ideas or too few? Explain your answer.
- 2) Rank order the commercial viability of Morse's list of business opportunities on p. 89 of the case based on your opinion of their “fit” for Morse.
- 3) In your opinion did the best ideas come earlier in the search process or later?

- 4) Was there a better way for John Morse to have proceeded in his search for a new venture idea in your opinion? If so how?
- 5) How might the “right” approach for someone else be the same or different?
- 6) What should Morse do next in your opinion - start a new business or get a job?
- 7) Does the Morse case offer any lessons about the process of becoming an entrepreneur?

Case 2 – Voice Concepts

This case is set in 1988 and deals with designing a proposed distribution system for a (then new product) – a “voice card” containing a recorded message from the sender - so that it can sell at a commercially feasible final price to the consumer. The challenge for you is to think of alternate distribution methods for the proposed “voice cards” that can pay enough “mark-up” (cut of the final retail price) for each of the necessary player(s), without putting the retail price so high that no one will buy the product. Please address the following issues:

- 1) What are the potential strengths and weaknesses of the proposed “voice cards”? Would you spend \$10 for a voice card to send to someone else? If not, what do you think is a realistic retail price for a voice card?
- 2) What is the monthly break-even quantity for a Faneuil Hall kiosk operator? Solve using the formula: $BEQ \times Price = Fixed\ Costs + Variable\ Costs$. Use \$9.95 for the retail price; \$3,162 for the monthly fixed costs [consisting of \$2,800 for kiosk operator monthly salary (4 x \$700 week) + \$320 space rent/month + \$41.66 chip recording machine rent]; and \$6.67 per card for the Variable Costs. Hence $BEQ \times 9.95 = 3162 + (BEQ \times 6.67)$. So, $(BEQ \times 9.95) - (BEQ \times 6.67) = 3162$. And, so $BEQ \times 3.28 = 3162$.
- 3) Do you think Voice Concepts has identified a viable “target market”? What do you think is the best target market for the voice cards? What types of advertising and promotion would you recommend to reach this target market?
- 4) Can you suggest an alternate way to distribute “voice cards” that can eliminate some of the “necessary players” and layers of mark-ups - so that the retail price can be lowered to what you consider a commercially-viable price? Could Voice Concepts sell direct to the public and eliminate the requirement for a costly retail sales staff to run the kiosks and message recording machines? How might they do this? What value does Voice Concepts add – if any? Could Omega eliminate Voice Concepts and sell direct to retail customers - how? Should Omega just sell the voice chips direct to Hallmark? Do you have any alternate suggestions to bring the final retail price down – to \$7/card? \$5/card?

Draft Market and Competitive Analysis for Your Business Plan - due March 5

The analysis of the target market (your potential customers, the size and growth rate of this market, and what you can charge for your product or service) and your competition (who, how many, market share, strengths & weaknesses) is the *most critical part* of a business plan. The results of this market demand forecast determines:

- 1) The commercial viability of the concept - does a *large enough potential market* exist for the product or service that will generate the level of revenues needed to execute the concept and to reward the lenders or investors in your business? What price can you charge? Based on what evidence? Will consumers actually buy your product or service at that price? Can you verify this in advance - how?
- 2) The competitive strategy to be used. What does the competitive situation look like now? Can you get an edge over your competitors - how? How much can you charge for your product or service? What does the price sensitivity look like for your product or service? What will you compete on – location, service, features, convenience, price?

- 3) Interest to potential investors - does the projected market size & growth rates indicate that viable earnings and an "exit vehicle" will exist for your investors in order to "cash-out" their investments? Who might want to buy your company?
- 4) Remember, the financial projections in your business plan are all based on (and are no more accurate than) your sales projections multiplied by your estimate of what price you can charge for your product (your pricing strategy). Profitability also depends on accurate cost projections, but with careful research you should be able to "nail your costs", so that the level of revenues is the greater uncertainty.

The market and competitive analysis is almost always the most difficult part of a business plan to prepare - the more you know about your target market (your potential customers and their behavior), and your competition and their pricing and distribution methods, the more *believable* your BP will be. Prepare a 6-9 page draft of your target market analysis and competitive analysis for your business plan, so that I can provide feedback and suggestions for you. (If you are missing key target market or competitor data, indicate what data you are missing, and how you plan to get it - or if you are going to estimate it, what relevant data you will use to base your estimates on.) In group projects, only one target market and competitive analysis is required, but be sure to identify all group members who are participating in that business plan preparation so that they can all receive credit.

Case 4- Michigan Lighting, Inc

This case deals problems that can arise when equal partners in a private business have a falling out, and illustrates why it is critical to agree on buy/sell valuations & buy-out procedures in advance when setting up a business. It also focuses on the suitability of different methods for valuing a private business, and the importance of psychological factors in structuring buy-outs.

Please answer the following questions:

- 1) How can Jack Peterson arrange a buy-out of David Scott to end their ownership conflict by a procedure that Scott will view as fair and impartial? Suggest some potential approaches: e.g. should they submit sealed bids – and the highest bid wins? Should they get an outside appraisal first - then the highest bid over the outside appraisal wins? Should they agree beforehand on a minimum bid amount, and then submit sealed bids? Other ideas?
- 2) What do you think MLI is worth to Jack Peterson? Pick a value and explain how you arrived at your valuation (Use at least three different valuation techniques to get a fix on potential value - such as (1) adjusted net book value (total assets less total liabilities increased or decreased for any off-balance sheet items); (2) a valuation based on some multiple of net income, EBITDA, or cash flow - e.g. 10 times net profits, 7-9 times EBITDA, etc. justifying the multiple you used; (3) any other valuation techniques such as discounted future cash flows - that you think could be helpful.

EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization) is a good valuation for Michigan Lighting (and probably the most-used measure for valuing existing businesses as well) because it looks at how much cash the business generates, independent of the age of the assets (depreciation), the tax rate paid (income taxes), or the financing of the business (interest expense). In the case of Michigan Lighting, the 1985 EBITDA is computed by taking the net income for 1985, and adding back to it the interest, income taxes and depreciation paid in 1985 (there was no amortization) as follows:

1985 Net income	\$115,209
Depreciation	55,978
Interest expense	56,259
Income tax expense	<u>44,350</u>
EBITDA	\$271,796

- 3) Construct an offer by Jack Peterson for Scott's 50% share of MLI (Peterson may well believe that 100% ownership is worth more than half of the present value, so your proposed bid may exceed 50% of your estimated valuation for MLI, above). Structure your offer to David Scott to respond to Scott's psychological needs - how can Jack cushion Scott's worries about what he will do after he leaves Michigan Lighting? Should Jack's bid be all cash up front; or cash plus a 5 year non-compete agreement for Scott with annual or monthly cash payments over five years? Can Peterson minimize his out-of-pocket cost by paying Scott some initial cash plus a percentage of MLI profits for 5 years? (Note that if Scott doesn't trust Peterson, he is likely to be suspicious of an "earn-out" since Peterson could manipulate MLI's expenses to make future profits lower, delaying Scott's repayment.) What is your rationale for your offer package (explain how it matches up with Scott's needs).
- 4) How should Peterson finance his offer based on his (and Michigan Lighting's) financial condition? How much of Peterson's bid can be financed by MLI's present borrowing capacity at their bank which is (100% of MLI's cash + 75% of MLI's accounts receivable, less any loans already outstanding to the bank, plus 75% of any other asset values not presently used as collateral - such as the \$200k excess market value of the Pontiac plant over its book value). How much will Jack have to back with his own personal assets as collateral?
- 5) What are your initial strategic suggestions for Peterson when he purchases MLI in order to get MLI's profitability up? First he should do this, next do that, then _____, etc. List the first five steps you would suggest to him.

Preparing financial projections for your business plan

When you are preparing your financial projections in your business plan, I would suggest using three different projections – best case, likely case and worst case.

- 1) **Best case** [the upper range of your revenue estimates if everything goes right];
- 1) **Median situation** [what available industry data indicates is likely to be the most-likely case with average luck]; and;
- 2) **Conservative scenario** [based on a low range of revenues taking existing problems into account].

What you are trying to do is to determine if the venture is likely to have adequate funds and cash flow to accomplish its objectives over the next several years at different levels of sales, and to lay out a probable financial scenario for the future in order to determine if additional infusions of capital will be needed (and if so – when), and whether the business is likely to be profitable. A current buzz word used by venture capital firms is “fully-funded”, which means a new venture has enough financing committed to fund it all the way to the point of the likely exit for early investors (including the VC firm), such as sale to a larger company or an IPO, without having to try to raise additional capital sometime in the future. If a business does not have sufficient initial funding to survive through revenue short-falls, it may be forced to seek additional funding at a greatly increased price (in terms of the equity that will have to be given up per dollar of new funding) during business down-turns, which can badly dilute or even wash-out the investment of the founders and initial investors.

GRADING POLICY

Your course grade will be determined as follows:

Attendance; class participation & your PowerPoint BP presentation.	10%
Your <u>three</u> individual case analyses (15% each)	45%
Your draft market & competitive analysis	15%
Your final written Business Plan	30%
Total	100%

I will grade on a curve to meet the Business School grade distribution guidelines, and plus/minus grades will be used.