

Profit Making for Nonprofits
and
Social Enterprise
Tool Kit

Jim Masters

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Profit Making and Social Entrepreneurship Tool Kit

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A. WHAT AND WHY of Profitmaking and Social Enterprise

<i>Highlights of This Section...</i>	
	<ol style="list-style-type: none">1. What is profit-making?2. Why profit-making?3. How did it start?4. Where are we now?5. What is Social Enterprise?6. What are the future challenges?7. Questions, questions, questions.8. Fears and Realities

1. What Is Profit Making?

"Profit" is defined as "the monetary surplus left to a producer or employer after deducting expenditures." (The Random House College Dictionary, 1973.) "Profit-making" in nonprofit organizations has generally involved activities or enterprises aimed at generating income that will help pay for ongoing operations or that extend the mission in new ways, e.g. providing full time employment for program participants. Profit-making is a way of generating unrestricted income, free from the "strings" which accompany government, corporation or foundation funding. Earned income is also called profit by some people.

"Fund-raising" is the more traditional method used by nonprofits to obtain funds. Fund-raising generally means an organization seeks gifts or donations or conducts special events to support its activities. These gifts/donations may be in the form of grants, bequests or individual donations. The amount, length of support and approved uses of funds are usually determined by the donor, rather than the recipient.

"Program Income" is the money a nonprofit earns when Federal, or sometimes state, grant money has been used to generate it. For federal programs, program income is defined as:

"...gross income earned by a (grant) recipient from activities part or all of the cost of which is ...borne as a direct cost by a grant... It includes but is not limited to such income in the form of fees for services performed during the grant."

Since program income is derived from grant funds, the federal funding source has the authority to decide how it can be used. The three major options are:

1. Funding sources requests a refund of the money earned. (The Treasury choice)
2. The program income is subtracted from the regular grant. (The OMB preference)

3. The money collected can be used by the nonprofit for an approved program expansion. (Fortunately, most Federal funding agencies usually do this.)

This publication focuses on the broad range of profit-making activity, but not including Fund-raising. We discuss business or revenue-generating activities, not grants; donations; or special events. The emphasis is on helping you to identify products or services which can generate income. It is unlikely that profit-making activities will totally eliminate the need for grant funds for most agencies; however, profit-making can be a viable source of supplemental funds, or can extend your mission. One subset of profit making is called social enterprise.

Social entrepreneurship -- for-profit enterprises operated by nonprofits -- enables them to continue or expand their work. Running a business that employs program participants builds a fresh new image for some nonprofits. We define the types of social enterprise for use in this publication on page 1-5.

A nonprofit can not distribute its net earnings as a dividend to individuals who have control over it (i.e., no benefits may inure -- or go -- to officers, directors, trustees)

...BUT...

A nonprofit organization can earn a profit. (e.g. hospitals, private schools, etc.)

For those nonprofits that also have a tax-exemption from the IRS, if the profit comes from activity that is related to their tax-exempt purpose then they do not have to pay taxes on it. If the profit comes from activity that is unrelated to their tax exempt purpose, then they will pay taxes at regular corporate rates. (This is not so bad a problem to have!) The test is made on the type of activity that generates the profit, not on the way in which the profit is used. More on this later.

2. Why Profitmaking?

Reductions in government funds, fierce competition for grants and bequests, and relatively small increases private sector contributions are prompting some nonprofits to look for other sources of funds. For others, a desire to go beyond traditional services to provide new opportunities for employment is a prime motivator.

Dramatic changes have affected nonprofits over the past five years; these changes make other income sources more important:

- An increased number of nonprofit organizations are competitors in a shrinking grant environment.
- Government policies have shifted more responsibility for responding to poverty and social problems to the nonprofit sector while reducing monetary support to that sector.
- New incentives are needed to keep quality staff.

Social Entrepreneurship

- The economy will never provide enough good jobs. Nonprofits are seeking to provide permanent employment for program participants

3. How Did it All Start?

The date of the first church bazaar or bake sale isn't recorded. Profit-making began at the populist, or grassroots level, when the first church or community group discovered the collection plate just did not contain enough. And, it is an idea closely tied to an enterprising spirit. So what seems to be a contradiction -- profit-making by nonprofits -- isn't such a contradiction: It grew out of social concerns and causes.

Volunteers were one of the most important assets of these early ventures. Many were women with enterprises reflecting women's skills and interests at the time -- sale of baked goods, crafts, and cookbooks. As time passed and the idea evolved, those enterprises evolved into business ventures we recognize today -- hospital coffee shops, thrift stores, bookstores, museum gift shops or restaurants, and Girl-Scout cookies.

Grants are finite, cyclical and dependency producing. You'll always be competing for them with life and death organizations like hospitals. Inevitably a losing game. The winning game is generating much of your own income.

Richard Stekel, Director, Denver Children's Museum

Just a few of the benefit and challenges:

Benefits	Challenges
Increased financial independence	Low success rate of business starts
Greater self-sufficiency and self-direction	Skepticism and hostility
Better reception from private funders	Complicates agency administration
Incorporation of a training program or work experience may help your program participants	Need for financial sophistication
	Energy may diverted to the for-profit at the expense of the nonprofit

Only 10-15% of nonprofits have solid prospects. That group would include... arts and educational institutions which have money-making experience and a public receptive to the idea. --

Edward Skloot, New York Consultant

On the Other Hand....

If survival's at stake, any organization should at least confront the possibility, however slim, of earning some income. The question is: how can the organization realize whatever potential it has? -- S. Loren Cole, California Consultant

4. Where Are We Now?

In the 1960's, the nonprofit sector exploded with tens of thousands of new agencies and hundreds of new programs. The Great Society programs reached past traditional public agencies to finance social movements and community based organizations. New structures were created to address complex social problems. Community Action Agencies (CAA's) and Community Development Corporations (CDC's) were designed to encourage business and community development in economically disadvantaged areas. CDCs helped neighborhood entrepreneurs operate business enterprises and build, rehabilitate, and manage housing. The long experience of the CDCs contains many of the issues, successes, and problems that a nonprofit profit-making enterprise will encounter.

Other nonprofit groups joined the profit-making movement out of necessity. Drug and alcohol rehabilitation centers and half-way houses for ex-convicts traditionally have difficulty attracting funds and finding permanent employment for program participants. Instead of relying on totally philanthropy or government support, these groups capitalized on one asset: an available labor pool. Sheltered workshops were created to meet the therapeutic and rehabilitative needs of both their clientele and the market area.

Expansion, professionalism and new possibilities typified non-profit enterprise during the 1970's. Universities began using empty space for summer conferences and seminars -- for a fee. Museums began selling reproductions of jewelry and carvings, stationery and bath towels. Zoos studied traffic patterns and began selling hot dogs, balloons, and animal food in spots with heavy traffic flow.

The expansion of the 70's was checked by federal budget ceilings in 1978 and cuts in 1981. The Urban Institute estimated that federal budget cuts cost the nonprofit sector \$25.5 billion through 1984. Local human service agencies experienced cuts of 15% to 25% in most programs.

The 1990's were characterized by "cause-related marketing" -- where nonprofits teamed up with for profit businesses for mutual benefit. The results of these partnerships run the gamut from the successful collaboration between Share Our Strength and an omelet pan manufacturer to the disastrous public relations debacle for the American Medical Association and Sunbeam products.

Defining Social Entrepreneurship

Some describe the overall purpose of nonprofit entrepreneurship as building “community wealth” – generating resources through profitable enterprises to promote social change and build assets for the community as a whole. Others take a more narrow focus and look at the benefits to the organization and the people directly involved.

Although these business enterprises take many forms, for purposes of this publication we will group them into the following three categories: **social entrepreneurship, direct entrepreneurship, and cause-related marketing.**

1. Social Entrepreneurship is mission related -- using ventures to accomplish or extend the mission of the agency. It provides jobs, competitive wages, career opportunity, and ownership for people who are disadvantaged, whether it be physically, mentally, economically, or educationally. Undertaking social entrepreneurship is the transformation of one's agency or a program into a place where there is a business venture with a social mission. Usually the business is related to its tax exempt purpose. This may be a single venture, or a “market aggregation” or “access to markets” project. Some agencies create a market for the products or services produced by program participants -- like a crafts catalog, a consignment shop, a carts-and-kiosks venture, a flea market, or farmers’ market.

Examples of social enterprises that are single businesses include:

A restaurant, run by a nonprofit, to assist formerly homeless and/or substance abusing men to learn the restaurant trade. (Delancey Street, San Francisco)

A Community Action Agency in Seattle sells holiday gift baskets, with products made by their clients, via direct marketing. They also run a for-profit thrift shop (Lower Columbia Community Action Council, Longview, WA)

A youth agency in San Francisco operates a Ben & Jerry's franchise to teach youth about the service industry. (Juma Enterprises)

A CAA runs nine (9) thrift shops. (Parkersburg, WV)

Examples of market aggregation ventures include:

Appalachia By Design, a knitting cooperative, assists residents to find markets for their hand-knit sweaters. They offer training, certification, and marketing assistance. (West Virginia)

A Community Action Agency in Seattle sells holiday gift baskets, with products made by their clients, via direct marketing. (Lower Columbia Community Action Council, Longview, WA)

An agency in Alaska sells native crafts through a high end mail order catalog. (Rural Alaska Community Action Program, Anchorage)

2. Direct entrepreneurship includes businesses created by nonprofits, that are designed to create profit for the nonprofit, even through it is not directly related to the charitable purpose of the organization. Examples of direct entrepreneurship include:

A museum runs a gift store and a cafeteria.

A museum, aquarium, arboretum, library or historical building offer their facility for weddings and parties.

A nonprofit owns its building and rents out office space to other organizations or to businesses.

Local governments run Off Track Betting, hotels, restaurants, parking garages, and radio stations.

The Girl Scouts sell cookies to raise money for club projects.

A university runs a materials testing lab, or a travel agency or an appliance store.

A nonprofit sells its mailing list.

3. Cause-related Marketing involves the agreement between a corporation and a nonprofit that benefits both parties. The three types of cause-related marketing are described briefly below.

1. Transaction-based promotions. The corporation donates specific cash or product in direct proportion to sales revenues. An example is the American Express Charge Against Hunger campaign;

2. Joint issue promotions. A corporation and a nonprofit take on a social problem through education and promotion. Money may or may not change hands. An example is "Hand in Hand," a program to promote breast health, sponsored by Hanes Hosiery and a number of nonprofits. It included magazine advertising, in-store promotions by Hanes, and free educational materials; and

3. Licensing. A corporation uses a nonprofit's name and logo in return for a fee or percentage of revenues. An example is credit cards with a college logo.

The Challenge of the New Millennium

More and more nonprofit staff and board members are looking at themselves from a different perspective -- as entrepreneurs. Many are using sound business techniques to sell products and services related to their social mission. As they begin to think like entrepreneurs, new income producing possibilities are emerging. The challenge is being pursued through increasingly creative ventures and partnerships:

Many Community Action Agencies, building upon 20 years of experience with Weatherization Programs, have started for-profit business subsidiaries to assist homeowners who were not eligible for the free services to assess and improve the weatherization of their homes. Some agencies contract with utilities, mortgage lenders, and real estate agents to rate the energy efficiency of homes.

The Los Angeles Coroner's Office opened a store that sells a variety of logo-imprinted items - body bag luggage, crime scene tape, body outline note pads, etc.

The Women's Business Center opened a coffee shop, called Coffee with a Conscience, in the Milwaukee Public Library, after the privately-owned shop went out of business. They use the shop as a business lab for new entrepreneurs, a marketplace for local bakery items, and a promoter of ecologically sound coffee growing practices.

In Middlebury, Vermont, a consignment shop named Neat Repeats raises money from the store to support many local nonprofits. Local nonprofits apply to Neat Repeats for grants. In 8 ½ years in business, the shop has donated \$500,000 to area nonprofits.

The Intervale Foundation's fledgling compost project began accepting yard and food waste to make high quality compost. They now sell their compost by the bag and truckload throughout Chittenden County, Vermont.

The Burlington Community Land Trust sponsored a "child's vision of home" project, inviting area elementary school students to draw their vision for secure and happy homes. The drawings were made into greeting cards and underwritten by the Bank of Vermont. All proceeds from the cards benefit the Land Trust.

Profit making is not easy. The agency has to run the nonprofit side of the agency, the new business, and it has to run the relationship between the two.

Questions, Issues, and Decisions

Where do we start...?

What do you need to do?

When do we show a profit?

What are the legal issues?

How is the Board involved?

We'll lose our tax exempt status!

But what about our mission?

Hey! I've got an idea!

Wait a minute... I've got a better idea...

Listen to this we can use...

Risk can be exhilarating for some but can cause uncertainty and anxiety for others. It is even more difficult if a nonprofit has become dependent on public sector and private contributions. Such an organization may be too accustomed to serving the requirements of its funding sources. Or, it has developed programs backed by inadequate funds that never seem to fill the demand of its constituents. Or, it has become too socially specialized. It may seem the complexities involved are overwhelming and starting a profit-making business is a high risk, but it can be done – and that is what this book is about.

This book provides you with the decision-making and information resources you can use to start a profit-making enterprise. It is meant to be written in and used. The exercises, work sheets, and resource lists are designed for group decision-making and involvement. Keeping a record of your thoughts is useful... write them down. Understanding what is involved is a start toward selecting and running a good business. Making the decisions and facing the issues takes initiative, planning, determination and intuition. All are part of the entrepreneurial venture.

Don't be discouraged about the time necessary to undertake entrepreneurship. The planning and discussions you have early in the decision-making process may be beneficial to your fledgling business venture – and avoid problems in the relationship between the nonprofit and the venture later on.

Fears and Realities

TYPICAL FEARS	REALITIES
1. Profit-making is an inappropriate activity for a non-profit organization: "We are a human service agency!"	1. What may have been inappropriate in the past is rapidly changing. Many non-profits have been doing this for years, e.g., Girl Scouts and others.
2. "We may lose money!"	Yes, you may lose money, but you may also make money.
3. "The community wouldn't like it."	3. There is a mixed public reaction to this strategy: Some think that we "should act like a business" and appreciate the trend of self-reliance. Some don't think it's appropriate.
4. "It's illegal for us to make a profit – we're a non-profit."	4. It is legal. All ventures can be operated and a profit made. A lawyer can help explain why.
5. "We can't do it... we don't know how to operate a business."	5. Many are doing it and making a profit. You can get the expertise you need.
6. "Business ventures will distract from our mission: providing services."	6. If you make money, the profits can be used to enhance the resources to provide programs that meet the mission.
7. "Our funding sources won't like it."	7. Some funding sources are encouraging profit-making activities. It is your agency and you have to make your own choices.

B. Review Possible Effects of Profit-Making Activity

Highlights of This Section...

1. Mixing moral and economic missions
2. What makes a business different?
3. Pluses and pitfalls

1. THE MORAL MISSION AND THE ECONOMIC MISSION

Peter Drucker make a distinction between the “moral mission” and the “economic mission” in his book “Managing for Performance.

Nonprofit institutions generally find it almost impossible to abandon anything. Everything they do is “the Lord’s work” or “a good cause.” But nonprofits have to distinguish between moral causes and economic causes. A moral cause is an absolute good. Preachers have been thundering against fornication for five thousand years. Results, alas, have been nil, but that only proves how deeply entrenched evil is. The absence of results indicate only that effort have to be increased. This is the essence of a moral cause. In an economic cause, once asks: Is this the best application of our scarce resources? There is so much work to be done,. Let’s put our resources where the results are. We cannot afford to be righteous and continue this project where we seem to be unable to achieve the results we’ve set for ourselves.

To believe that whatever we do is a moral cause, and should be pursued whether there are results or not, is a perennial temptation for nonprofit executives—and even more for their boards.

The nonprofits are human-change agents. And their results are therefore always a change in people—in their behavior, circumstances, vision, health, hopes, above all, in their competence and capacity. The non-profit institution therefore needs to set specific (as opposed to open ended) goals in terms of its service to people. (p 111 – 112)

The problem with the moral mission is that it is by nature un-achievable. Further, it does not have any built in criteria that tells you where it is ok to stop investing resources into it. So the effort to maximize the moral mission goes beyond the optimal expenditure levels to places where unit costs just keep going up.

Another way to think about this is the relationship between the mission drive and a market drive.

Purpose and Mission, defined broadly, is why you were created, the ends you wish to accomplish, and the values that you hold as important, and the major strategies you will use to get there. It has an historical basis and tends to reflect the perception of the desired future as it was thought to be at the time the organization was founded.

Market forces are those forces which are beyond the control of the organization and reflect the realities of today. "Market" is defined here to include the economy, demographics, social values or science and technology. These forces reflect themselves in what is demanded from the organization and include changing needs and desires by the society. The convergence of changes that are shaping the future are often called Megatrends.

In an ideal world, the mission of the organization and the market are headed the same direction, and the values and needs of both are related or linked.

MISSION DRIVE AND MARKET DRIVE

In the real world, the mission and the market may diverge or begin to work in different directions. Society (the market) may be changing faster than the organization. What was valued by the market at the time mission was set may be in less demand and be held in less esteem. Or, the economy has changed dramatically -- leaving your historic mission behind.

MISSION DRIVE

MARKET DRIVE

ASK YOURSELF THESE QUESTIONS:

1. What are the costs of being totally Mission driven? What are the benefits? Is our mission up to date?
2. What are the costs of being totally Market driven? What are the benefits? Has the market changed in ways that we need to respond?
3. How do you find the right balance between Mission and Market in your organization?
4. Can you redefine your mission to include market drives? Or do you have to hold the two separate and continually work to reconcile their inconsistencies?

So, one of the biggest challenges in starting a profit-making enterprise inside a nonprofit is finding the right mixture or balance of their conflicting purposes or agendas.

Business is a very single minded pursuit. Its goal is to make a profit and increase earnings for its owners. To be successful in most businesses, it is necessary to focus primarily and usually exclusively on business goals. The major goal of a nonprofit is to obtain grants or contracts to use to provide services or address social concerns for the benefit of the community. While this seems obvious, conflicts between the two sets of purposes will consume hours and hours of time among board members.

A non- profit-making venture must deal with the same kinds of problems and risks as any business in that industry, and it must compete with established, traditional businesses. The profit-making venture must be free of constraints if it wants to increase its chances for success. If a nonprofit tries to achieve too many social goals through a profit-making enterprise, the two sets of goals become tangled and confused which acts as an additional restraint and add costs to the profit-making venture.

This does not mean that nonprofit purpose or concerns are thrown away. It is possible to go about your exempt purposes generate income. Some Board and staff members want to develop programs that answer social concerns. Others want to develop an alternative, steady funding source. These differences do not have to split the organization apart.

2. What Makes a Business Different?

Elements of running a business and a nonprofit are alike; there are also other elements that make them very different.

		Differences and Similarities of Business and Nonprofits	
		Business	Community-Based Nonprofit
Business Elements	Purpose	Profits	Social Concerns
	Organizational Structure	Sole Proprietorship (single owner) Partnership (two or more owners) Limited Partnership Corporation	Corporation
	Policy Decisions	Individual owner (s) Agreement between general/ limited partners Board/shareholders	Board of Directors/Trustees Government regulations or trust conditions
	Day-to-Day Management	Individual (s) General partner(s) Officers of the corporation and mgmt personnel	Executive Director and staff
	Market	Customers (a cross-section of the general population willing to purchase certain products)	Clients (distinct or targeted segments of the population eligible for receiving services or in some way benefiting from activities of the organization)
	Capital	Loans, personal savings, profits, investors, stocks	Government funds, traditional and alternative private foundations, trusts, cash contributions and donations of goods and/or services.
	Competition	Other businesses (large or small, sophisticated or simple)	Other nonprofits (large or small, sophisticated or simple)
	Cash Flow	Fluctuates depending on market, seasonality, economic factors. Profits are its only source.	Relatively stable once grants/contributions are secured. Fluctuates on political climate
	Professional Advice	Usually pays for the advice of accountants, lawyers, marketing, and/or management specialists	Sometimes pays, finds help for free, or secures "loaned" help from other organizations, Board, staff, or community volunteers

There are many more subtle differences and similarities and one clear, major distinction:

Businesses do not rely on consensus or group decision-making; management decisions are made within a hierarchy and humanistically applied.

Charles Cagnon, Business Ventures of Citizen Groups.

The qualities of a business are also different than those of a nonprofit. Attitude, approach and tone are -- well, "business"like, or at least more focused.

A nonprofit must be willing to give decision-making for the profit-making venture, once it begins, to venture management and staff. This may cause some qualms as it involves risk and measure of trust. If that flexibility is not given, the business' chance of success is low. "Democratic Management" systems rarely work; too many conflicting interests make a business vulnerable especially if it is a small enterprise. The profit-making enterprise has a primary purpose to you, the parent organization: to generate income. Management will need to concentrate all of its efforts on business goals: making a profit. The prime demand on business -- satisfying the customer through dependable quality and performance -- makes it necessary for business management to make decisions quickly and consistently.

Pluses and Pitfalls

MISSION RELATED: Possible Pluses

1. Resource Diversification.
2. New employment opportunities for low-income people; meet a need.
3. Opportunity to rethink and sharpen mission, products, markets and accountability.
4. Introduce a market focused activity designed to solve a problem.
5. Self-reliance for mission accomplishment; not subject to changes in funding.

Possible Pitfalls -- Mission-Related

1. Perception that private sector activity will replace need for public responsibilities.
2. Perception that profits will replace need for public money.
3. Shift agency focus from low-income people to focus on markets with higher income.
4. Perception that it is inappropriate for a nonprofit to compete with local businesses.

PROGRAM RELATED Possible Pluses

1. Credibility.
2. Discipline of cash flow analysis, breakeven analysis, and other profit-making techniques.
3. If go with known products and services, will have low-entry costs. Build on strengths.
4. Increased funding agency support for strategy.

Possible Pitfalls -- Program-Related

1. Management time diverted.
2. Longer-term payoff.
3. Public relations risk; funders may have problems

PERSONNEL: possible Pluses

1. Stimulate entrepreneurial impulses.
2. Exciting and dynamic organizational culture.
3. Fresh start, recharge batteries, new fun, inspiration.
4. Feeling of being in tune with the times; prevent "brain- drain."
5. Strengthen personal responsibility.
6. Profit-making results provides clear feedback on performance.

Possible Pitfalls -- Personnel-Related

1. Creating a dual-class system; rewards to the entrepreneurs and not to service providers.
2. Equity for all agency members; dual-personnel policies.
3. Program managers do not have business management skills...they have program management skills.

PLUSES AND PITFALLS EXPANDED VERSION

MISSION RELATED	
<u>Possible Pluses:</u>	<u>Possible Problems:</u>
1. Resource diversification.	1. Perception that private sector activity will replace need for public responsibilities.
2. Meet a need.	2. Perception that profits will replace need for public money.
3. Opportunity to rethink and sharpen mission, products, markets, and accountability.	3. Shift agency focus from low-income people to focus on markets with higher income. Bi-modalize out clients.
4. Introduce a market focused activity designed to solve customer’s problem, not just to deliver services.	4. Perception that it is inappropriate for a nonprofit to compete with local businesses.
5. Self-reliance for mission accomplishment; not subject to changes in funding emphases.	5. Our market niches are the multiply handicapped populations, and we should “Stick to our knitting.”
6. Helps to de-stigmatize services.	6. The poorest of the poor are insured only by society through public funds.
7. Diversity to other populations in need.	7. Some of our board/community/clients/staff will oppose it.
8. Grow past existing catchment area.	8. The mind set that we can only provide specified services to defined populations is very powerful.
9. Focus on Megatrends and strategic planning.	9. Lowers the quality of our services.
	10. Public funding agencies see us as their employees.

PROGRAM RELATED	
<u>Possible Pluses</u>	<u>Possible Problems</u>
1. Credibility in community.	1. Management time diverted.
2. Discipline of cash flow analysis, breakeven analysis, and other profit-making techniques.	2. Longer-term payoff.
3. Better known products and services.	3. Investment of resources in ventures instead of low-income people. Risk that there will be no profits or will be loss.
4. Low-entry costs.	4. Public relations risk to our reputation.
5. Many growth markets.	5. Drag of venture structure maintenance.
6. Increased funding source support for this kind of activity.	6. Proliferation of providers.
7. The only "certificate of need" you need is a business license.	7. We don't know how to compete.
8. Develop new negotiating and business skills in partnership formation.	8. We lack marketing skills.
9. A way around fee capitation.	9. Our catchment area is our limit.
10. A way around limits of number of visits.	10. We move too slowly – others beat us to the market.
11. Third-party payments, yum-yum!	11. Undercuts or squeezes our existing unit-of-service cost structure.
12. Compensation tied to performance. "Variable pay-out tied to pay-in."	12. Legal risk, lawsuits.
13. Puts us into the performance contracting trend.	

PERSONNEL RELATED

<u>Possible Pluses</u>	<u>Possible Problems</u>
1. Stimulate intrapreneurial impulses. Motivate staff.	1. Creating a dual-class system; rewards to the intrapreneurs and not to the service providers.
2. Exciting and dynamic or organizational culture.	2. No more equal pay for all agency members; existing compensation systems won't work.
3. Fresh start, recharge batteries, new fun, inspiration	3. Program managers do not have business management skills ... they have program management skills.
4. Feeling of being in tune with the times.	4. Mind set issues.
5. Prevent "brain-drain."	5. Our definition of quality must change.
6. Strengthen personal responsibility.	6. Don't know what our products are.
7. Profit-making results provides clear feedback on performance.	7. Don't know how to package our services.
8. New source of income for staff.	8. Some of our staff do not believe that they can shape the future, or ... that it will happen at all!
9. Practice for private practice.	9. Forces us to cream, take the easy customers.
10. Learn new ways to access, deliver services and close a case.	10. Our image is dead plants and blue jeans, not new furniture and "dress for success."

CLIENT or PROGRAM PARTICIPANT RELATED	
<u>Possible Pluses</u>	<u>Possible Problems</u>
1. Clients get what they want, not what you deliver.	1. Creates a “class” mentality.
2. Problems specifically defined, time-limited goals for improvement.	2. Contrary to the idea that we should “do all that is possible, keep people as long as needed.”
3. Some clients will perceive that we have more skills, more current knowledge.	3. Forces clients out before all that needed to be done has been done.
4. Clients get better sooner, because the agreement between the client and therapist about what it means to get better has changed.	4. May push clients into accepting “fad” or “trendy” definitions of problems.
5. More cost effective.	5. May push therapists into trying untested or experimental methods before they understand them.
6. The exchange relationship is more balanced.	6. Wealthier clients get better services and more attention.
7. Clients may be more invested in working to solve problems.	
8. Clients become customers and are treated as such.	

C. Prepare the Organizational Climate

<i>Highlights of This Section...</i>
1. Getting to yes – or no. 2. Exercises for fun board meetings 3. 20 questions to ask and answer before we begin.

1. Getting to yes -- or no.

1. TALK ABOUT IT WITH EVERYONE, BOARD AND STAFF... LOT'S OF TALK. You can not really make a "sneak entry" and just ignore those who are strongly opposed... it will come back to haunt you.

2. TALK ABOUT THE RATIONALE for this strategy. The changing times... the need for new resources... what's happening to old resources.

3. CITE EXAMPLES OF SUCCESS. Others that are making it happen in agencies just like yours.

4. BE REALISTIC. Talk about the real risks... everyone knows that businesses can make money... and can lose money. It is better to admit the potential problems and talk about how they can be overcome.

5. DEVELOP CRITERIA FOR WHAT YOU WILL NOT DO. Turn objections into venture constraints. By saying what you will not do, you will have defined what you can do.

6. TALK ABOUT PERSONAL REWARD AND INCENTIVES. Entrepreneurial behavior is encouraged when staff members are rewarded for their efforts and success.

7. TALK ABOUT THE LONGER-TERM. Almost every agency will agree that new methods and resource diversification are necessary when you consider the longer term needs.

8. IDENTIFY THE KEY SUPPORTERS ON THE STAFF AND BOARD. You will be surprised who is for it... and who is not.

9. BUILD OVERALL TRUST. The decision to initiate profit-making ventures usually happens in agencies where there are high levels of trust in general between staff and board.

REMEMBER...

1. YOU CAN NOT MAKE SOMEONE BE A PROFIT-MAKER...IF HE/SHE DOES NOT WANT TO BE ONE.
2. THE EXECUTIVE DIRECTOR, THE BOARD, AND THE PROGRAM DIRECTOR MUST ALL AGREE... OR IT WON'T WORK.
3. SELF-INTEREST IS A VALID AND NECESSARY INGREDIENT IN SUCCESSFUL VENTURES.
4. YOU CAN NOT OPERATE A PROFIT-MAKING VENTURE LIKE YOU OPERATE A GRANT-FUNDED PROGRAM.

2. Fun at a Board Meeting

EXERCISE: Why do we want to initiate it in our agency?

You	Board	Management	Clients	Stakeholders
-----	-------	------------	---------	--------------

Provide funds to support our principal activity
Earn money for unrestricted income for our agency

Business activity will help accomplish our mission
Develop experiences/jobs for clients
Provide structured activity/money/for clients
Jobs for people in the community/econ dev

Create greater visibility for our organization
Compete more effectively
Reinvigorate our organization
Be on the cutting edge of new technology
Develop a new business thrust
Use specific business techniques/e.g. marketing

Change our organization into a different kind of entity
Diversify or expand our product/service lines
Expand or penetrate new markets/market segments

Utilize excess staff capacity
Provide incentives for staff to earn extra money
Keep salaries down
Create career paths for people who will otherwise leave
We heard about this social enterprise idea,
and we try everything that's new
Salvage a defunded program/activity
Pressure from Board
Pressure from funders
Other reasons

DISCUSSION: What are the implications of different motives – and where do they lead you?

2. More Fun. EXERCISE: WHERE ARE WE NOW?

1. READINESS OF BOARD AND STAFF

- a. Several of us in the organization are ready
- b. A few of us are ready, including some of the leadership
- c. I am ready

2. WE WILL EXPECT COMMITMENT AND SUPPORT from:

- a. the entire agency
- b. the senior management
- c. one person -- "our entrepreneur"

3. DEGREE OF IMPACT ON MISSION

- a. We adapt our mission when opportunities or threats appear.
- b. We change when our funders tell us
- c. Our historic mission is sacred and can never be changed

4. DEGREE OF CHANGE IN OUR traditional image

- a. human growth and community change organization, some of whose funding sources happens to be Federal agencies
- b. a multipurpose services provider for indigent people
- c. we are a local provider of federally defined services

5. OUR COMMITMENT to the entrepreneurs

- a. The organization is behind you to help when you need it
- b. We'll jump-start you, keep us posted
- c. Good luck, Lone Ranger -- and your horse Silver stays with us

6. ACCOUNTABILITY AND MEASUREMENT

- a. We may have to revise current accounting and reporting systems or devise new procedures
- b. One new form should do it
- c. Fill in the box marked "other" on our current report

7. FINANCIAL EXPECTATIONS:

- a. Big bucks -- when it hits
- b. 15% R.I.
- c. Whatever

8. TIME FRAME. I expect it will take
 - a. One to three years to break-even
 - b. Less than 122 months to start generating profits
 - c. No time at all to generate profits -- and I want the money NOW!

9. CONSUMERS for our entrepreneurial effort may be
 - a. Target markets for whom the service is right
 - b. Some mix of our current customers
 - c. Low-income people only

10. OUR CURRENT CONSUMER GROUPS/OTHER STAKEHOLDERS
 - a. Will think this is a terrific idea
 - b. Won't care as long as it does not affect them, or we can work it out with them.
 - c. Won't like it and will try hard to stop us

11. WHAT WE NEED TO SUCCEED
 - a. Customers who will pay a fair price for quality services
 - b. Good business planning, management, loans, fiscal controls
 - c. A funder for the start-up costs

12. THE COMPETITION
 - a. May not like it but we will do it anyhow
 - b. We will check with the IRS and our funders to make sure it is ok
 - c. We will not do it if somebody else is already doing it

13. NONPROFIT CHARTER and corporate culture
 - a. Permits all kinds of income generating activity, related and unrelated
 - b. We will only do activity that is related to our mission
 - c. Nonprofits -- by definition by tradition and by law -- can't make a profit

3. Twenty Questions to Answer Before You Begin Your Profit-Making Venture

Purposes:

1. What are the income goals from profit-making activities by program or venture over the next three to five years? For the agency as a whole?
2. Given the Agency's mission, what kinds of profit-making activities will not be considered, if any? (Specifically: Related versus Unrelated Businesses; markets to be targeted - traditional versus new markets; will traditional client groups be charged user fees?; supporting small businesses owned by others versus small, in-house businesses).
3. What social objectives (i.e. profit-making constraints or costs), if any, will be added to the income objectives of profit-making activities? (To what degree will profit-making projects also be social enterprises?)

Risks and Incentives

4. How much time and money is the Agency willing to risk over the next four years on initiating profit-making activities (i.e., how much can you afford to lose?) (Specifically: How much per venture and how much in toto? Where will start-up funds come from? Can the expenditure of these funds and board/staff time be risked for an uncertain return after considering other Agency priorities and pressing client needs?)
5. Should the Agency attract private sector and/or other non-profit partners in initiating specific ventures? If so, what is the criteria for partners and when will they be sought? Are there partners who will not be considered?
6. If an in-house venture fund is established, what will be its size? What will be the criteria for use of these funds to initiate ventures and what will be the process by which funds are requested and investment approved? Are these in-house loans or grants?
7. If the venture makes a profit, how much of that profit belongs to the Agency? How much is used to replenish the "venture fund"? How much reverts to the program that generated the profit? How much should go to the individual staff member(s) as entrepreneur? If the venture loses money, how is the loss divided between these parties? What, if any regulations or requirements exist concerning program income or profit-making activities?

Structure and Decision-making

8. What will the role of the Board be in approving specific ventures? In making management decisions in their operation?
9. Will there be a Board Committee specifically that monitors all ventures and/or will there be advisory committees for individual ventures? If there will be advisory

committees, will membership include non-agency representatives?

10. Should there be a separate subsidiary corporation/s for ventures? If so, should it be a nonprofit or for-profit corporation? Should it be dependent on venture type, degree of venture success, and/or status of implementation? If so, what will be the criteria for this decision of when to spin-off to a separate corporation and who will make this decision? Can we approach this decision in phases?
11. Who will be responsible on staff for initiating ventures? Can anyone make a proposal? What is the role of program managers in venture management? Will profit-making activities be part of the staff evaluation criteria and salary increase decision? Will one staff member or department be responsible for all profit-making activities?

Venture Management and Policy Support

12. What staff and Board training and technical assistance is necessary for profit-making and how will it be obtained? (Specifically: legal, business, and accounting assistance). If these are limited, are we willing to “buy” these services or do we need to learn them ourselves?
13. What new capabilities and responsibilities will be required of the fiscal department? Will new support staff need to be added to the Agency to support profit-making activities? Will their time be “cost allocated?”
14. What personnel policies, if any, need to be revised or amended to encourage and permit profit-making activities? What other agency policy documents may need to be changed -- bylaws, articles of incorporation, etc.?
15. When will formal business plans be required and what will be the internal criteria for their approval? When will feasibility studies be required?
16. What constraints exist, if any, in the use of grant funds and/or grant purchased equipment in profit-making activities? When should the Agency seek specific approval for each venture from the funding source that bought the equipment? Can the for-profit lease or rent the equipment from the nonprofit?
17. How will the Agency assure that profit-making activities will not “significantly” detract from the Agency's mission and the operation of grant funded programs?
18. How will the policies developed from the resolution of these questions be communicated to all staff and Board members?
19. How will this decision be communicated to the community at large and your Agency's program participants and other stakeholders?

Evaluation

20. What will the criteria be for the evaluation of the overall profit-making decision and when will it be evaluated? By whom? For what purpose? What is the process for adjusting the business direction as a result of the evaluation?

5. What Do You Want from the Venture? Develop Venture Selection Criteria

Once the exploration into starting a profit-making enterprise begins, you'll need to decide what you want to accomplish with the business. Look at the questions that have come up during meetings and the issues you've had to face. Then decide whether or not those issues pose critical or minor challenges. Is the type of business important to the venture? Is private sector involvement preferred or unacceptable? Is preserving the image of the agency important? The importance of those and other issues should be summarized and weighed, because they become the factors that cause your Board and management to vote "yes" or "no." These issues become your venture selection criteria.

Criteria for Nonprofit Profit-Making Ventures

Criteria	Required	Preferred	Doesn't Matter	Not Preferred	Unacceptable
1.					
2.					
3.					
4.					
5.					

2. Feasibility. Methods for Identifying a Sector of the Economy and Venture Selection

<i>Highlights of This Section...</i>
Identify some of the ways that a venture might be selected.
How to Identify Business Opportunities. <ol style="list-style-type: none">1. Customer demand.2. An entrepreneur makes it happen.3. Buy a business or franchise4. Systematic Analysis of Opportunities Unbundle existing programs/assets5. An example of asset analysis6. Keep track of YOUR analysis and revisit or add to your venture selection criteria7. Screen your options.

There are several approaches to finding a business opportunity.

1. Customer demand. The phone rings and a customer insists you provide the services, You already know how to provide the service, you have the staff, the tools and the materials. So you do a “product line extension” to a new market or customer segment. This is looked at briefly in section 2.1 on page 2-2.

2. An Entrepreneur Makes It Happen. A staff person or group of staff have the expertise and tenacity and to create a business. They have the knowledge and experience needed to get started -- and the “fire in their belly” and bootstrap the business off the ground. This is described in section 2.3, pages 2-3 to 2-14.

3. Systematic Analysis. The third way is through a formal environmental scan, a planning process, or another types of systematic analysis. There are four approaches provided here.

A. One approach starts with your existing services and assets. Some checklists for use in “unbundling” your existing services and identifying possible markets for them are included in Section 2.3, pages 2-15 to 2-24.

B. Another approach is described by Peter Drucker in his superb book “Innovation and Entrepreneurship.” (Harper Books, 1993) He says that about 1/3 of most products and services “go sour” each year. Since most replacement ideas do not work, you need a pipeline with several times the number of products that are becoming obsolete in order to have enough winners to keep your product line fresh.

He identifies seven major sources from which new business opportunities flow:

1. The Unexpected
2. Incongruities
3. Process Need
4. Industry and Market Structures
5. Demographics.
6. Changes in Perception
7. New Knowledge

C. Another approach is described in Frank Lusby's paper, "Design of Subsector Programs for Enterprise Development." (Handed out separately.)

D. Another can be gleaned from the paper on "The Future of Human Services," included as an appendix to this workbook. Jim suggests that there are certain programs that are growth industries – and that these spawn innovation at the edges and business opportunities. And – there are some declining programs, whose public support has waned or budgets are shrinking or whose ideas have run their course. Businesses related to them are less likely to grow.

4. You Buy A Business. Another way is that an existing business or a franchise company has already done some of the analysis and they sell the analysis or the business to you.

The first three of these are explored below. Buying a business or franchising are beyond the scope of this publication..

21. Customer demand. The phone rings – or the person walks in the door.

This is what Peter Drucker calls "the unexpected success or failure." Here's the conversation:

"I'll pay you to do the same weatherization and energy conservation service on my house that you did through your program for my neighbor."

"But you are not eligible for our services, sir."

"I know that – I'll pay you for the work."

"We provide free services only to people who meet these income guidelines...."

"I don't meet your eligibility requirements, but I like your work. Will you do it? Or not?"

Or,

“I want the same counselor that helped my cousin to help my wife and I work through some problems.”

Or,

“We want to rent your conference room for a meeting.”

Or,

“Our local business association staff quit. We want your training department to help plan and manage our annual meeting.”

D.2. An Intrapreneur Makes It Happen.

The way to stimulate and encourage staff people to develop ventures is describe by Gifford Pinchot. The next eleven pages summarize his ideas about how this happens inside an existing organization. In the past, people with ideas and aspirations to run a business left agencies and went out on their own, taking their ideas, talent and drive with them. Many agencies have come to accept this as a fact of life, without looking at what incentives they might offer such people to stay. Industry has come to grips with this phenomenon and has given it a name, "intrapreneuring." Intrapreneurs are:

- People who work almost entirely for themselves within the organization.
- The ones who figure out how to turn a profitable idea into reality.
- "Dreamers who do."
- Able to take hands-on responsibility for creating innovation within an organization.
- People who introduce and produce new products, processes, and services, which enable the organization as a whole to grow and profit.

They differ from the entrepreneur in that the entrepreneur fills this role outside an organization.

Innovation means "doing new things;" which is different from creativity or "thinking up new things." The intrapreneur doesn't necessarily need to be creative, but is able to take creative ideas and make them practical. The intrapreneurial vision is a "working model of all aspects for the business being created and the steps needed to make them happen."

Adapted from: Pinchot, GIFFORD III; Intrapreneuring: New York: Harper and Row, Publishers, 1985. p.40.

1. Many staff members who began their career in the agency move on to the private sector. Or, spin off and start a new agency – then compete with you for clients or funding.

2. The questions to ask are:

- Why does this happen?
- What are the motivations for leaving the agency and moving to private practice and self-employment?
- What are the rewards that are expected by the staff member who establishes his/her own practice? Is it:
 - Money?
 - Sense of adventure?
 - Being their own boss?
 - Dissatisfaction with the organization?
 - Frustration with the bureaucracy and paperwork?
 - A sense of the "real world" leaving them behind
 - A feeling that entrepreneurial behavior is frowned on by other members of the organization and not rewarded?
 - Status?
 - Self-control of hours and income?
 - Different clients to work with?
 - Others?

In creating INTRAPRENEURS who will operate their venture inside the agency, these rewards (now sought on the outside of the agency) must be created within the agency.

HOW CAN THIS BE DONE?

1. Analyze the interests of your staff.
2. Identify the reward systems that are present or absent in your organization.
 - a) Compensation system
 - b) Fringe benefits
 - c) Other personnel policies
 - d) Management policies
 - e) Management attitudes
3. Discuss the possible options for keeping people on staff who can develop income for your organization. What is it that the agency and the executive can do?
4. Select options that will work for everybody, i.e. that are perceived as:
 - a) Fair
 - b) Equitably applied.

WHAT ARE THE **SIMILARITIES AND DIFFERENCES BETWEEN MANAGERS AND INTRAPRENEURS?**

Managers

Mission oriented

Agency-wide focus

Planning

Systems

Standards

The Board

Compliance

Revise budget annually

Boundaries

"The way we do things..."

Risk averse

We have clients

Prestige comes from within
system, mostly superiors

We don't compete

Intrapreneurs

Customer oriented

One product or service

Ready, Fire, Aim

People

Innovation

The exchange relationship

Modification

Revise budget weekly

No boundaries

"What the customer wants"

Failure is an exciting opportunity to learn

I have customers

Prestige comes from
customers

I compete

Adapted from: "Intrapreneuring," by Gifford Pinchot III, Harper & Row, Publishers. 1985.

ORGANIZATIONAL SUPPORT FOR INTRAPRENEURING

Organizations may also need to change some aspects of their internal management in order to accommodate the intrapreneur and effective management of business venture.

Intrapreneurs need a structure that allows them to work hours that may be different from those worked by other agency staff. They probably require different incentives in both pay, benefits, and autonomy than traditional program managers. They also need different access and services from administrative support staff, such as fiscal, clerical and legal personnel. Personnel policies may have to be revised to accommodate the special work needs of intrapreneurs.

Gifford pinpoints ten "Freedom Factors" which should be present to support intrapreneuring.

10 Freedom Factors that Support Intrapreneuring

1. Self Selection. Studies show that successful ventures were headed by a "zealous, volunteer champion," not someone who was merely assigned, or worse, cajoled into assuming responsibility. Intrapreneurs appoint themselves to their role.
2. No Hand-off. "Innovation is not like a relay race in which an idea can be handed off from runner to runner." Organizations must provide ways for intrapreneurs to stay with their intra-prises.
3. The Doer Decides. The intrapreneur needs to have the authority to do the job in his/her own way, without having to constantly stop to explain their actions and ask for permission.
4. Corporate "Slack". Intrapreneurs need discretionary resources to explore and develop new ideas.
5. Ending the Home-Run Philosophy. Some organizations are only interested in starting business ventures with huge success as their only goal. The highest return will come from starting many initially small intrapreneurial thrusts, each of which has some short-term promise and a variety of future possibilities.
6. Tolerance of Risk, Failure and Mistakes. Innovation cannot be achieved without risk and mistakes. Even successful innovation generally begins with blunders and false starts.
7. Patient Money. Organizations need to stick with the venture long enough to allow it to succeed. It is counterproductive to a new business to give and then withdraw money before it has a chance to overcome initial losses and lack of

profit.

8. Freedom from Turfiness. The organization must discourage turf battles. These may include boundaries between programs; boundaries between functions, such as marketing, fiscal, etc., and boundaries between levels of hierarchy. To function effectively, the business must be able to cross the boundaries of existing patterns with the organization.
9. Cross-Functional Teams. Organizations should allow small teams with full responsibility for developing an intra-prise to work with the intrapreneur to manage the venture.
10. Multiple Options. Intrapreneurs need the freedom to use the resources of other divisions or outside vendors and experts.

Adapted from: Pinchot, Gifford III; Intrapreneuring; New York: Harper and Row, Publishers, 1985. pp. 198-199.

How to Stifle Innovation

In her book, "The Change Masters: Innovations for Productivity in the American Corporation," Rosabeth Moss Kanter identified ten rules for stifling innovation. They are:

1. Regard any new idea from below with suspicion -- because it's new and because it's from below.
2. Insist that people who need your approval to act go through several other levels of managers first to get their signatures.
3. Ask departments or individuals to challenge and criticize each other's proposals. (That saves you the job of deciding; you just pick the survivor.)
4. Express your criticisms freely, and withhold your praise. (That keeps people on their toes.) Let them know they can be fired at any time.
5. Treat identification of problems as signs of failure, to discourage people from letting you know when something isn't working.
6. Control everything carefully. Make sure people count anything that can be counted, frequently.
7. Make decisions to reorganize or change policies in secret, and spring them on people unexpectedly. (That also will keep all staff members on their toes.)
8. Make sure that requests for information are fully justified, and make sure that it is not given out to managers freely. (You don't want data to fall into the wrong hands.)
9. Assign to lower-level managers, in the name of delegation and participation, responsibility for figuring out how to cut back, lay off, move people around, or otherwise implement threatening decisions you have made. And get them to do it quickly.
10. And above all, never forget that you, the higher-ups, already know everything important about this business.

* Simon and Schuster, 1983, pp. 100-101.

WHAT HAPPENS? How does an intrapreneur work?

Invisibility

Solo flights

Networks for ideas and advice

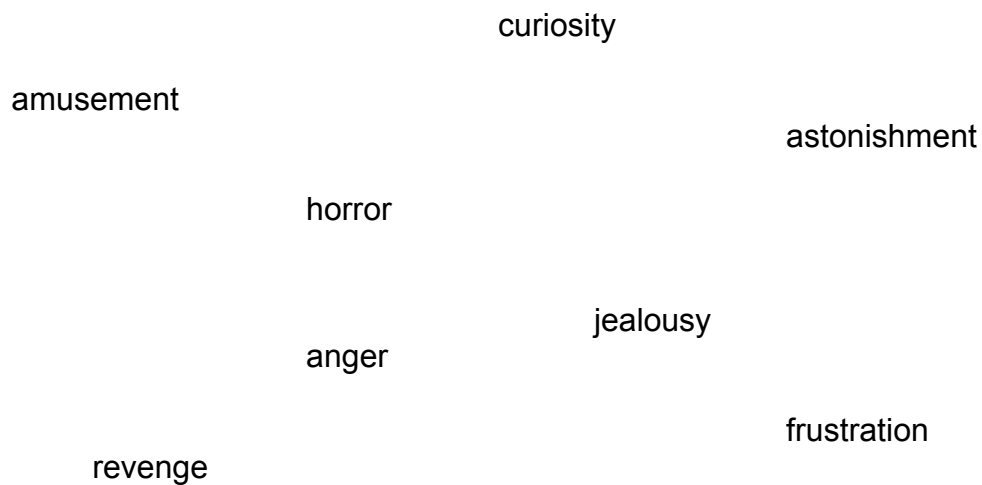
* Team creation. The work intensifies

Bootleg resources for the reality test

Cut the deal with the sponsor

Formal presentation to top staff and board.

* When the development of the business idea becomes visible inside the organization, the responses from management or peers may be all over the map:



PROCESS STEPS AND RULES FOR THE INTRAPRENEUR

1. Keep quiet.
2. Avoid tripping agencies "autoimmune system" that kills intruders that try to force deviations into the budget/accepted range of activities/the way we do things around here.
3. Under-promise and over-deliver.
4. Cut your deal with the sponsor before the cash flows.
5. Go to customers and reality test the idea before you make a formal proposal inside the agency.

HOW TO BE A SPONSOR

1. State your vision of the future and the future of the agency. This perspective is important to an intrapreneur.
2. Allow yourself to be selected.
3. Be a colleague, not a boss.
4. Help offset the intrapreneur's weaknesses, or find people who will.
5. Think cheap, and urge your intrapreneur to do so as well.
6. Work out goals and milestones. Ask, "How do we know when we are making progress?"
7. Look at the results, not the methods.
8. Be accessible.
9. Give clear feedback. Don't be coy.
10. Expect mistakes.
11. Be prepared to take some heat.
12. Understand your limits and communicate them. Is this idea worth more (to the intrapreneur, to you) than the next promotion?
13. Educate the intrapreneur as to how decisions are made and the other elements of your corporate culture.
14. Help on the timing and shaping the content of "the big presentation" when you take this idea public inside the agency.

MOTIVATING INTRAPRENEURS -- AND BINDING THEM TO THE AGENCY

Try working your way down this list, starting by appealing to the employees altruism and commitment as the reason why they should do this inside the agency. Then, work your way down the list.

Achievement Needs:

Autonomy, responsibility, freedom, resource control _____

Mission (portability) _____

Risk reduction _____

Affiliation Needs:

Team _____

Mentor/Sponsor _____

Opportunity cost _____

Resources/\$, staff, name _____

Personal growth _____

Financial Compensation Needs:

Salary

Cola

Performance Bonus

ADDITIONAL REWARDS FOR BEING "OUR" INTRAPRENEUR

Base plus bonus or profit sharing

profit share, 80you 20 them

safety net on employment

O.K. You've left our employ. How about being:

A subcontractor? 60% to you and 40 them -- of the net

Partner in a joint venture? 50/50 split

An entrepreneur outside the agency who licenses our service/name? Cut a deal for:

40 you 60 them

30/70

Agency is in effect a service bureau to the venture.

You'd better do one of these, or they leave and take the business with them, OR THEY BECOME A COMPETITOR.

The follow exercise has been done several times with people from agencies who plan to be the manager for the employee who is the entrepreneur, and with the employee who plans to be the entrepreneur. Guess what? They come out on opposite sides of most of these issues – so it is a checklist you can use to cut your deal on key elements of the relationship.

DEAL DEVELOPMENT EXERCISE

WHAT DOES THE AGENCY WANT FROM THE INTRAPRENEUR?

1. Product belongs to
2. Mission
3. Agency image
4. Business plan
5. Sell inside/outside
6. Time allotted to develop
7. Board approval for
8. Proof this idea will make money
9. Resources required
10. Time limit on our deal
11. Risk sharing
12. Written contract
13. Sponsor
14. Formula profit sharing
15. Team formation authority
16. Non competition agreement
17. Compensation
18. Benefits
19. Safety net

WHAT DOES THE INTRAPRENEUR WANT FROM THE AGENCY?

1. Product belongs to
2. Mission
3. Agency image
4. Business plan
5. Sell inside
6. Time allotted to develop
7. Board approval
8. Proof this idea will make money
9. Resources required
10. Time limit on our deal
11. Risk sharing
12. Written contract
13. Sponsor
14. Formula profit sharing
15. Team formation authority
16. Non competition agreement
17. Compensation
18. Benefits
19. Safety net
- 20.
- 21.

WALL SIGN for INTRAPRENEURS:

HONOR THY SPONSOR

The SPONSOR is to the INTRAPRENEUR

as the

VENTURE CAPITALIST is

to the ENTREPRENEUR

Systematic Analysis

a. Analyze Existing Agency Capabilities and Services **1. Finding Products in Your Strengths**

As many nonprofits begin to consider profit-making activities, they initially consider businesses in which they have little experience, e.g. "Let's get a McDonald's franchise and earn millions." In most cases, the businesses that are the easiest to establish with the lowest initial risk are those businesses that use existing knowledge, skills and other assets to develop products and services that you can sell. This section provides you with worksheets to help do unravel your agency and programs:

- To catalog existing human, financial, and equipment resources belonging to the nonprofit;
- To use this list as a starting point for possible products that make use of those resources and build on existing capacities that can be provided to expanded or new markets; and
- To identify those ventures that should have early priority consideration.

Hints for completing analysis:

- Each program of the agency should complete this assessment. All staff members should participate.
- Complete the inventory of assets first. Then, an open brainstorming session should be held with from which potential product and market lists can be developed.
- Consider all ideas, and pick two or three potential ventures. Some of the criteria for selection are included in this assessment document.

Start a Business with Programs People, Positions, Programs, and Property

You have some of what you need to start a business at this very moment. Nonprofit agencies have capital and human resources that can be used to make money. Activities, equipment, skills and property use ebb and flow. Analyze your resources, determine "down time" and sell it. Sell to people, other nonprofits, businesses or government.

Selling what you already have and what you already do has great advantages. It minimizes risk, increases resource use, and reduces up-front start-up capital required for a business. Such a formula means profits will happen earlier. A few tips:

- Analyze your true costs to sell the product/service. Don't charge too little!
- Determine your "opportunity cost". If you do one thing, you have chosen not to do another -- could your time and capital be invested somewhere else at a higher return?
- Study the market and respond to its needs and not your desires.
- Identify your assets first.

The Range of Enterprise

Business activities may be **related** to the tax-exempt purpose of the organization or they may be **un-related**. We discuss the implications of this in detail later. We mention it here just to help you think “outside the box.” As ideas are generated the distinctions between related and unrelated activities may blur. Eventually you will have to find a lawyer who can help you with a precise determination -- and to help sort out the implications for your organization.

The "Spectrum of Nonprofit Enterprise" definitions may also stimulate discussion.

Program: The activities or services specified or permitted in an organization's funders, mission or purpose.

Program Revenues: Income earned directly from program activities (fees for services, admission for events).

Convenience: An enterprise activity related to the purpose of the organization that runs it (provides family counseling, taxi service for elderly for a fee).

Selling the Name: Marketing the name (by licensing) or prestige of an organization in order to make a profit. (T-shirts with the organization's logo).

Downtime: Income derived from the use of a nonprofit's assets when the organization is not using them (rental of space, hiring-out skilled personnel to other organizations -- counselors, computer programmers, teachers or computer usage).

Related Extensions: Expanding an enterprise activity related to the organization beyond its immediate needs and clientele (an elderly program that develops day trips into a tour service, selling products produced by clientele).

Unrelated Extensions: Activities unrelated to the exempt purpose of the organization (real estate development of unused land, investments in any type of business from oil wells to pizza parlors).

Adapted from Crimmins, J.C. and Keil, M. *Enterprise in the Nonprofit Sector*, Washington, D.C., 1983.

Worksheet for Asset Analysis. Unbundling Services Into Elements and Components

Sometimes we conceive of a service as being a single, unitary thing. In fact, many services as we define them are really "systems" of activities or functions which take place in a sequence and which ultimately produce that which we then call "the service". Learn to break these definitions up into their discreet elements. Review each function, activity and product for possible sale-ability!

EXAMPLE.

A. Bundled. Information and Referral Directory.

"We do a survey of all human services providers, and gather information on their services, which we print in a directory, which we give to other providers, and we use the directory to refer people who need services."

B. Unbundled products and possibilities.

Also collect and provide information about potential clients to agencies. Market research into population characteristics, broker agreements between agencies or sectors. Move into outreach, recruitment, assessment or testing, or referral services on contract.

Contract to do community education, or implement PR campaigns.

Provide information about agencies to clients. Sell ten one-page descriptions for a dollar.

Produce directories by program area, e.g. individual directories for health, education, youth services, etc.

Sell to different markets (e.g. personnel directors). Sell to those who do not provide information.

Sell at a discount to those who do.

Offer briefings or training about what agencies do.

Provide transportation services to clients, providers.

Develop other publications or reports for agencies.

Provide copying or other office services.

UNBUNDLING EXERCISE.

1. Describe one of your "bundled" products or services.

2. Break it into discreet elements. In column A, list as many specific functions, activities, steps or pieces of the product or service as you can.

A. Activities/functions.

B. Sell to??

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3. Now, in Column B, identify a NEW market for as many separate pieces as possible.

Worksheet. Programs or Pieces of Programs

Analyze each potential element of service and identify possible market(s), and then list the opportunities and barriers that exist in producing and selling those products to those markets. Consider the “down-time” – the time that is currently not being sold to a “funding source” or time of less productivity for potential products, as well.

Program	Current Activities	Chunks or pieces	Benefits of each piece	Possible Markets
Opportunities /Barriers				
Opportunities /Barriers				
Opportunities /Barriers				
Opportunities /Barriers				
Opportunities /Barriers				

Worksheet. Assets -- Human Resources - Staff, Volunteers, Consultants

The talents and skills of staff members and volunteers provide are assets that can perhaps be sold. The familiarity of constituents with the agency or programs is an asset that may be sold. Analyze each potential product and identify possible market(s), and then list the opportunities and barriers that exist in producing and selling those products to those markets. Consider the “down-time” – the time that is currently not being sold to a “funding source” or time of less productivity for potential products, as well.

Persons/ Constituents	Current Activities	Professional/ Personal Skills	Downtime (when)	Products/ Markets
Opportunities /Barriers				
Opportunities /Barriers				
Opportunities /Barriers				
Opportunities /Barriers				
Opportunities /Barriers				

Worksheet . Assets -- Equipment and Physical Resources

List equipment and facilities whether donated, rented, or owned. Consider when each is in use and that current “downtime” and determine if it can be sold, rented, or used to produce something. Consider the “traffic” at each facility location – who uses the location and what products they need, who passes by the location and what products they need, who the neighbors are and what products they need. Michael Friedland, now at the NED&LC, used to advise nonprofits to “put a soda machine in your lobby and hygiene products in vending machines in your rest rooms.”

Equip./Space Available	Purchased or Rented?	Funding Source	Downtime	Sell, Rent, or Produce?	Traffic/ Products
Opportunities/ Barriers					
Opportunities/ Barriers					

Worksheet. Publications, Consultation, Brand Name, Internal Agency Sales

Programs can sell **how** they do things as well as **what** they do. Consider the product list and decide which may be sold outside the agency based upon current areas of expertise and reputation, or sell it inside the agency across programs.

Potential Product	Specific Possible Products/Markets	Status of Current Product Sold	Start-up Needs for New Product
Publications			
Opportunities/Barriers			
Consultation			
Opportunities/Barriers			
Products with Program Logo			
Opportunities/Barriers			
Internal Sales to Other Agency Programs			
Opportunities/Barriers			
Other Possible New Products			
Opportunities and Barriers			

LOOK FOR COST SAVINGS, TOO

In order to compare other sources of income with the possibility of a venture, you can also look at ways to generate revenue through better money management or investment.

Some board member is going to ask you if you looked at this, so you might as well have some answers.

Worksheet: Investments

List all current funding sources, balances, and investments. Consider the possibility of generating additional funds with these current resources, receiving a better return on any investments made, and other such opportunities. Note any barriers that need to be resolved in order to use current financial assets for profit-making activities.

Accounts	Amount	Source of Funds	Invested?	% Annual Return
Opportunities/ Barriers				
Opportunities/ Barriers				

Opportunities/ Barriers				
Opportunities/ Barriers				

Worksheet: Potential Budget Savings

Saving money is making money! For each account, list budget categories and current expenditures; then identify less expensive alternatives, and the opportunities and barriers that exist for implementing those savings. Especially consider those opportunities for agency-wide bulk purchases and centralization of services across various programs, where feasible.

Budget Categories	Current Budget	Possible Bulk Purchase	Less Expensive Alternatives
Opportunities/ Barriers			
Opportunities/ Barriers			

Opportunities/ Barriers			
Opportunities/ Barriers			

5. An Example of a Profit-Making Analysis

After undertaking a profit-making analysis, a nonprofit micro enterprise program generated the following list of potential profit-making opportunities. The next five pages report on what they found and what they did with it.

- Concessions at events
- Start a consulting business
- Write and sell handbooks for business loans, business plans, etc.
- Sell a video that would teach business skills and celebrate the success of their business program graduates
- Build strategic alliances with businesses
- Start a for-fee mentoring program utilizing graduates
- Start a for-fee review of business plans utilizing graduates
- Sell a discount card to the public to buy services/products from businesses at reduced rates
- Start an awards program and have a fee to nominate businesses

Using the graduates of their program, they could:

- Sell ceramic mugs, T-shirts, and other promotional items with profits going to the program
- Offer short business seminars for a fee, or advanced seminars
- Sell instructional manuals
- Sell items at their Business Fair to support the program

After brainstorming this list of ideas, the organization needed to assess the best opportunities for success. Two methods of doing this are presented on the next pages - is the “power of vertical markets” and “the expanding products and expanding markets” matrix.

The Power of the Vertical Markets

- After the nonprofit has identified its potential products, those products need to be tested against and shaped by the customer types, i.e. the markets.
- The generic product is then customized and packaged to meet the needs of the target markets.
- The product should be stated in terms of the "benefits" that the typical buyer in that market segment will receive with purchase.
- We buy for what the product will do for us, what results we will receive, and how it will solve our problems.
- Ask potential customers within a market segment what they want and, more important, why they want it -- the benefits to them.

The market segment should be described in terms of the benefits derived from your product, their packaging preferences, their customizing preferences, and how to best target them. Try completing the following grid:

	Market Segment	Market Segment	Market Segment
Product #1:			
Product #2:			
Product #3:			

Here's an example from the entrepreneurship program mentioned on the previous page:

	Market Segment: New Entrepreneurs	Market Segment Existing Entrepreneurs	Market Segment University professor of business
Product #1: Business Plan Handbooks	The handbooks motivate entrepreneurs to write business plans and provide the tools to do so. It solves the problem of needing a business plan to go to the bank for a loan	The handbooks help them figure out cash flow and financial record-keeping before it's too late!	Provides examples of "real life business" for a traditionally academic audience.
Product #2: Discount Card for Services from member businesses	Method of Promotion	Method of Promotion	None
Product #3: Promotional Items	Advertise their support of the program	Advertise their support of the program	None

Next, further analyze each product, the market segment, and how you are addressing their unique needs. Again, an example from the entrepreneurship program:

Product	Market Segment	Problem/ Opportunity	Solution	Benefit
Business Plan Handbook	University Professors of Business	Need to teach students about entrepreneurship	Our packaged curriculum	Their students will learn entrepreneurship!
	Existing Entrepreneurs	They are losing money	They need to prepare and understand the financials of the business	Save their business!

Try filling out this chart for your products and the prospective market segments:

Product	Market Segment	Problem/ Opportunity	Solution	Benefit

Another way to look at the possibilities you've identified...

Expanding Products and Expanding Markets Matrix

	Existing Product	Improved Product	New Product
Existing Market	a. <i>Safest, easiest</i>	b.	c.
Expanded Market	d.	e.	f.
New Market	g.	h.	<i>in. Highest earning potential, highest investment/risk</i>

Expanding YOUR Product and Market

Start with your existing product and existing market and complete the matrix.

	Existing Product	Improved Product	New Product
Existing Market	a.	b.	c.
Expanded Market	d.	e.	f.
New Market	g.	h.	i.

6. Keeping track of your analysis.

There are powerful arguments keeping us from making profits as nonprofits. And, there are equally powerful forces pushing us to profit-making. It is critical to look at these reasons before a nonprofit chooses, or chooses not, to develop a money-making venture.

A simple “force field analysis” may provide enough framework for a planning group to identify the pluses and minuses. Draw a line down the center of a page and list plus on one side and minus on the other. Identify the factors or forces that are prompting you to do this, and those that are inhibiting you. (Kurt Lewin invented this in the 1950's and it still works!)

Or, following a strategic planning model, you might use a SWOT analysis. A “SWOT” (Strengths, Weaknesses, Opportunities, Threats) analysis is one way for groups (or individuals) to see the restraining and motivating forces involved in making major decisions. Having lists of those reasons may make the decision making easier.

It may take months to complete the initial step and decision-making necessary to starting an enterprise. Using a SWOT analysis at different times during the planning process may be helpful:

- In the beginning, to show you what you'll be facing;
- When you're trying to choose the structure of the venture;
- During market analysis when you try to generate ideas for products; and
- While looking at financing needs.

List three or four elements in each section of the chart. Pay close attention to the weaknesses and threats. The staff and Board must address the weaknesses and threats prior to the launch of the venture. This is a preliminary brainstorming exercise, you'll be prompted later to get into the details of your assets as an organization.

**SWOT Worksheet: Strengths, Weaknesses, Opportunities, and Threats
For Your Profit Making Adventure**

Strengths	Weaknesses
Opportunities	Threats

7. Screen the Options

Highlights of This Section...

How do we decide what to sell?

How can we screen the business options?

"What can we possibly sell?"

Finding an answer to this question is one of the more exciting aspects in developing a business. Possibilities are endless. And, if you aren't prepared, discussions on choosing your product or business venture may become as endless as the possibilities.

You and your Board need enough background to select a business enterprise suitable to your organizational purpose, profit making goals and community.

Have you identified any possible ventures from your asset analysis?

Dredge up that list of venture funding criteria from your initial meetings. Are they still relevant? This was the worksheet found on page 1-27.

Some additional criteria might be:

- something we can start easily and expand over time
- low start-up costs
- low-risk to our reputation
- fewest barriers from staff resistance, mission resistance or funder resistance.

Now, put three of the best ideas down on paper – and take it through your decision making process to get the approval(s) needed.

Worksheet Summary of Your Venture Opportunities

Venture #1

Product/markets:

Start-up needs:

Steps for initial action:

Who/when:

Venture #2

Product/markets:

Start-up needs:

Steps for initial action:

Who/when:

Venture #3

Product/markets:

Start-up needs:

Steps for initial action:

Who/when:

E. Identify the Project Manager or the Venture Manager Early-On

Highlights of This Section...

Who will run the process to create the business?

Who will run the business?

Identify the Characteristics of an Intrapreneur”

The issue of running a business like a business will usually stir controversy among staff. Generalizations and discussions abound on what makes a good business person and who is most entrepreneurial minded. There are no hard and fast rules for identifying an entrepreneur.

Nonprofits and business both attract creative people. Qualities found in successful entrepreneurs are also found in some of the leaders of the nonprofit world.

Selecting an individual to be in charge of a profit-making enterprise should include attention to personal qualities of successful entrepreneurs as well as skills needed for the job such as:

- Excellent knowledge of their "industry"
- High energy level
- Self-confidence
- A high tolerance for ambiguity
- Likes to solve problems
- Thinks their accomplishments are within their own control not due to luck or circumstances
- Good at using help or listening to feedback for ideas and solutions
- Don't let their egos get wrapped up in who gets credit
- Don't mind taking risks but are not "gamblers." Sometimes referred to as calculated risk takers"
- Commitment to the larger purpose of the organization
- Respect for and understanding of the nonprofit's mission.

Qualities to look for in an intrapreneur:

- Small business experience
- Interest in financial matters
- Energetic, attention to details, cautious
- Ability to express performance expectations of staff
- Customer focused.

A good entrepreneur or business manager will pay strict attention to costs, revenues, cash flow, production, and the balance sheet (liabilities and assets). He or she will monitor all transactions and be able to present the overall financial picture of a venture. And he or she will have the ability to manage staff: clearly stating goals and insisting on

performance without destroying motivation, initiative, or creativity.

Qualities to look for in other staff members are:

- Willingness and ability.
- Experience in the type of business selected.
- Some understanding and agreement with the purpose of the parent organization.

Candidates for social entrepreneurship are evident in your agency. Help them get the support and training they need to take on this new role.

If possible, select your intrapreneur early in the business planning process. Invite the intrapreneur to help lead the feasibility process and “buy-in” to the business from the start.

*From William A. Duncan, *Looking at Income-Generating Businesses for Small Nonprofit Organizations*.

3. Feasibility Work Continues

In this chapter, we look at (a) various legal considerations, (b) factors to consider in forming a business structure, and (c) analyzing the competition, and (d) market plan development. For many ventures, this will complete your preparation work – and the venture will become visible to the public. For others, you will need a full-fledge business plan and more detailed financial information, which is covered in Chapter 4.

Highlights of This Section

Is this legal?
What are the tax implications?
What is “related” vs. “unrelated” income?
What is program income?

A. Legal and Tax Considerations

Questions about the legalities and taxes are a normal part of developing a profit making venture. Outsiders and many insiders do not understand that it is legal for a nonprofit to be involved in profit making activity.

The bottom line (ahh, a business term) is that nonprofit agencies can earn profits, but are constrained on what they can do with them. And, the profits may be taxable if they come from activities that are unrelated to the tax-exempt purpose.

In Section A, we review a few of the areas where legal issues may arise, including charges of unfair competition, used of property purchased with Federal funds, distribution of profits, and tax issues. In Section B, we discuss the legal structure of the venture.

"Unfair Competition"

A charge of "unfair competition" is usually made by other local businesses. You will first hear about the complaint from an elected official, funder, or reporter. You can be completely legal and still be subject to charges of unfair competition. And – remember – major companies sue each other all the time for infringement of this or that just to slow the other company down for a few months. Have your description about why this is legal ready BEFORE the phone starts ringing – so you can be pro-active in your response. Have a letter from your lawyer, the minutes of the board meeting, and other information on-the-shelf and ready for use.

This idea that any nonprofit that goes into business in by definition competing unfairly used to be fostered by none other than the U.S. Small Business Administration. In a paper written by SBA's Office of the Chief Counsel for Advocacy, *Unfair Competition by Nonprofit Organizations with Small Businesses: An Issue for the 80's*, November, 1983, arguments are presented against nonprofit having any kind of profit making ventures.

The publication examined the impact of Federal policies and activities that allow nonprofit organizations to engage in commercial activities. It also contains recommendations for tax and legislative reforms to correct the threat SBA sees. Early in 1984, OMB was considering a proposal to draft new rules regulating nonprofits use of equipment obtained under Federal grants. This action was a direct result of SBA's claim that a "real and significant participation by nonprofits in essentially commercial activities" exists. All nonprofits were viewed as threats because the arguments SBA made did not make a distinction between large nonprofits and smaller organizations involved in profit making, e.g. between the multimillion dollar university testing lab and the neighborhood group selling recycled materials.

Statutes or regulations SBA targeted, and its recommendations are listed below. (The full report can be obtained from SBA.) Be alert to these issues. The possibility exists OMB or IRS could pass them on in regulatory form. Or, you may find SBA's arguments being adopted at the state level or used in the rhetoric of legislators:

- Higher tax (taxing nonprofits at the maximum corporate rate instead of on the normal sliding scale, or outright prohibition of unrelated business activities)
- Defining more clearly what constitutes "unrelated trade or business" (IRS should look at the extent to which the business activities impact on commercial firms.)
- Making unrelated business activities a criterion for revoking tax exemption by IRS

promulgation of a rule that a nonprofit involved in a percentage of business activities will be presumed to be operating for other than tax-exempt purposes.

- Eliminate or restrict exemptions from tax on unrelated business income (by an act of Congress or the IRS eliminating activities operated for the convenience of its members, e.g., hospital cafeterias and the like) and restrict exemptions from income derived from basic or pure research, and eliminate exemption for income derived from applied research.
- More closely regulate commercial use of Federal agency-supported equipment.

SBA's proposals sound ominous. They're not when you consider other factors that balance the recommendations:

- If funds from Block Grants are used, states are responsible for dealing with the issue of unfair competition and state rules may apply.
- Your feasibility or marketing study may demonstrate that a proposed venture won't unfairly compete with established private competitors.
- The mutually beneficial economic relationship between nonprofits and the private sector may be described in your business plan. They may be a partner in your venture.

SBA also just changed their rules to permit certain loan programs to loan money to ventures owned by community development corporations.

Using Property

Most property owned by a community based nonprofit organization can be used in profit making activities, providing you allocate the costs and compensate the nonprofit for use of the property. For example, weatherization programs do for-profit weatherization using their tools, materials and staff, and pay the nonprofit for their use.

The Federal Government has a limited right of transfer over certain non-expendable personal property. Compensation to the Federal Government for its share of the remaining property's current market value is usually made.

Certain non-expendable and expendable personal property can be used without compensation to the government.

State rules, not Federal rules, apply to property bought with block grant monies. Check on what State administrative and fiscal practices apply.

Reviewing the OMB circulars and funding agency rules on Federal property rights is worth the time. Many nonprofits still receive Federal grants or have become involved in

partnerships with the private sector which use Federally purchased or owned property. OMB has promulgated uniform rules governing grantee management of property bought with Federal funds. As long as you allocate costs among various uses and pay fair rent for using the property you should be O.K.

Receiving Benefits From Business Activities

As a general rule, Board Directors or members, and employees of a nonprofit may not benefit from the services of a nonprofit. An exception can be made where the individuals themselves are members of a **bona fide** charitable class.

State Conflict of Interest laws, state Block Grant regulations and state Ethics Commission policies all apply. Conflict of Interest rules, thoughtfully adopted into a nonprofit's bylaws, protect it from charges of benefiting from the nonprofit's own services or business profits.

“Self-Dealing”

"Self-dealing" is a term describing business transactions -- deals -- between the nonprofit organization itself and "related individuals" (officers, directors, board members, trustees or substantial contributors) who are directly connected with the organization.

Private foundations are prohibited from any self-dealing transactions. A private foundation cannot conduct business with its own officers, directors, trustees, or substantial contributors involving (but not limited to) the sale, exchange or leasing of property, the lending of money, or the furnishing of goods services or facilities.

All other 501 (c) (3) organizations (defined as public charities) do not have such an outright prohibition. The 501 (c) (3) organizations that remain (public charities) are permitted self-dealing transactions that are structured and carried out in a way that does not violate the private benefit test underlying tax-exempt status. This is the "inurement provision" which states that the corporate asset may not insure (go) to benefit an individual.

The IRS has a number of texts and standards for determining whether a transaction is considered self-dealing. Determinations are made on a case-by-case basis. Generally, the IRS looks for "arm's length" standards to be followed in any transaction with a related individual. E.g., if you rent space from a Board member, then you should get 3 bids, pay fair market rent, and the board member should abstain from all voting on the matter.

How the transaction is set up and carried out is important, what records are kept, who talks to whom, whether objective appraisal is available for providing fair market value. Because of these factors, getting a prior ruling from the IRS is one approach to covering yourself., however it is impossible to know how the IRS will react. Getting a letter from

your lawyer is probably an easier way to cover yourself.

Now, think about this – exactly how many organizations do you know of that have ever lost their 501 (c)-(3) tax exemption because their unrelated income exceeded the allowable amount?

Taxes: Unrelated or Related Business Income

Is there any precise measure for determining how unrelated or related your business's goods or services are? Can you tell what income is taxable and what is not? The answer to the first question is no; to the second, it is yes -- to a certain extent. We don't mean to equivocate. IRS judgments are made in the context of individual situations. Consider this: broad statements of tax policies allow flexibility; without it, standard application of tax rules occurs -- and that is anathema to business.

Making a judgment of how far you can go in selling goods or services before a venture's income becomes unrelated involves some practice. On the surface a nonprofit's goods or services may seem unrelated. If a venture uses appropriate accounting methods and has a strong sense of how to apply IRS tax guidelines to determine related or unrelated income tax or tax exemptions, the boundaries of what a venture can do begin to expand.

The IRS looks at what percentage of your TOTAL AGENCY BUDGET comes from the net income of unrelated ventures.

So let's say you have an agency budget of \$1,000,000. You could have up to 15% (or maybe 25% or maybe 40%) of that total that is net income that comes from unrelated sources and still remain tax exempt. That's a lot of income for most organizations.

So let's say your venture has a gross income of \$300,000, expenses of \$250,000, which nets you \$50,000. So you have 950,000 from grants, and 50,000 from the business. And that is 5% of your TOTAL AGENCY BUDGET. It is that 50,000 of income that the IRS looks at as the percentage of unrelated income.

Rules of thumb:

If your unrelated income gets to be 15% of your agency budget, consult a lawyer.

If the conclusion is that it may affect your tax-exempt status, spin it off into a separate corporation. Problem solved.

Taxes: Filing

Reporting Federal taxes for a business is easy. You fill out IRS Form 990T and send it in with any tax payment. The 990T is a public document.

By law, you must also keep a copy of this form readily available for any member of the public who wants to see it. Some agencies leave copies with the receptionist.

Contact State authorities to find out what taxes apply to your venture. Develop and keep a tax schedule for the business. Note the dates when State or Federal taxes (sales tax, social security taxes, unemployment, FUTA, and so on) are due.

We will end this section with an issue that will probably never happen to you – that you earn so much money that the IRS determines that you are no longer a public charity – you have become a private foundation.

Private Foundation or Public Charity?

The first test used by the IRS is to determine the percentage of a nonprofit's income from public sources (government and public contributions). An organization receiving 33 1/3 percent or more public income is automatically considered a public charity. (The IRS also considers additional factors if the percentage is less than 33 1/3 percent but more than 10 percent).

A second test gauging public income can qualify an organization as a public charity; public support must be greater than 33 1/3 percent but the amount of investment and unrelated business income, less the appropriate taxes, must be less than 33 1/3 percent.

So think about this. What do you think the odds are that you will earn so much money that more than 66 2/3 of your income will come from those sources -- and that less than 33 1/3 of your revenue will come from government sources? If this does happen, it could bring about a corresponding change in tax status -- from public charity to private foundation. If you are earning so much money that you have this kind of problem – call me. We'll do lunch. On you.

Now, on to more relevant matters – choosing your business structure.

B. Choosing Your Business Structure*

Highlights of This Section. . .

1. Will the business be related or unrelated to your tax exempt purpose?
2. Will it be run inside the agency, or – separated from it?
3. How much control do you want?
4. What are the forms of ownership available?

This chapter* walks you through the decisions that will lead to a choice about the type of business ownership. The basic idea is to find a structure and a fit with the parent agency that is right for your profit-making venture. **Keep in mind that a complex, sophisticated structure isn't necessary: selection of a business structure depends a great deal on the scale of the venture.** A \$20,000 business can be run out of a desk drawer and a checkbook. You will need the help of Board and staff to complete this process and, if scale of the business is large, the assistance of legal counsel.

Choosing a final business structure involves three preliminary questions:

- Profit. Should we operate the business as related or unrelated to our exempt purpose?
- Separation. Should we run the business in-house or as a separate entity?
- Control. If a separate entity, what is the preferred proportion of ownership? If part of the nonprofit agency, what proportion of the business is controlled by the Board of Directors?

Ownership, control, and separation decisions will evolve through discussions with Board members and staff. The “decision tree” on the following page helps visualize these choices. After the chart, there is a more detailed discussion of each choice.

*Major portions of this chapter were adapted from: Wiewel, Jim, Ridker, James H., Mier, Robert, Gilroth, Robert - *Business Spin-offs: Planning the Organizational Structure of Business Activities: A Manual for Not-for-Profit Organizations*. University of Illinois, Center for Urban Economic Development (UICUED), Chicago, IL, 1978 (sponsored by Grant No 06-06-01539, US Dept. of Commerce, Economic Development Administration).

The Decision Tree [sic]

Reprinted from: *Business Spinoffs: Planning the Organizational Structure of Business Activities*. Center for Economic Development, University of Illinois, Chicago, 1982.

Related or Unrelated Activity: Options and Advantages

Decisions all have certain advantages and disadvantages. (And opportunity costs and unintended consequences, but that's another article). The next several pages describe some of the possible options and implications of each.

This decision involves choosing between a business activity that is "unrelated" to your nonprofit purpose as stated in your Articles of Incorporation, or is "related" to your nonprofit purpose.

Profit Decision Options and Advantages

Option	Advantages
"For Profit" with Unrelated Business Activity	Write-off losses
	Access to capital
	Access to entrepreneurs
	Access to jobs, image, and responsibility
	More freedom for operations
"Not-for-Profit" with Related Business Activity	Access to grants and subsidies
	Related business has no size constraints
	No income tax liability
	Less controversy
	Appeal to entrepreneurially-spirited volunteers

The **Separation Decision** involves control and protection issues.

Separation Decision Options and Related Advantages

Option	Advantages
No Separation – run it inside the existing nonprofit	Management and control
	Organizational and staff development
	Flexible use of personnel
	Safeguard community purpose
	Shield from an uncertain market
	Lowers start up costs
Separation	Focused purpose – less confusion
	Inspire confidence
	Access to capital and human resources
	No tax exemption issues
	Protects parent organization from liability

The **Control Decision** contains input and tax issues.

Control Decision Options and Related Advantages

Option	Advantages
“Controlled” Corporation (50 percent or more)	Retain control but allows for input; if wholly-owned (100 percent), retain complete control
	Consolidate tax returns of multiple subsidiaries in holding company **
“Non-Majority” Ownership (50 percent or less)	Create maximum options for input (entrepreneur, employees, communities); some control may be possible
	Parent organization not taxed on some payments received from subsidiary
	May avoid criticism – “we’re just a small player.”

**There is some confusion here. Under the Internal Revenue code, a “controlled” organization for Unrelated Business Income Tax (UBIT) purposes is one that is over 50% owned by the parent -- IRC 512 (b) (13) (d) (ii). This means that all passive income (except dividends) received by the parent of the controlled subsidiary is taxed as unrelated business income (UBI). If there is less than 50% ownership, passive income is NOT taxed as UBI. (This is different from the rules for holding companies. Check with your attorney on holding companies.)

THIS MAY HAVE CHANGED.

CHECK WITH YOUR ATTORNEY FOR THE LATEST ON THIS TOPIC.

Business Structure Terms

Take a few moments to familiarize yourself with some terms that will be used in this discussion.

Parent (or existing) Corporation

The formally-structured existing group that wants to initiate a new entity (in this case, a nonprofit corporation established to serve community interests).

In-House Program or Venture

An activity operated under direct control of the parent corporation's Board of Directors and subject to the parent's articles of incorporation and bylaws.

Separate Entity

An entity legally distinct from the parent corporation. If it has a corporate form of ownership, it files its own articles of incorporation and establishes its own bylaws. Its Board is responsible solely for its own obligations and debts.

Subsidiary

A separate entity related to the parent organization because it is wholly controlled or partially owned or controlled by the parent.

Spin-off

The process or end result of establishing a venture as an entity separate from the parent organization.

Discussions About Separation -- Continued. "In-House" or "Out-of-House"

A parent organization may face the decision of operating a venture within its own structure -- "in-house" -- or establishing a separate entity -- "out-of-house". This choice must balance the organization's need to maintain direct control and nurture the project against the need to create other options for management and limit risk exposure. We can begin by comparing the advantages and disadvantages of not separating or separating the business venture.

In-House Operation (Not Separating)

In-House Advantages

- Management and control – decisions can be implemented immediately.
- Organizational and staff development - more time for fostering the ability to function independently, and time to organize management and staff prevents potential splintering of staff.
- Flexible use of personnel - staff readily shared among programs, prevents added expenses of hiring additional staff, no need for formal election of new Board.
- Community purpose safeguarded - demonstrates to community a commitment to community and organizational goals.
- Shield from uncertain market - protects enterprise by providing capital or other resources (shared personnel, bulk purchases, absorbing some expenses within other budget items) during uncertain economic times.
- Tax exemption - for the parent if enterprise is related to its purpose.

In-House Disadvantages

- Dilution of purpose -- either from too much neglect (low- priority) or too much attention.
- Parent liability - for claims against in-house activity (significant when there is the chance of personal injury or unexpected cost over-runs; protection from the former can be achieved through adequate liability and workmen's compensation insurance.
- Parent tax exempt status could conceivably be jeopardized - if NET profits of an unrelated activity reach 15% of the total parent organization's budget; spin-off may become necessary. The worst case here is that you would just spin-off the venture. You should be so lucky as to have this "problem!"

Out-of-House (Separating)

Out-of-House Advantages

- Focused program purpose – staff and Board are concerned with a single, unique set of activities, management can focus efforts and resources and should be able to make decisions quickly.
- Inspires confidence and credit - activities removed from controversial activities of parent, has more neutral image that can attract other resources.
- Access to capital and human resources - lenders attracted to separate profit-making ventures whose financial statements and capital structure are clearer to understand, can attract new board members with particular political connections or special expertise.
- Totally protects parent's tax-exempt status - removes any issue about the spin-off's profits affecting the parent's tax exempt status.
- Protection of the parent from liability - a separate venture is responsible for all claims made against it.

Out-of-House Disadvantages

- Loss of control - decisions are made by a separate Board and are not subject to review or approval of parent Board. Disapproval can only be voiced by voting in, or out, Board members at annual elections "Outsiders" may attempt to take control of a profitable subsidiary if membership rules are loose and open (staggered election/appointment procedures and provision for removal of Board members written into the bylaws can prevent this).
- Redundant use of resources and high costs of forming a separate entity - administrative costs for a separate entity are higher than for an in-house program; incorporation costs vary, and a separate entity cannot easily share costs of staff, equipment, supplies, space with the parent. A management contract would enable the new entity to, for example, rent space, 10% of the executive Director's time and 25% of the book keepers time, make 3,000 copies a month, etc.

More points to consider...

While the advantages and disadvantages of keeping an activity in-house or separating it from the parent are useful, they are not absolute. Other organizational indications that a separation may be unavoidable are:

- A need to focus the Board of the subsidiary on a the venture.
- The Board has become over-burdened by too many or too divergent programs.
- A venture operates ineffectively because it is stigmatized by association with the parent.
- Programs and ventures are competing and draining staff or other shared resources.
- Work plan activity of the subsidiary activity is well- developed -- staffing, cash flow and other issues can be reasonably projected to assure its continuance as an independent entity.
- Capital is needed and separation may make it possible to get it.
- New ownership forms serve some goals of the organization: creation of a co-op, selling of stock interest in a specific activity to community residents or employees.
- The "unrelated" operations of an in-house activity threaten tax status of the parent. (Again, this almost never happens).
- Substantial risk is involved in the activity that would cause the agency to assume excessive liability. (The Head Start parents become agitated about your new business venture -- Sky-diving for Tiny Tots.)
- Separation provides tax advantages not available to a nonprofit agency, i.e. tax loss carry-forward and depreciation that shelters profits.

Fiscal reasons may be the most compelling rationale for separation. The in-house option may be more appropriate if the program:

- Fits the tax exempt purpose of the parent – it is clearly related.
- Reduces the likelihood of distraction for the Board or staff.
- Complements existing programs and can take advantage of existing resources.

If you choose the separation option it will be necessary to keep a strict separation between your organization and the subsidiary in the following ways:

- Avoid meddling in day-to-day affairs.
- Separate sets of bylaws establishing membership and voting.
- Separate Board meetings.
- Independent Board minutes, financial records, and contracts.
- Clear separation of personnel responsibilities.
- Separate bank accounts, adequate capitalization of subsidiary.
- Business dealings of subsidiary not restricted to provision of services to parent.

- Separate dealings with clients.
- Subsidiary not held primarily for financial gain of the parent.

Example: The board of the nonprofit adjourns at 10:00 p.m. The Board (mostly the same people) of the venture starts its meeting at 10:15 p.m and votes to authorize payment of \$25 to the nonprofit agency for use of their conference room for the venture board's meeting.

The treasurer of the venture writes the check, which the nonprofit logs in a "unrelated income – space rental to a business."

Control of the Organization that Owns the Venture

"Control" is the ability to make decisions. If you have chosen to create a separate for-profit organization, you will need to decide the extent to which you want the venture corporation's actions to be influenced by the tax-exempt agency. There are two primary methods for doing this: (a) types stock ownership and rights attached to each type -- and the percent of each class of stock you own, and (b) what you put in the bylaws of the venture about making appointments or replacements to the Board of Directors.

The percent of ownership determines the extent of control and the percentage of net profits the owner will receive when the venture declares a dividend to shareholders. If your nonprofit owns 55% of the stock in a for-profit venture, you get 55% of the dividend distribution.

There are three basic level of control; total control, majority ownership and minority ownership. Your rights vary with each.

Majority Owned Corporation (50 percent or more)

In some states, all stock must be voting stock. Thus, control of votes is reduced in proportion to percentage of ownership. This problem can be circumvented. Many corporations incorporate in Delaware where voting rights are not required. By doing so, a corporation can issue non-voting stock in exchange for capital without giving up control. Non-voting members would be entitled to dividends.

Input into operations is still allowed if bylaws are appropriately structured.

If ownership is less than 50 percent the parent is not taxed on some payments received from the subsidiary, e.g., receipt of rent or interest payments from the subsidiary are tax exempt to the nonprofit parent as explained on page 3-11

Subsidiary as Controlled Corporation (50 percent or more)

The subsidiary is considered a "controlled" corporation if the parent owns at least 50 percent. Ownership of "controlled" corporations entitles a holding company, owned by the nonprofit, to consolidate tax returns of those subsidiaries in which the nonprofit has at least 50 percent ownership.

I also recall the Pikes Peak Mental Health Center has a 502 (c) (2) holding company that owns all their buildings and equipment, and leases them to programs.

Input from other sources can occur when ownership is less than 100 percent. Input may be capital from an entrepreneur, community ownership of stock, employee ownership of stock or representation of the Board of Directors by people other than those appointed or elected by the parent organization.

The greater the percentage of majority ownership, the easier it is to retain complete influence over the subsidiary. A minority interest has the potential to create problems and disagreements.

Organizations that spin-off multiple subsidiaries and holding 50 percent or more interest in the subsidiaries have the advantage of consolidating tax returns. Consolidating tax deductions (such as losses, depreciation, and tax credits of one subsidiary) offsets the profits of another subsidiary. Be careful. The IRS requires that **both** parent organization and the subsidiaries be **for-profit corporations**, and owned 50 percent or more by the same parent. (There are other tax breaks and these should be checked by an accountant who has access to current IRS corporate tax rules.) If your organization is at, or reaches, the point where such a complicated business structure is needed or considered, you will need to form a "holding company."

Holding companies are established by nonprofits (the parent) as subsidiaries and in turn own for-profit subsidiaries. As a business structure, it should only be considered where it serves a legitimate business purpose and where there would be an advantage to consolidating tax returns. All issues of separation, extent of ownership and control in establishing a corporation apply. This is a good way to create a tax shelter for your property – to cover losses in a leasing venture.

Holding companies have a disadvantage; they create an additional layer of administration and management and require additional reporting.

The disadvantages of a "controlled" or "wholly-owned" subsidiary are: liability of the parent for taxes on interest or rent payments received from the subsidiary, too tight or complete control reduces incentive of others to contribute to the subsidiary, and stigma if the parent is politically oriented.

A subsidiary is considered "wholly-owned" and completely controlled if the parent owns 100 percent of the stock.

Minority Owned (less than 50 percent ownership)

The greatest opportunities for participation and controlling voice by those other than the parent organization are found in the minority ownership option. Major stock holders may be employees, the community or an entrepreneur. If an entrepreneur is chosen, he or she is given authority to run the operation.

In this option, the parent company provides seed money to attract other investments or additional capital that may not be otherwise available. The parent however relinquishes control of the subsidiary. Although bylaw or charter provisions requiring super majority vote on some issues can grant the minority owner virtual veto power, usually the non-owner's influence is limited to indirect control -- being hired as a consultant or by means of personal rapport.

Another advantage -- dividends from the subsidiary (even a controlled subsidiary) to the parent are passive income and are therefore tax free. The risk of stigma from close ties to a politically oriented parent or social service program is also reduced through this form of ownership.

Forms of Ownership

We will now look at various forms of ownership. The business form you select will become the legal entity that owns your for-profit venture. We aren't lawyers – so this is not legal advice. This is background info for you to use so you do not have to pay a lawyer to explain these basics to you. There are several options you can consider and being aware of the advantages and disadvantages of each will make the final decision that much more informed and, we hope, easier. Again, the corporate form of ownership isn't necessary to start a business. At some point in the course of growth, you may need to reconsider the form of ownership.

Some basic costs (rent, inventory) will not vary in setting up your business. Other costs (especially legal fees) will rise or fall depending on the ownership structure you choose.

We look at several forms of ownership, including another nonprofit corporation, and the more traditional forms of ownership, including Stock Corporation, Employee Stock Ownership Plan, Co-operative, Sub-chapter S corporation, General Partnership, Limited Partnership, and Sole Proprietorship. We start this discussion and will end it with the insight that you are going to need a lawyer to help you do this.

Forms of Ownership - Nonprofit Corporation

Form a new nonprofit whose statement of purpose includes the type(s) of ventures you want to operate.

One nonprofit can always “control” another if it has the right to make enough board appointments, i.e. form another nonprofit and appoint the board.

Sign a management contract for your management staff (e.g. accounting) to help run it on a committed part-time basis, lease it some equipment and space on a cost-sharing basis and you are off and running.

Forms of Ownership - Stock Corporation

A stock corporation allows the parent corporation the broadest range of control -- based on the percentage of stock it owns. At the same time, the parent enjoys protection not available in other business forms. The key features of a stock corporation are: it owns property and conducts business in its own name, it can sue or be sued, earnings are taxable.

Stock Corporation Advantages

- Liability of the owners is limited to the extent of the value of shares held.
- Transfer of stock ownership is relatively easy unless controlling interests of stock are being exchanged.
- A corporation has perpetual life. It is considered to exist in perpetuity no matter who the owners are.
- Decision making power is proportional to the amount of stock held by a shareholder (except in states where cumulative voting is required).
- Centralized management, owners elect a board who sets corporate policy and selects top management.

Stock Corporation Disadvantage

- Double taxation because corporate earnings are taxed and after-tax earnings distributed to shareholders as dividends are also taxed (in many instances this may not be as bad as it seems: the corporation reduces taxable income through deductible expenses; for-profit corporations receiving dividends from other "allowed" corporations can deduct 100% of dividends received if they are members of an affiliated group or 85% if they are not, and individual shareholders are also entitled to a dividend exclusion).

Obviously these are complex matters and you will have to secure expert advice. The discussion here is just to get you going on this and to give you some basic information so you do not have to pay an expert to give you basic training.

Forms of Ownership - Employee Stock Ownership Plan (ESOP)

The Employee Stock Ownership Plan can be a useful option:

- As a vehicle for employee ownership and control of a business that complements the parent organization's social goals, and
- As a way to raise capital at a lower cost than direct borrowing or by a public offering of shares in the business.

The core of the ESOP is a trust owning stock in the company. The trust acquires stock over the years as the company contributes shares of stock or cash to purchase stock. This method is used when ownership will be ultimately transferred to employees.

Raising capital is relatively easy. The trust can borrow money and use it to purchase newly issued stock from the company. The company then makes annual payments to the trust who in turn repays the bank. In most ESOP's, employees start with a small percentage of ownership, however a community organization can advance social goals by ultimately transferring ownership of the company to the employees.

ESOP Advantages

- Provides incentive of ownership, when accompanied by real participation in decision making, productivity is increased. (Amount of annual contribution can be tied to performance level compensation but no more than 15% total payroll per year.)
- Capital can be raised at low cost (without outside investors at the expense of loss of control) because of readily available pool of equity in trust.
- Reduced taxes through stock contribution to trust which is treated as a business expense deduction, or a large contribution that creates an operating loss that can be carried back to previous years to offset taxes paid at that time.
- Creates a ready market for stock where none existed, shareholders can liquidate their equity by selling stock to the ESOP.

ESOP Disadvantages

- Can dilute ownership and earnings over time depending on voting rights of the stock issue (should be checked, as state laws vary).
- May decrease borrowing capability if debts exceed equity ratio.
- The right of repurchase of stock may strain finances if poor flow situation exists.
- Intricate legal details make setting up an ESOP fairly expensive and difficult.
- Employees are exposed to some risk if the ESOP is used as a pension plan, as retirement benefits are tied to the future of the company.
- A corporation can use an ESOP to unload a marginal company; this happens when a corporation sells interests to employees while knowing the business is not good.

Forms of Ownership - Cooperatives

Cooperatives are another vehicle for achieving business and social goals. A cooperative is controlled by its members - one member, one vote. Control comes from within the membership, not from outside shareholders who are neither consumers or involved in production activities. Membership is often limited to those in like circumstances. There are three types of cooperatives:

- Consumer Co-ops such as food or housing co-ops, and credit unions; members pool efforts to provide a good or service to themselves that they do not produce.
- Producer/Marketing Co-ops are often used by farmers who run individual farms; members lease commonly owned land in a producer co-op; and, in a marketing co-op share the sales outlet for the goods they produce.
- Workers Co-ops are structured so company employees are its owners; members work to produce goods or services they may or may not consume.

A co-op is a distinct entity. It can own property. Management can be centralized by selecting a Board of Directors who can make operating decisions and hire staff. Profits can be distributed to members (this is known as patronage dividends) on the basis of a member's dollar volume of transactions with the co-op. The advantages and disadvantages are:

Co-op Advantages

- It is a completely democratic form of business. The people who are affected by the decisions are the ones who make them.
- Lower costs through bulk purchases, member contributed labor, equipment sharing, and pooling of produce.
- Taxable profits may be reduced to zero by distribution to members; a co-op may retain up to 80% of earnings for future business needs and members pay individual income tax on their pro-rated share of earnings -- they are not taxed later when actual cash dividends are received.

Co-op Disadvantages

- The organization that creates it has no control.
- There may be legal restrictions in the state.
- Organizational costs may run high for a time if efforts are expanded to maximize participation in the decision making processes.

Forms of Ownership - Sub-Chapter "S" Corporation

This form of organization has potential for smaller nonprofits even though it is better suited to private individuals in the business world. IRS allows it as a means of giving owners a smaller business limited liability protection without subjecting their earnings to double taxation.

In a conventional "C" corporation, profits are taxed at graduated corporate rates. Salaries of officers are deductible expenses and, consequently, reduce corporate profit subject to taxation. Salaries of officers are also subject to individual income tax. If salaries become too high, the IRS may treat the excess as a dividend. This means double taxation on the corporation because the same money is taxed as part of corporate profit and as income to individuals. Sub-chapter S corporations are taxed in the same way as a proprietorship or partnership to avoid this problem.

To qualify as a sub-chapter S corporation, you must meet the following IRS requirements:

- Have individual shareholders
- Have no more than 75 shareholders
- No shareholder may be a non-resident alien
- Have only one class of stock
- No more than 80 percent of gross receipts may come from outside the United States
- Gross receipts from royalties, rents, dividends, interest, annuities, and gains on sales or exchange of stock securities may not exceed 20 percent

A corporation may not be a stockholder in a sub-chapter S corporation. This last item is of prime concern. It excludes a community organization or its subsidiary from any ownership interest or control. It could, however, be a useful option in attracting a private entrepreneur to develop a non-subsidiary business.

Sub-Chapter "S" Corporation Advantages

- Stockholders do not assume unlimited liability; each owner's (stockholder's) financial risk is limited to the amount invested or loaned.
- Protection from double taxation.
- Tax deductible expenses -- fringe benefits are deducted as operating costs and not treated as taxable income.

Sub-Chapter "S" Corporation Disadvantages

- Stockholders must be individual citizens who all agree to this form of ownership.
- Corporations may not hold stock, which presents difficulty in raising capital.
- Corporate investments are limited; no wholly-owned subsidiaries are allowed.
- Tax shelters are limited because the shareholder is limited to his/her share of the

net operating losses that s/he may deduct from personal income; deductions can be made only up to the value of stock owned or any loans made by the individual.

Forms of Ownership - Partnerships

A partnership is an unincorporated business formed by two or more people. It is very easy to set up and allows a pooling of money, talent and experience. It also carries with it a personal risk of financial loss -- either partner can commit the resource of the venture. Misunderstandings, responsibilities, roles and uncertainties must be thoroughly discussed and defined as early and clearly as possible -- and put into writing! A written partnership agreement will protect the partners from future misunderstandings. Discussion about creating a partnership agreement should include the following and be described in detail:

1. The name and type of business.
2. The partnership business purpose.
3. Amount invested by each partner -- cash, property or services, method and timing of capital contributions specified, and determination of true market value of services or property to be transferred to the partnership.
4. Duration of partnership -- a specific beginning date if the partnership was formed for business purposes having a certain time limit.
5. The amounts of salaries, method of payment, salary balance, (does each partner receive the same or differing amounts?) deduction of salaries as an operating expense prior to profit distribution.
6. Additional capital contributions and the circumstances requiring additional contributions and provisions if a partner cannot make additional contributions.
7. Division of work and duties, specific amounts of time to be devoted to the partnership, authority boundaries and responsibilities of each with job descriptions, restrictions on authority, especially in expenditures.
8. Profit and loss distributions, how profits will be shared, equally or otherwise, when and how profits will be distributed.
9. Distribution of assets in case of a dissolution.
10. Provisions for dissolving the business.
11. Provisions for withdraws or admissions of additional partners.

12. Dispute settlement.
13. Settlements or provisions in the event of death or incapacity of a partner.

Forms of Ownership - Limited Partnerships

A limited partnership has some of the benefits of a partnership and a corporation. A limited partnership is usually a short-term partnership formed for a specific purpose or project. Partners are designated as either a "general" or "limited" partner. Their responsibilities to the whole partnership are distinct and clear:

- General partner provides management skills, know-how and control.
- Limited partner provides the capital.

Many real-estate ventures are organized with one general partner and several limited partners.

A corporation (for-profit) may be either a general or limited partner. If it is a general partner, all of its assets are at risk. If a corporation is a limited partner, it is protected from risk because the stockholder's liability is limited to the value of their stock. (Legalities of this form of partnership are very complex; consulting a lawyer is highly advised in setting up a limited partnership). This type of business form attracts investors willing to put up money and looking for tax advantages but who do not want to risk personal liability.

Nonprofit participation in a limited partnership is hazy; no clear policy has been established. Activities of the limited partnership may be viewed as "unrelated" business. To avoid jeopardizing nonprofit tax exempt status, a subsidiary for-profit could be established as a partner to protect the parent organization.

Limited Partnership Advantages

- Highly attractive to investors because of tax shelter benefits (income is treated as taxable personal income of the partners).
- Joint ventures are possible (a partnership set up for a specific project **without** setting up a separate corporation, selling stock or appointing a Board of Directors).

Limited Partnership Disadvantages

- General partner assumes unlimited liability for claims against the business.
- Vulnerable to dissolution at any time unless otherwise specified in the agreement.
- Limited life of partnership (specific time frame or "life" of general partner).

- Any change in general partner must be agreeable to other partners and a new agreement must be devised.
- Limited partners have no restrictions on transferring their interests.

Limited partnerships are one way to develop public/private sector partnerships since either entity can be a limited or general partner. Self interest is a corporate motivator. Many private sector corporations want improved public images, stable communities in which to do business and quality employees. A limited partnership business formed between a private sector corporation and a community based organization can benefit both partners.

Forms of Ownership - Sole Proprietorship

One person owns it all. In the business world, this is the least expensive way of starting a business. In the nonprofit world, it would prove costly in terms of the community. There would be a high risk of showing favoritism in setting up one person in business and not another, and a subsequent drain on the parent's resources with no return from the proprietorship.

Proprietorship Advantage

- Least expensive way to start a business; and it's clear who is in charge.

Proprietorship Disadvantages

- Single owner has absolute control over all aspects of the business. The nonprofit who helps them start it has no control. This may be the purpose of a program – such as a microbusiness program – but it is not a way for a nonprofit to start a venture itself.
- All income taxable to proprietor, tax rate dependent on income bracket.
- Business totally dependent on actions of proprietor.
- Source of capital limited to assets of the proprietorship; ability to raise capital depends on personal reputation of proprietor.
- The sole proprietor is personally liable for business debts.

There are risks and disadvantages in this form of ownership. We can't think of any reasons why a community organization would choose to develop a sole proprietorship for its venture when there would be no direct control or direct ownership interest.

The main point of this chapter is that there are all kinds of ways to structure ownership or control of a venture. You can pick the degree of control you want to have, balance that against the advantages and disadvantages of each type of ownership, and figure out how to move the money from one entity to another –depending on the type selected -- through management contracts, dividends, and gifts.

Don't spend a lot of your time agonizing over structure decisions. Decide what you want out of the venture and get a lawyer to structure the ownership and relationship so that it happens.

The Preliminary Choices

By this point a lot of critical material will have been covered, a number of decisions made. Before filing the official documents that make your venture a legal entity, review the ground work to see if there are any remaining issues that need to be resolved:

Discussion and decisions have been made on the following:

Decision	Yes	No	Outstanding Issues
Non-separation			
Separation			
Control			
Majority Owned			
Controlled Corp.			
Holding Company			
Minority Owned			
Form of Ownership			
A Nonprofit Corporation			
Stock Corporation			
ESOP			
Cooperative			
Sub-Chapter S Corp			
Partnership			
Limited Partnership			
Proprietorship			

Another checklist appears on the following page. It is not exhaustive, nor does it cover all situations.

Get a lawyer!

Legalities Checklist

- ___ 1. Corporate name decided
- ___ 2. Articles of Incorporation and Bylaws drafted, reviewed by legal counsel, governing body, staff or others as needed
- ___ 3. Filed or applied for:
 - State Charter.
 - Federal Tax-exempt Status Forms (yes, a c-3 can control a c-3)
 - Social Security Election Form
 - Federal Employer Identification Number
 - State Employer's Withholding Tax Registration
 - State and local Sales Tax License (if goods are to be sold)
- ___ 4. First Board meeting arranged, with minutes reflecting:
 - Acceptance of office by members
 - Adoption of Articles and Bylaws
 - Adoption of Basic Policies and Procedures
 - Designation of management authority, including authority to hire staff and conduct business
 - Approval of budget, including specific authorization for any budgeted liabilities
- ___ 5. Approval by Board/Governing Body of:
 - Loan agreements
 - Lease agreements
 - Purchase of service contracts, management contracts
 - Shared staff arrangements
 - Subcontracting arrangements, cost allocation agreements
 - Customer referral agreements with the parent
- ___ 6. Record keeping systems for use in completing Federal Report Forms (e.g. 990) developed
- ___ 7. All documents reviewed and approved by legal counsel and auditor or accountant

O.K. You are exhausted by the technical stuff, and you haven't even opened the doors on your business yet. This stuff is all necessary but not sufficient to ensure business success. Now, it's time to "get down to business."

C. Analyze the Competition

Highlights of This Section...

1. Who is your competition?
2. Who are your customers?
3. How can we position our services?

Try to gauge the strengths and weaknesses of each competitor. Shop your competition by calling them or going there, then write your opinion of each principal competitor.

	Competitor 1:	Competitor 2:	Competitor 3:
Principal Product			
Facilities			
Marketing Characteristics			
Labor Pool			
New Product Development. How do they do it? How often?			
Adaptability to Changing Market Conditions			
Customer Service			

Rating the Competition

Have any of your competitors recently closed or scaled down operations or withdrawn from your market area? State the reasons if you know them:

	Competitor 1:	Competitor 2:	Competitor 3:
Closed or Scaled Down Operation?			
Withdrawn from Market? (State which market or markets)			
Reasons for Closing, Scaling Down, or Withdrawal?			

More competitors can mean a growth industry! A decrease in competitors may mean a declining industry – or a mature industry in which the “biggs” are forcing out the “smalls.”

Advantages over Competitors

Below is a list of characteristics which may indicate the advantages your product(s) or service(s) enjoy over those offered by competitors. These characteristics are the basis for capturing your projected share of the market. Think about each characteristic; for example, a higher price may not be a disadvantage if the product is of higher quality. Spell out the specifics of each characteristic; the unique characteristics of your product can be the used in advertising and sales promotion. Use one worksheet for each competitor.

	Product #1: Advantages/Disadvantages	Product #2: Advantages/Disadvantages
Price		
Quality		
Performance		
Labor pool		
Versatility		
Speed or accuracy		
Ease of use or operation		
Size or weight		
Style or appearance		
Other characteristics not listed:		
What, if anything, is unique about your product?		

D. Identify and Describe the Customer Groups

Highlights of This Section...

1. What are the basic elements of marketing?
2. What is market segmentation?
3. How do I do market research?
4. How to write a customer profile statement.

The Five P's of Marketing

1. **Public** -- the WHO
2. **Product** -- the WHAT
3. **Price** -- the HOW MUCH
4. **Place** -- the WHERE and WHEN
5. **Promotion** -- the WHY BUY

Successful recruitment requires attention to all of the five P's.

Promotion Is Last ... not first. You can have perfect promotion and if the target public is wrong, the product is poor and/or non-responsive, the price too high (or the benefits too low), and the place of distribution (including timing) is inconvenient -- you will have poor sales.

Marketing Is More than a Pretty Brochure and an Annual Report!

It **Begins with the Customer** ... and not with the service provider! It's not what you're providing, but what they are **needing**. Listening to the customer means putting yourself in your customer's shoes, seeing the world through his/her eyes.

When you have Too Few Customers, it is, unfortunately, Your Fault. You will need to change one of the five P's to attract more customers ... because it is unlikely that you can change the customer's preferences to meet your needs.

Marketing begins with the **Customers Needs, Wants, and Habits:**

- ... that leads to the development of a responsive service;
- ... that will be priced right;
- ... that will be easy to obtain; and
- ... that will be communicated in a way where it can be heard on the customer's terms.

Marketing Is Everybody's Job in the Shop ... from the volunteers who ring up

merchandise to the manager or owner. Everyone assists the customer and defines the service that makes it either attractive or unattractive to buy.

Marketing, like everything, **Costs Money ... But Not Necessarily a Lot ... Or Even More than You're Spending Now.** Spend your limited marketing dollars strategically.

Public: Segmenting & Targeting Your Markets

1. The Who in the major market is really not homogeneous ... it varies in age, size, demand, need, gender, values, etc.

Of the 100,000 people living in a five-mile radius of our shop, we have several market segments with distinct characteristics. Some of these are described below.

2. Again, each market segment will want the service for a different reason. A separate marketing strategy will be needed for each priority market segment.

Market									
Segment A		Segment B		Segment C		Segment D		Segment E	
Target Each Segment According to Their Specific Needs and Wants									

Our market is made up of three target market segments: professional women in the workforce, college-age women, and women with young children. Professional women are looking for designer clothing at reasonable prices, college-age women are looking for casual clothing at low prices, and women with young children are looking for good quality children's clothing at reasonable prices.

3. After segmenting your major market, the next step is to set priorities -- **Target Marketing.** (Which market segments will be your priority customers?)
We will target professional women because they will visit the shop often and spend more money than our other market segments.

4. Target marketing means emphasizing different benefits and different choices of communication methods -- **go where the customers are and solve their unique**

problems.

After deciding who will be your target market segments, you can plan to **reach them by:**

- **Media** - Choose the media that is most appropriate to your target market -- Where do they go? What do they read? When can they best be contacted?

We will target working women through mailings to members of women's professional organizations.

- **Message** - Choose the benefits your shop offers that will solve the particular problems of the target market; communicate your shop in a way that targets customer's needs.

We will be open until 8PM during the week to allow women to shop after work.

- **Methods** - Design and modify your shop's offerings to meet the specific needs and/or preferences of your market segment.

If three out of every five women who come in ask if you ask for bridal wear, or resort wear, or maternity clothes -- have it the next time they come in!

Market Research Options

- 1. Be your own customer ... "shop your own store"**
- 2. Use your current customers** as a research sample
- 3. Use focus groups.** Ask potential customers that represent your target market about your product, your price, your place, and your promotion
- 4. Evaluate current efforts** and modify for increased effectiveness
- 5. Analyze demographic statistics** prepared by others
- 6. Try Questionnaires and Surveys ...** by mail, in publications, in your agency's waiting room, on the street, door to door, at tables in areas heavily trafficked by your target market. Use your surveys as promotional tools, as well as information collection tools.
- 7. Use what is effective for your competitors.** How do other thrifts local shops in your area market their shops to similar target markets? Do you fill a different niche market? Perhaps they will refer people to your shop.

Elements of a Customer Profile

Can you describe your targeted customer in less than ten sentences? Can you answer the following questions? An example of a customer profile for a thrift shop follows this exercise.

* Who are your customers?

* Where are they located? _____

* What are their needs and wants?

* What are the benefits of your product that meet their needs/satisfy their wants?

* What does their typical day look like -- what do they read, what do they watch, where do they go?

* How are they most likely to buy and where?

* What are the costs to them to buy the product? Do the benefits outweigh costs?

* Do they **want** the product or do they **need** the product? (Needs outweigh wants; the price for a **needed** product can be higher than for a **wanted** product).

* How many of them are there? _____

If you can't describe your desired customers - you won't be able to find them!

Examples of a Real-Life Customer Profile Statement

Example 1: A Thrift Store in Alabama:*

1. Income: \$0 to \$12,000 per year
2. Age: 19 - 25 years old
3. Single
4. Female
5. Receives public assistance
6. Value seeker / price conscious
7. Value seeker / quality of clothing
8. Has pride in the ability to purchase “smart” versus receiving give-away items
9. Urban / inner city resident
10. Public housing resident
11. Strongly influenced to make seasonal purchases (Christmas, Easter, back-to-school, etc.)
12. Non-credit card user (not eligible for extended payments, checking accounts)
13. Seeks purchase of household goods to ease household duties (toasters, microwaves, irons, etc.)

As a result of the thrift store shopper, the store communicates the following benefits to the shopper:

1. Quality clothing at a low price
2. Used appliances at a low price
3. An increase in purchasing power (more for your money)
4. No membership/application fee (not blocked by application process)
5. A wide variety of goods to choose from

*Thanks to Carol J. Poe of the Jefferson County Committee for Economic Opportunity for sharing this profile with us.

Examples of a Customer Profile

Example 2: Senior Tours Business Operated by a Tennessee Community Action Agency:

1. Females
2. Age 60 -- 80
3. Money conscious
4. Like to travel
5. Income between \$8,000 and \$10,000 (enough to pay for some travel, but not so much they can pay full prices on their own)
6. Health relatively good
7. A desire to explore, curious about the world
8. Talkative, gregarious
9. At least 5th grade education
10. A sense of humor
11. Retired or other wise free to travel
12. Low use of medication that might require them to stay at home
13. Attend church fairly regularly
14. Trust other people
15. Live alone

Examples of a Customer Profile

Example 3: Equipment Storage Sheds manufactured by an Alabama Agency

(This represents one target market segment of potential purchasers)

1. Urban or suburban area
2. On a lot of one-half acre or larger
3. Family income over \$25,000
4. Children, one year old or up, e.g. toddlers or above
5. Other kids in neighborhood
6. Two car garage, with two cars in it
7. Owned or recently purchased a riding mower, rototiller, chain saw, leaf blower, or other power equipment (The more power equipment the better. Can get lists from manufacturers warranty returns or local retailers)
8. May have other seasonal gear, skis, boat, horse saddles, etc.
9. No straight-in access or rampway to their basement, stairway only

From these customer profiles, list what the agency wants to communicate to the shopper in terms of benefits:

Example 2: Senior Tours Business Operated by a Tennessee Community Action Agency:

Example 3: Equipment Storage Sheds manufactured by an Alabama Agency:

Positioning: The Battle for Your Mind

Now, combine the results of your analysis of your competitors and your analysis of your customers. The “positioning” process invented by Trout and Reis is an excellent framework for doing this.

To cope with the product explosion, people have learned to rank products and brands in the mind. Perhaps this can best be visualized by imagining a series of ladders in the mind. On each step is a brand name. And each different ladder represents a different product category.

Some ladders have many steps. Others have few if any.

A competitor that wants to increase its share of the business must either dislodge the brand above (a task that is usually impossible) or somehow relate its brand to the other company's position.*

* *Positioning: The Battle for Your Mind*, by Al Ries and Jack Trout, Warner Books, 1986. (Highly recommended!)

How to analyze and use the ladders in your target customer's mind

1. Each target market group, by definition, has shared perspectives and opinions about a product or service. You must understand the target market, their socioeconomic characteristics, values, etc. This is your "customer profile statement." The customer profile statement is written for each homogeneous group who share a common set of elements that will influence or lead them to a purchase decision for the product or service.

2. Before you can determine your ranking on the target customer's product ladder, you must also analyze your competitors and their benefits. Competitors for our products come in two types. They are:

a) **Direct Competitors.** These are other organizations (private, public, and/or nonprofits) that offer similar products to your products, and that are realistic options to customers who choose to buy a product or service to solve their problem. The reasons why your target market group select one of your direct competitors are called their *Key Success Factors*.

b) **Customer Alternatives.** There are always other options to "solving the problem" besides buying a product or service from you **or** your direct competitors. These include:

(i) doing nothing and living with the problem;

(ii) "self-help," deciding to solve the problem by the customer's own action; &

(iii) seeking help from peers and family rather than buying from a formal organization.

The reasons why your target market group select one of your indirect competitors, one of the customer alternatives, are called their *Attractions*.

3. After you have analyzed the target market and analyzed your competitors put yourself inside the mind of your target market. How would that target rank the competitors and alternatives? Be realistic. Where would **you** fall on the target's ladder -- which rung? Honesty is the key here: it is better to be lower on the ladder and know where you are than to delude yourself. Knowing where you are gives you an opportunity to use your position, whatever it may be, in your marketing. Fill in the ladder below.

Your Target Customer's Mind Ladder: Rank all your direct and indirect competitors and yourself on the ladder.

	Competitor	Success Factors/Attractions
Rung 1		
Rung 2		
Rung 3		
Rung 4		
Rung 5		
Rung 6		
Rung 7		

4. After developing each target group's mental ladder (with the rank of your product and your competitors'), you are now ready to position or re-position yourself and your product. You want to make a statement **about your level** on their mental ladder, about your place in their perceptual ranking, and why this is a benefit to them.

You want to make a statement about **the reasons why** you are where you are on the ladder, e.g. about your *Key Success Factors* or why you are preferable to other *Attractions*, and why this is a benefit to them. This can be done in two ways. One is described in # 5 below, the other in # 6.

5. The first approach is to **position yourself against those on higher rungs**. Turn what they are ... and what you are not ... into your asset.

Examples of "Positioning Against" a Leader:

Product Ladder	Product Leader	Positioned Product
Soft Drinks	Colas	"The UnCola" (7UP)
Rental Cars	Hertz	"Avis: We Try Harder"
Mental Health Program	Large Institution	"Personalized Attention"
Private Practice	Very Busy	"Immediate service, at your convenience..."
Top Group	Class Act	"Reasonable fees"

Oldest in Town	Experienced	"Modern day training .. most recent techniques"

6. The second approach is to **develop distinctive competence**. This is a narrow range of excellence, or product niches, in which you exceed other competitors. This communicates what separates you from the pack, i.e., from all of the others on the ladder. It may also offer an alternative to the indirect Attraction.

Examples of Distinctive Competence:

"The largest..."

"The one chosen by..."

"The only..."

"Specialists in..."

"For women who..."

"For those in XYZ community..."

Examples of Alternatives to other Choices:

"Instead of hurting..."

"Enough is enough. When anger goes on forever..."

"You can get through it..."

List some other phrases that might be used to differentiate your agency or service from the competitors by communicating your distinctive competence, or by describing you as a better alternative.

Differentiation through distinctive competence:

Alternative to Indirect Attraction:

Note: For both **Positioning Against** and for **Distinctive Competence** you should not use differences that are inconsistent with how your target market understands the world.

If you are fabricating differences the target will dismiss your claim because it is not consistent with the ladder in his or her mind. If you say you are the "only ones in community X or specialty Y..." it had better be true. Otherwise it is a strike against you. "They don't know what they are talking about." Or worse, "They are lying to me."

Similarly, differences that you may perceive as real but that the target market does not perceive as meaningful or real are at best irrelevant, and at worst are costing you customers. At minimum they are taking up space that should be filled with a real message. At worst, they are turning people off or sending them in some other direction.

Test your messages by asking **Real People** from your target market if they understand and believe what you are saying.

Select a few of the best statements to use for this one target market. THEN, USE THEM **C O N S I S T E N T L Y**:

- a. In your brochures, letters, press releases, reports, etc.
- b. In your conversations when friends ask you "what do you do?"
- c. In talking with customers when you are describing your services
- d. When board members make presentations
- e. Other places???
- f. Still more places???

Use the worksheet on the next two pages to analyze each of your separate products or services.

Worksheet: Positioning

1. ONE Product or Service_____

2. ONE Selected Target Group: Customer Profile Statement

3. List Your **Direct Competitors**/Their Key Success Factors

- a. _____ / KSF's
- b. _____ / KSF's
- c. _____ / KSF's
- d. _____ /KSF's_____

4. List **Indirect Customer Alternatives**/Key Attractions

- a. _____/KA's_____
- b. _____ / KA's_____
- c. _____/KA's_____

5. **Your Target Customer's Mind Ladder:** Rank all your direct and indirect competitors and yourself on the ladder.

**Competitor / Success
Factors/Attractions**

Rung 1: _____/_____

Rung 2: _____/_____

Rung 3: _____/_____

Rung 4: _____/_____

Rung 5: _____/_____

Rung 6: _____/_____

Rung 7: _____/_____

8. Select a few of the best statements to use for this one target market. THEN, USE THEM **C O N S I S T E N T L Y**:

- a. In your brochures, letters, press releases, reports, etc.
- b. In your conversations when friends ask you "what do you do?"
- c. In talking with customers when you are describing your services
- d. When board members make presentations
- e. Other places???
- f. Still more places??? _____

The Business Perspective

Up to this point the focus has been on profit-making from a nonprofit perspective. Let's, for a moment, switch sides and look at a venture from a business viewpoint. You need to have some indication whether the business you propose is feasible from a business perspective and whether it meets the intent of your organization. The following list can be adapted to suit the particular conditions of your organization if needed.

- * Is there a real market for the venture's goods and services? Is it relatively stable and will it increase over time?
- * Does the business require large amounts of initial capital and would large debt financing hamper the business start-up phase?
- * Is the organization willing to share ownership and provide equity financing if needed?
- * If the business fails, will the organization be saddled with a large debt, unused and unsalable inventory and staff unemployment?
- * Does operation of the business result in significant training and experience from community members and organization staff?
- * Are there significant opportunities for community members to assume management and staff responsibilities?
- * Will the venture create problems (health hazards, pollution, noise).
- * Will revenues and profits generated by the business be returned to the organization for use in other activities?
- * Are goods and services available to all members of the community or are they restricted in any way?
- * Is the market for goods or services one that other community groups might easily capture?
- * Have all the ways financial benefit can be accrued been identified (e.g. rents, royalties, interest, securities, sales and assets)?

When you think these questions can be asked you will have made basic business decisions and chosen a direction for your profit-making venture. If the questions aren't easily answered, there may be issues or concerns that need to be reviewed and openly discussed with your Board and staff. You may want to keep the following in mind:

- * You need financial sophistication to run a business.
- * Seek investments, not gifts.
- * Don't drain the nonprofit's resources.
- * Problem solvers are needed on the Board.

4. Business Planning and Operations

This section describes (a) options for business plans, (b) target marketing, (c) pricing, (d) location, (e) financial analysis, (f) business life cycles and the relevance for financing, and (g) some sources of financing.

A. Prepare a Business Plan Outline

Highlights of This Section...

What is in a business plan?

A business plan may be necessary for a large enterprise, you are seeking investors, or loans, or if you are spending more than \$10,000 in start-up costs. The basic purposes are:

- To give you a path to follow with goals and action steps allowing you to organize and guide your business;
- It is THE presentation document to use when looking for financing; and
- It helps you to develop as a manager, and, used over time, can help increase your ability to make judgments.

Some of the topics to be covered by a business plan has already been covered. You now need a framework in which to put the material.

On the following page you will find a one-page business plan outline. Either follow the outline or move the elements around to suit your approach. One of the major keys to writing a business plan is to condense and summarize essential material.

Following that there are two different business plan outlines - a short version and a medium version. For a long version, see the Appendix for US Small Business Administration's sample business plan.

Business Plan Outline - Short Version -- The Official GOOD IDEA Form

This is an official form, cleared for adoption by all nonprofit agencies by the Society of Intrapreneurial Explorers. It was created to assist in the early process of exploration and consideration of an idea, to structure the answer -- sort of -- to the key question: Is this a GOOD IDEA? Or what?

- a. date
- b. what's the notion/glimmer/idea for this product or service
- c. why is this needed?
- d. by whom is it needed? what are the characteristics of potential customers?
- e. what specific benefits does this idea provide -- that meet the needs of the customers?
- f. what are the names of three real people who are potential customers -- with whom I can explore this idea
- g. so what did they say about this when I called them? Be honest! Shall I call 3 more?
 - 1.
 - 2.
 - 3.
- h. what is the development process/cost/date by which I can have a prototype to show to, or saleable idea to explain, to customers?
- i. who are three real competitors? Why can we compete? What is our sustainable competitive advantage?
 - 1.
 - 2.
 - 3.
- j. what is the potential payoff for this idea; units sold x price = gross revenue minus estimated cost = profit.
- k. who should be in my skunkworks?
- l. does this idea need a champion? when? who is the champion?

Business Plan Outline - Medium Length Version

A. Cover Page with Business name, address, contact information

B. Statement of Purpose/Executive Summary

Describe the purpose of the plan, business structure, owners, and information pertaining to loan payback if applicable.

C. Table of Contents

D. The Business

- Background and History
(What business are you in?)
Products/Services Description
- Market Information
(Who are your customers, how many are there?)
- Competition (Why are you better?)
- Marketing Strategies/Milestones
(How will you reach customers?)
- Location
(Why did you choose this location?)
(What renovations are needed?)
- Licenses, Permits, and Insurance

E. Financial Data and Information

- Projected Balance Sheet
- Income Statements (Profit and Loss Statements)
- Cash Flow
- Money-leveraging Strategies

F. Administration and Management

- Organization
- Key Personnel
- Incentives for Key Personnel
- Management System

G. Appendices: Possible Details Regarding...

- Products and/or services; market research; resumes of key personnel; references for key personnel; references for the business; copies of contracts; copies of leases; sales closings that will be used; photographs of the business; etc.

B. Continue with Customer Analysis – And Target Marketing

Highlights of This Section...

How do I research my target market?
What should be included in a marketing plan?
How do we promote the business?

Low-cost Market Research Techniques

There is an abundant amount of information available for your marketing analysis – in most cases all you have to do is ask. Here is a list of low-cost resources available to you:

Government Resources: Your local offices of the US Small Business Administration, Small Business Development Center, Service Corps of Retired Executives, regional/local economic development offices, and related programs offer many valuable resources. Check the Appendix for a list of Business Information Centers (BIC). BICS have many resources ranging from books, videos, CD-ROM, and Internet access, available for free use. Census data is widely available to help narrow your target market.

Your Agency: Talk your business idea up with everyone and anyone. Find out the best way to communicate with your target audience.

Competition: Gather advertisements from your competition and analyze them for effectiveness.

State Agencies of Transportation: These agencies keep detailed traffic counts for state roads and can guide you to resources for local traffic counts. They can help answer “how many people ride by my location in a car?”

Trade Organizations: Specialty trade organizations have business directories and trade publications available for a small charge.

Market Planning Analysis - Marketing Plan Elements

- A. Executive Summary
- B. Who is Your Market? Describe age, sex, occupation, lifestyle, income, etc. of your various market segments.
- C. What is the present size and growth potential of the market? Clearly define your target market. What is your expected share of the market?
- D. What percent of the market will you have now and expect in the future?
- E. How will you **attract** and **keep** your segment of this market? Describe product quality, price, public relations, and selling strategies.
- F. How will you advertise? Discuss your choice of media.
- G. What form of product distribution will you use and why? How will you ship your products?
- H. What features or services will you offer that will justify your price?
- I. How will you handle credit sales? Will you extend your own credit or accept major credit cards?
- J. Monitoring System. How will you determine the effectiveness of your marketing strategies?
- K. Marketing Budget

Sample Marketing Plan - Business: Boat Buddies

I. Overview

Product Line Description

A line of unique fishing tackle boxes, made from durable plastic materials, designed to be attached to the hull of a fishing boat. The product has a patent pending.

Business Description

- A manufacturing company, in its formation stages, to be located in the Midtown, Mississippi area.
- The company will be incorporated.
- Initial capital investment is estimated to be \$20,000.
- The location of the business provides easy access to component parts produced locally and is centrally located for efficient delivery of products.
- The markets to be served are:
 - Short-Term (first year): The States of Mississippi, Louisiana, Tennessee, Arkansas, and Alabama
 - Long-Term: Nationwide

Industry Description

The target consumer for this line is the sport fishing boat owner. The tackle box industry is to be considered in pricing policies only.

Market Conditions

- Economic Issue
- Industry sales appear to be impacted by Disposable Personal Income (DPI). Research (quote your own source) indicates a 10.15 percent DPI increase in the last year and a projected DPI annual growth of 9.2 percent over the next three years.

Size of Market

Outboard motor boat sales for the last five years were 2.386 million units (quote source). Projecting sales over the next five years using an average of the previous period and assuming 75 percent of those of the previous period are still in use, results in the potential of those plus 298,250 new boat owners in the regional market.

Sample Marketing Plan - Business: Boat Buddies (con't)

II. Marketing Issues

Customer Profile - Fishing boat owners

- Hold a high to moderate interest in fishing
- Currently own fishing tackle boxes
- Read or subscribe to fishing magazines
- Occasionally watch fishing programs on television
- Occasionally attend boat and fishing expositions
- Occasionally participate in fishing contests
- Male head of household

Product Positioning

The product line is to be positioned as a new convenient accessory for fishing boats.

Its function is to provide added convenience for the boat fisherman.

The product's advantages are to be perceived as: 1) convenient, fast access to fishing lures; 2) safe storage for fishing tackle; and 3) added value to the fishing boat.

Pricing Issues

- For fishing boat owners: While the product is not considered competitive to tackle boxes currently in use, pricing must be perceived as a value to the consumer as compared to the tackle box they now own.
- Cash discounts need to be offered to all market channels. Customary terms of 2 percent discount if paid within 10 days; net due in 30 days is advisable. If pricing is to be offered on a delivered basis, average freight costs must be included in the published price list.

Packaging Issues

Products distributed through market channels for boat owners should be shrink-wrapped with a brochure explaining product features and installation instructions. Twelve items packed in a cardboard shipping container. Copy on shipping container should include the name of the product, name of the manufacturer, product code number, and gross weight of case. This information should appear on front, back, and both end panels.

Distribution Issues

Sales Service

An office procedure needs to be developed to coordinate orders received, production scheduling, shipping, and invoicing.

Sample Marketing Plan - Business: Boat Buddies (con't)

Shipping Issues

Shipments to market channels serving boat owners should be scheduled through UPS for orders less than five cases. Larger orders are to be shipped via common carrier. Delivery schedules need to be established and customers advised.

Storage Issues

Raw materials/components from suppliers.
All components are manufactured locally. Proper order scheduling will keep storage needs at a minimum.

Finished Goods

Depending on order velocity and productive capacity, finished goods will be stored in plant or in local, outside warehouses.

Inventory Control

A complete inventory control system needs to be established to provide adequate customer service levels, while minimizing working capital requirements.

Market Channels for fishing boat owners

Wholesale/chain

- Boat supply houses
- Discount chain stores
- Chain hardware stores
- Fishing tackle distribution
- National chain stores
- Mail order houses featuring boating and fishing equipment

Retail

- Marinas
- Fishing tackle stores

III. Objectives

Short-term (first year)

- To attain distribution in 300 retail outlets
- To attain distribution with one retail chain having national distribution
- To reach annualized sales volume of 5,000 units

Long-Term (five years)

- To attain retail distribution in 1,500 retail outlets
- To obtain a supplier agreement with three major mail order houses
- To attain distribution with five retail chains having national distribution
- To reach an annualized sales volume of 50,000 units by the end of the fifth year

Sample Marketing Plan - Business: Boat Buddies (con't)

IV. Strategies

- Conduct preliminary test sale program in local market
- Direct sales and media efforts toward areas of high incidence on fishing and boating
- Maximize efforts to publicize and advertise product line, just preceding and during the fishing and boating season.
- Provide adequate staffing to supervise sales efforts and ensure high levels of customer service.

V. Tactics

- Contact local market retail outlets for initial sales. Analyze movement of dealer reaction. Project sales after 90-day test.
- Establish a reporting system to track sales efforts and results.
- Develop a sales brochure for use in all sales presentations and direct mailings. Brochure should describe all features and benefits of the products, shipping and billing procedures, and should include pictures of the products and installation instructions.
- Develop a media plan to include scheduling ads in major fishing and boating magazines. Copy and art work is to be developed for various size ads.
- Develop a publicity program consisting of news releases describing new product, its features, and benefits.
- Release will be mailed to fishing/sport editions of all state newspapers and appropriate magazines.
- Schedule participation in all major boat and fishing shows in the state and region. This will require development of collateral materials to be used in the booth, including brochures, photographs, product samples, etc.
- Schedule participation in the major fishing contests in the state and region. Arrange to give products to all professional contestants. Obtain photographs and testimonials from the contestants.
- Contact major mail order houses offering fishing and boating supplies. Secure marketing agreement to advertise in their publications.

From: *Small Business Marketing*, Mississippi Department of Economic and Community Development, June 1991.

Eight Steps to Effective Target Marketing -- and the Five “P’s” of Marketing

1. Identify the **PUBLICS** or target market(s) – the customer groups.
2. Research their characteristics, needs, wants, problems.
3. Develop the Customer Profile Statement for each target market subgroup that describes them in great detail.
4. Develop a solution -- a service **PRODUCT** -- to the target's problem.
5. Package the product and describe its **BENEFITS** in terms that key directly to the needs and interests of the target market(s).
6. Communicate or **PROMOTE** the benefits to the target market.
7. Provide the service at a **PRICE** they are willing to pay.
8. Provide the service or product to the target market in a **PLACE** where they will come to buy.

Assumptions for Target Marketing -- and the First "P"

1. When you try to sell everything to everyone at the same time... you are selling nothing to no one most of the time!
2. The best sales are one-on-one, but limited resources means that the best available alternative is selling to groups of people. They are put in groups because they have beliefs or other characteristics that make them similar in terms of their likely response to the benefit that your service will produce for them.
3. The first of the "P's" in marketing are the "**publics**" you are trying to reach. These are your customer groups. In marketing terms they are called target markets, or market segments. Groups are created based on the shared demographic and/or psychographic characteristics of the people involved.
4. You must get the right message to the right group of people at the right time for a sale to be made.
5. You cannot control whether or not someone will "buy" your idea or service, but you can control how appropriate your product is for the people you want to have buy. You can package it in a way that is attractive to them, and you can make it easy for them to buy at the time and place they want to buy, at the price they are willing to pay.
6. A quality product is a must, but quality without communication to the right customer in his/her terms is not enough. You must communicate to the customer in terms they will instantly recognize and understand.
7. Before your customers will listen to you... you must listen to them... to find out what they want and why they want it.
8. You get who you ask for! This is distressing for some people, but the image you have is based primarily on messages that you yourself send out. Use this workbook to analyze ALL the message you are sending -- and to simplify those messages to a few key phrases that speak directly to the interests of the customer groups that you want. Then, repeat, repeat, repeat.

The Second of the Five P's of Marketing ... Promotion

After deciding who your target market segments will be, you then develop a plan to reach them by sending a precise message through the media that you have determined that they read, listen to, or watch.

Message

Choose the "benefits" of your program that will solve the particular "problems" of the target market. Communicate your message about these benefits in the target customer's terms. Your benefit(s) must key directly to the wants or needs you identified in the Customer Profile Statement.

Media

Choose the vehicle(s) that will get your message to each target market. Where do they go? What do they listen to, watch or read? When can they best be contacted? Try to use several different media for sending the message to the target market you are trying to reach.

There is ONE MAJOR RULE to always keep in mind when developing promotional messages and materials:

SELL THE BENEFITS ----- AND NOT THE FEATURES

What are FEATURES?

- A description of the product or the service.

What are BENEFITS?

- A description of how the customer will benefit from using the product or service.
- A description of how the product or service will solve the customer's problem or offer them a new opportunity.
- A description of the unique opportunity (in relationship to competitors) that your product provides the customer.
- A description of the results that can be expected by the customer when they use your product.

The Focus of The Benefits Description Is The Customer!

Quotes About Benefits to Keep In Mind:

In the factory we make cosmetics, in the store we sell hope!

-- Charles Revlon, Revlon Cosmetics

(Cosmetics are the features -- and hope is the benefit)

It is not very difficult to persuade people to do what they are all longing to do.

-- Aldous Huxley

Two stonecutters were working on the reconstruction of St. Paul's in London when Sir Christopher Wren asked each what he was doing. The first replied, "I am cutting stone." The second answered, "I am building a cathedral."

("Cutting stone" is a feature -- the cathedral is a benefit)

People acquire services or products because they meet their needs. They get services or products because of their self-interest, not because of fascination with you or your organization!

C. Another of the Five P's of Marketing ... Pricing

Highlights of This Section...

How do I price my product or service?
How do I know what price will provide a profit?

Price can be thought of as three different kinds of costs to the customer: (1) direct dollar costs, (2) indirect dollar costs, and (3) intangible costs:

1. Direct Dollar Costs -- the amount of money it costs for the customer to acquire your product or service. (Most publicly funded services are without direct dollar cost to the customer, i.e. free)
2. Indirect Dollar Costs - these are the costs incurred by the customer in order to buy our product: for example, transportation, loss of income during training period, cost of day care, storage costs, renovation of the place where the item might go, customization or alteration costs, time off from work, learning to use it.
3. Intangible Costs - for example, risk, providing personal information that they fear may be revealed, possible embarrassment, etc.

The decision to buy is a rational decision that has two elements -- customer perceptions of total cost and customer perceived benefit/value.

$$\frac{\text{PRICE (All costs)}}{\text{VALUE/BENEFIT}} = \text{CUSTOMER COST}$$

When price exceeds value to the customer, the cost is too high and the customer does not buy:

$$\frac{\text{PRICE} = 100}{\text{VALUE} = 90} = \text{CUSTOMER COST OF } 1.11$$

When value to the customer exceeds the price, the relative cost is low and the customer buys:

$$\frac{\text{PRICE} = 100}{\text{VALUE} = 110} = \text{CUSTOMER COST OF } .90$$

We can increase sales either by:

- **Lowering the price**, including all of the direct, indirect, and intangible costs incurred by the potential customer. Try to do this first, it will be least expensive for you.

OR

- **Increasing the value** (benefit) through changing the product. If you add features, this increases your cost. Perhaps you can increase by value in other ways, such as by better communicating the full range of existing benefits in relationship to the price.

Profit Costing And Pricing For Services*

Introduction

This Management Aid discusses costing and pricing of services to assure that each job earns a reasonable profit. The figures used in the tables and examples do not reflect what your service costs, prices, and profits actually would or should be. The figures are used to demonstrate costing and pricing, and are rounded off for further simplicity. Because of the importance and sometimes complexity of costing and pricing, it is good business practice to consult your trade association, and particularly your accountant to learn what are the best current practices, cost ratios, and profit margins in your service business.

Costing Problems

Many small businesses are not making a profit today because they do not know the basic concepts of costing and pricing. The situation is most serious in the service business because each service performed has a different cost. Frequently, the service business must bid for jobs by making a price quotation in competition with similar businesses. Can you calculate your costs for your service and quote a price that is competitive and returns a profit?

Without realizing what they are doing, some business owners set their selling price below their total cost. This may result in more business for the company, but a loss will be incurred on each sale. Occasionally, a small business owner who lacks a knowledge of costing will try to compensate by setting prices very high. The end result is that the business is not price competitive and does not attract sufficient customers to survive. Frequently, a business earns a profit on some particular service and loses money on other services without knowing which services are earning a profit and which services are incurring a loss. The year-end income statement combines the profits and losses from the various services performed over the year. Therefore, it is impossible to determine the profitability of specific service jobs from a year-end income statement.

Use a simplified approach to cost accounting that reflects the needs of the small business and reports the cost with a reasonable degree of accuracy. The total cost of producing any service is composed of three parts: 1) The material cost; 2) The labor cost; and 3) The overhead cost. Direct materials and direct labor plus overhead equal the total cost of service.

* Reprinted from "*Profit Costing and Pricing for Services*", US Small Business Administration, Management Aids, No. 1.020

Cost Determination

Direct Material Cost: The direct material cost is made up of the cost to you for parts and supplies that are used on specific jobs. Once the list of parts and supplies to be used is developed, a check with the supplier will give an up-to-date material cost. The shipping and other handling (storage, etc.) costs for the parts should be included in the material cost.

Direct Labor Cost: The direct labor costs include those labor costs identified with a specific service job. The labor cost involved in providing a service is determined by multiplying the number of direct labor hours required by the cost per direct labor hour. It is very important to determine accurately the amount of direct labor hours involved to complete the service; therefore, you must use a time clock, worksheet, or a daily time card for each employee to determine the exact amount of labor time spent on each service job.

The hourly cost of direct labor can be figured (priced) two ways. 1) It can be the hourly wage only with fringe benefits, social security, workers compensation, etc., (all labor-related costs) allocated to overhead. 2) The hourly direct labor cost can include the hourly wages plus the employer's contribution to social security, unemployment compensation, disability, holidays and vacations, hospitalization and other fringe benefits (payroll costs).

By the second method, the added payroll costs for vacation, holidays and benefits are expressed as percentages of direct hourly wages. For instance, if two weeks of vacation and ten holidays are given annually, this amounts to four weeks per year, or 6.25% (i.e. four weeks off divided by fifty-two work weeks less four weeks off = 6.25%) of total labor cost was for time off.

Thus, to determine the total direct labor cost per hour by this method, you must add the prorated cost of the payroll taxes, workers' compensation, holidays and vacation pay, hospitalization etc., to the hourly wage paid. As a rule of thumb, the sum of the various payroll-benefit costs have generally been in the range of 20% to 30% of the hourly wages paid. It is more complicated to figure, but more precise to use the higher labor cost (including labor related payroll costs in addition to hourly wages in direct labor costs). The following table shows a sample calculation for figuring the total direct labor cost using this more exact method.

Total Direct Labor Cost

<i>Column 1</i>	<i>Column 2</i>	<i>Column 3</i>	<i>Column 4</i>	<i>Column 5</i>	<i>Column 6</i>
Hourly Direct Wages	Payroll Taxes @12%	Workers' Comp @3%	Total Direct Labor Cost Per Year*	Vacation & Holiday Cost per Work Hour**	Actual Labor Cost Per Week Hour***
\$2.68	\$0.32	\$0.08	\$6,406.40	\$0.19	\$3.27
3.26	0.39	0.10	7,800.00	0.23	3.98
3.40	0.41	0.10	8,132.80	0.24	4.15
3.62	0.43	0.11	8,659.04	0.26	4.42
3.85	0.46	0.12	9,209.20	0.28	4.70
4.10	0.49	0.12	9,807.20	0.29	5.01
			\$50,014.64		

* 40 hrs/wk x 52 wks/yr = 2,080 hrs/yr

** 6.25% of columns 1 + 2 + 3

*** Columns 1 + 2 + 3 + 5

Overhead Cost: Overhead includes all job related costs other than direct materials and direct labor. Your overhead cost depends on which of the two ways you figured direct labor costs. If you did not include these expenses in direct labor, then you must include them in overhead. In our examples, however, these labor-related costs are included in direct labor and not in overhead. Either way, the effect on the total job cost is the same but your overhead cost will vary accordingly.

Because they may not know how to allocate (or assign) overhead costs to the services performed, many small business owner-managers miscalculate or avoid considering overhead costs.

Overhead is the indirect cost of the service and is made up of indirect materials, indirect labor, and other indirect costs related to particular services. Indirect materials are too minor to include as direct material costs. Incidental supplies and machine lubricants are examples. Indirect labor is the wages, salaries, and other payroll-benefit costs incurred by workers who do NOT perform the service but who support the main service function, i.e. clerical, supply, and janitorial employees. Other costs like taxes, depreciation, insurance, and transportation are also part of the overhead cost because the service cost includes a portion of all indirect costs (overhead). The following table projects total overhead for all services for one year. To figure the portion of overhead related to particular services, or jobs, you allocate the various overhead costs by calculating the overhead rate.

The way you calculate the overhead rate should relate the overhead costs to the primary cause for the overhead cost being expended, reflecting a reasonable amount of total overhead to each service. The overhead rate can be expressed as a decimal, as a percentage, or as an hourly rate. The use of the overhead rate helps to assure that all the overhead costs expended throughout the year will be recovered as the business's services are sold throughout the year.

In a situation wherein employee wages vary a lot, as when higher paid employees work with more expensive equipment, the overhead cost is allocated on the basis of direct labor cost. This occurs because a large proportion of the overhead cost will consist of equipment depreciation (other indirect cost), interest on the capital invested in equipment, and electrical costs. The overhead rate is determined as follows:

$$(1) \text{ Overhead Rate} = \frac{\text{Total Overhead Cost}}{\text{Total Direct Labor Cost}}$$

This is the most common method for allocating overhead cost to the specific service performed. The above rate is suitable for machine shops and automobile repair shops.

In some cases there is relatively little difference in the hourly wages paid to different employees. In other cases, no relationship exists between the level of the worker's skill and the amount of equipment used by the worker. Under such circumstances, total overhead costs may be allocated on the basis of direct labor hours as follows:

$$(2) \text{ Overhead Rate} = \frac{\text{Total Overhead Cost}}{\text{Total Direct Labor Hours}}$$

The above rate is suitable for businesses such as secretarial services or janitorial services. The overhead costs result mainly from the workspace, supervision, and electricity that the workers need in order to provide the service. Using formula (2), it is possible to determine the overhead cost per hour per employee.

Calculating the Overhead Cost: In determining the total overhead cost, a small business should not depend solely on last year's income statement. Due to inflation and business growth, last year's overhead costs do not accurately reflect today's overhead cost. The best approach is to project the overhead costs for the near future, i.e., the anticipated overhead expenses for the next six months to one year. The projected overhead cost will reflect additional administrative salaries, the depreciation of new equipment that the business plans to purchase, rent increases, energy cost increases, etc. Table 2 shows projected overhead expenses for a small business -- ABC Repair Company.

The payroll taxes included in the **projected overhead expenses** for the service business are only those paid on executive and office salaries. The direct labor payroll taxes, holiday pay, vacation pay, etc., are included in the **direct labor cost** shown in the following table.

ABC Repair Company -- Annual Projected Overhead Expenses

Indirect Materials	
Office Expense	\$450
Postage	\$2,900
Repairs	\$2,700
Shop Supplies	\$2,400
Utilities	\$2,400
Telephone	\$4,400
Total - Indirect Materials	\$15,250
Indirect Labor	
Executive Salaries	\$30,000
Office Salaries	\$7,000
Payroll Taxes	\$12,000
Travel & Entertainment	\$700
Total - Indirect Labor	\$49,700
Other Direct Costs	
Accounting	\$2,400
Advertising	\$4,800
Auto/Truck Expenses	\$5,400
Depreciation	\$9,650
Insurance	\$1,250
Interest	\$2,560
Licenses	\$650
Misc. Expenses	\$500
Rent	\$8,450
Total - Other Direct Costs	\$35,660
TOTAL OVERHEAD	\$100,610

To insure that all overhead costs are included, it is best to project the overhead costs for a full fiscal year. This aids in the treatment of expenses that occur only once each year, i.e. business licenses.

Cost Calculation Example:

Perhaps the most common type of service business is the repair business. The cost calculation procedure illustrated here for the repair business can be used for other types of service businesses. The only precaution that needs to be taken is that the appropriate overhead rate formula which reflects the business's operation, as discussed above be used in the calculation.

It has been estimated, based upon previous experience, that a specific repair job will require \$20 of parts and two hours of labor by an employee whose labor cost is \$5 per hour (these estimates will be used throughout this aid). As discussed earlier, the total cost of producing any service is composed of 1) the material cost 2) the labor cost, and 3) the overhead cost.

To determine the material cost (the cost of the parts) check the cost of the part in your inventory or get a price quote from your parts supplier. A parts wholesaler is the source of the \$20 material cost in this example.

To determine the total direct labor cost, the number of hours of direct labor used is multiplied by the actual direct labor cost per hour. An employee whose actual **direct labor** cost is \$5 per hour, including payroll taxes and fringe benefits (see Table 1), requires two hours to complete the repair job.

Labor Cost = Direct Labor Cost per hour x hours required
Labor Cost = \$5 per hour x 2 hours
Labor Cost = \$10

The projected overhead expenses were projected to be about \$100,000 per year, as shown in Table 2. The nature of the repair business is that overhead costs are most directly related to direct labor costs than to direct material costs. The total projected direct labor cost including payroll taxes and fringe benefits was determined to be \$50,003.20 (see Table 2). The formula selected to determine the overhead rate based upon the direct labor cost is:

$$(1) \text{ Overhead Rate} = \frac{\text{Total Overhead Cost}}{\text{Total Direct Labor Cost}}$$

$$\text{Overhead Rate} = \frac{\$ 100,000.00}{\$ 50,003.20}$$

$$\text{Overhead Rate} = 2$$

In most small businesses, the overhead rate is between one and two, (between 100% and 200% of the direct labor cost). This is based upon the author's five years of small business management consulting experience. Businesses that are very labor intensive, i.e. janitorial services, will have an overhead rate much less than 100%.

To determine the overhead cost allocated to a specific job, the labor cost is multiplied by the overhead rate as shown below.

(1) Overhead Cost = Direct Labor Cost x Overhead Rate
 Overhead Cost = \$10.00 x 2.00
 Overhead Cost = \$20.00

To determine the total cost of the repaired job, the material cost, the direct labor cost, and the overhead cost are added together.

Material Cost	=	\$20.00
Direct Labor Cost	=	10.00
Overhead Cost	=	<u>20.00</u>
Total		\$50.00

Pricing: Calculate the profit and add it to the total cost to get the price to charge for the service, in this case a repair job. Prices charged by competitors (similar service businesses), economic conditions of supply and demand, and legal, political, and consumer pressures all influence the profit you can expect for your service and hence the price you can charge for your jobs. Inflation, the amount of business you have, i.e. number of jobs, and your productivity (the efficiency and quality of your business and service) also all affect your profit and the way you figure your prices. You can choose from several pricing methods. Common business practice is to express profit as a percentage of the base used for pricing calculations no matter which pricing method you use.

Pricing Alternatives: In considering the total cost of the repair job discussed above, the material cost can normally be predicted with a high degree of accuracy. Labor and overhead costs cannot be predicted with such a high degree of accuracy. An employee may not feel well on a given day or there may be an equipment breakdown. Either will result in higher than expected labor costs. A provision to adjust for fluctuating labor and overhead costs can be established through your approach to profit. The profit can be applied to the three costs independently allowing for variations in labor and overhead costs among jobs. For example, a 10% profit on material, a 30% profit on direct labor, and a 30% profit on overhead can be used to determine the price of the services.

Pricing Alternatives

Material Cost + Profit of Material
 $\$20.00 + \$20 \times 10\% = \$22.00$ $\$2.00$

Direct Labor Cost + Profit on Direct Labor
 $\$10.00 + \$10 \times 30\% = \$13.00$ $\$3.00$

Overhead Cost + Profit on Overhead
 $\underline{\$20.00} + \$20 \times 30\% = \underline{\$26.00}$ $\underline{\$6.00}$
 $\$50.00$ Cost $\$61.00$ Price $\$11.00$ Profit

The concept of applying a different rate of profit on the three underlying costs (material, labor and overhead) is one method of dealing with the large difference in predictability of costs that exists between labor and materials in most service businesses. To reflect the fluctuations in utilization and cost of labor and overhead from job to job, your profit on labor and overhead should normally be higher than profits on materials.

Direct Cost Pricing: With this method you set your selling price based on direct cost, i.e., on direct materials (DM) and direct labor (DL). DM of \$20 plus DL of \$10 equals direct costs of \$30. Overhead (OH) costs are \$20; so to earn the \$11 profit you need, your selling price must be at least \$31 above your direct costs. To find the percentage of profit on direct cost to charge, divide direct costs into overhead plus needed profit:

$$\begin{aligned} \$31 (\$11 + 20) - \$30 &= 103 \frac{1}{3}\% \\ (\text{proof } \$30 \times 103 \frac{1}{3}\% &= \$30 \times 1.033 = \$31) \end{aligned}$$

Profit Margin Pricing: This profit rate is expressed as a percentage of your full costs. Full cost is divided into the needed profit to get the percentage of profit margin.

$$\begin{aligned} \$11 + \$50 &= 22\% \\ (\text{proof } \$50 \times 22\% &= \$11) \end{aligned}$$

Profit can also be figured as percentages of assets used on the job. This method is called *return-on-asset pricing*. Thus, full cost per job *plus* the needed profit (rate of profit *times* the amount of assets used per job) *equals* the job price:

$$\$50 + (\$80 \times 14\%) = \$50 + \$11 = \$61$$

One of the most widely used pricing methods for service-oriented businesses is **time and material pricing**. Time is expressed as the labor cost per hour, calculated as 1) direct-labor (DL) and payroll benefits (see Direct Labor Cost explanation), **including** 2) overhead (OH) costs not related to materials, and 3) needed profit. Material cost is the direct material (DM) cost and over-head (OH) plus 30% for needed profit.

Note: the overhead has been allocated to labor and materials.

Time: DL \$5 per hr. x 2 hrs. =	\$10	
OH \$7 per hr. x 2 hrs. =	<u>\$14</u>	
	\$24	
		+ \$7 for needed profit = \$31

Material:	DM \$20	
	OH <u>\$3</u>	
	\$23	
		(\$23 X 30%) =
		(\$23 + \$9 for profit) =
		<u>\$30</u>
		\$61

In most small repair businesses, there is **not** a large amount of overhead cost associated with obtaining parts as a telephone call can order them. Charging a large amount of overhead to parts may result in pricing yourself out of the market.

By all these methods you are deriving a selling price for your service. Sometimes, however, you start with the selling price already established -- by competition or economic conditions. Then you must figure out the most cost you can incur and still earn your needed profit.

Summary

The total cost of producing a service is composed of direct material, direct labor, and overhead costs. This cost information is used as a basis for setting prices and profit. From alternative pricing methods you select one that earns a satisfactory profit and is easy for you to use. Given regulations, competition, and the economy, you must have a pricing strategy that keeps your service competitive and profitable. The more exactly you figure your costs and set prices, the greater your chances for continued and profitable business.

D. Another of the Five P's of Marketing ... Place (Location)

Checklist: Questions You Should Ask About Location

- Is the location convenient?
- Is the location safe? Is it perceived as safe by area residents and visitors?
- How much property insurance you would you need to have?
- Is it close to other businesses that shoppers visit?
- Is it where people would like to come to buy your product or service?
- Is it convenient and attractive?
- Are there parking spaces? Is the lot clean and safe?
- Is it near public transportation?
- Any zoning problems?
- Is there good signage? Can you have a clearly marked sign that is lit at night?
- Is there an elevator and handicapped access?
- Is the appearance of the store attractive?
- If you are renting or leasing space, would you be able to get a lease long enough to make it worthwhile to renovate the space? Will the landlord contribute to the renovations?
- Are there restrictions on hours you can be open? Does this limit the convenience to your buyers?
- Can the site be made comfortable? Are the restrooms clean?

Adapted from *New Business*, Massachusetts Dept. of Commerce and Successful Marketing & Public Relations, National Assn. of Community Action Agencies.

E. Assess Financing Needs

Highlights of This Section...

What financial statements do we need?
How do we read these statements and use them?
What kind of financing is available?

Prepare Pro Forma Financial Statements

Detailed financial statements should be included as attachments to your business plan. Here are brief descriptions, followed by templates for start-up expenses, a balance sheet, and an income statement. Additional statements should include a cash flow statement. See the Appendix for a description and outline for a cash flow statement.

Start-Up Expenses*

Start-up expenses are the various expenses it takes to open your doors for business. Some of these will be one-time expenditures, while others will occur every year. The worksheet on the next page provides a generic form for determining your start-up costs.

We've seen this category of expenses totally overwhelm the new business owner – occasionally to the point of closing the doors instead of opening them! Don't leave anything out, and when you're through add at least a 10 percent safety factor for items you did not anticipate.

The Income Statement**

The income statements are projected first. Once this has been accomplished, the balance sheets can be projected. Following that you can calculate the ratios and cash flow.

Income statements are generally projected for three years. The steps to follow when developing this statement are: 1) develop revenue forecasts by product or service category; 2) determine gross profit margin by product or service category; 3) estimate operating expenses or overhead; and 4) calculate resulting Profit or Loss.

The Balance Sheet**

A balance sheet is a statement of assets, liabilities, and equity. The term "equity" is the accounting term for the amount of funds that are claimed by the owners after considering all of the funds owed to creditors. Assets are what you own, such as accounts receivable, and equipment. Liabilities are what you owe, such as accounts

payable, bank loans, and mortgages. Equity is whatever is left after you subtract the liabilities from the assets. The balance sheet is referred to as a “position” statement because it indicates the amount of assets, liabilities, and equity as of the date of the balance sheet.

The Cash Flow Statement*

Cash Flow is the life blood of a business. Passive Cash Flow is required, needed, and necessary for a business to run and to continue to operate. Having sufficient cash available, at the right time can be a difficult juggling act for a business manager/owner. Too often, the importance and ability to have the right cash flow at the right time is “lost” on the small business owner. Too much cash can be as big a problem to the business owner as not having enough. Too much cash at any one time can cause the business owner to get sloppy, lazy, and irresponsible.

In order to manage cash flow properly, you start with a budget or plan as a reference point to judge, manage, and adapt activities to what is really happening. The advantages of this are:

- It forces the business person to forecast, plan, and set goals for income and expenses;
- It forces an understanding and awareness of the cash position of the business;
- It forecasts when money (CASH) will be needed in the business; and
- It can be used as a tool to analyze “what happened?” as well as assist the owner in thinking through the cause and effect of management decisions.

Cash Flow is NOT a stand-alone document! It is used in conjunction with the Balance Sheet and the Income Statement to help the business person to keep on top of the business and be in control of what is happening.

Cash Flow is the sum total of all the cash flowing through the business and shows the incoming cash or revenue, outgoing cash or expenses, and the differences which will require borrowing if outflow is greater than inflow. It shows the cash position of the business.

* From: *The Beginner’s Guide to Developing a Small Business*, Dale L. Lane, Ed., Micro Business Development Program, Champlain Valley Office of Economic Opportunity, Inc., June 1996.

** From: *Developing a Winning Business Plan* by Joseph Eve & Company for the Montana Microbusiness Finance Program.

Common Misconceptions of Cash Flow

1. Cash = Profit **WRONG!**
2. Liberal cash drawer policy
3. Working Cash = Capital Resources **WRONG!**
(Working capital is to meet day-to-day requirements. Capital resources are fixed assets)
4. Accounts Receivable = Cash **WRONG!**
(Accounts receivables are promises – they cannot pay current obligations; neither can inventory, new orders, etc.)

Cash Flow and Cash Management:

- Plan for the cash supply required to run the business.
- Control and manage the cash flow of the business
- Allows the business to Invest any surplus to earn added income.
- See the Appendix for *Understanding and Controlling Cash Flow*, a publication of the US Small Business Administration. This is an excellent and detailed guide to preparing a cash flow statement. There is a simple example of a cash flow in the following pages.

The following pages provide financial planning worksheets and samples of these worksheets. There is also a discussion of break-even analysis.

Worksheet: Business Start-Up Expenses

Expense	Cost
Total Cost of Capital Equipment	\$
Beginning Inventory of Merchandise	\$
Legal Fees	\$
Accounting Fees	\$
Other Professional Fees	\$
Licenses & Permits	\$
Remodeling Work	\$
Deposits:	
Rent	\$
Utilities	\$
Phone	\$
Advertising (grand opening, etc.)	\$
Signs	\$
Promotion (door prizes, etc.)	\$
Business cards, stationary, office supplies	\$
Bookkeeping System	\$
Other:	\$
	\$
	\$
	\$
	\$
Sub-Total Start-Up Expenses	\$
Plus 10 % Safety Factor	\$
TOTAL START-UP EXPENSES	\$

From: *The Beginner's Guide to Developing a Small Business*, Dale L. Lane, Ed., Micro Business Development Program, Champlain Valley Office of Economic Opportunity, Inc., June 1996.

Worksheet: Pro Forma Income Statements

NET SALES	12/31/00	12/31/01	12/31/02
Sales Flat-Plate Collectors	_____	_____	_____
Installation Fees	_____	_____	_____
Service Fees	_____	_____	_____
Subtotal	_____	_____	_____
COST OF GOODS SOLD			
Inventory	_____	_____	_____
Labor and Fringe	_____	_____	_____
Sales Contract	_____	_____	_____
Installation Contract	_____	_____	_____
Service Contract	_____	_____	_____
Subtotal	_____	_____	_____
GROSS MARGIN	_____	_____	_____
OPERATING EXPENSES			
Management and Fringe	_____	_____	_____
Clerical and Fringe	_____	_____	_____
Professional Services	_____	_____	_____
Travel	_____	_____	_____
Insurance	_____	_____	_____
Rent	_____	_____	_____
Telephone	_____	_____	_____
Advertising	_____	_____	_____
Office Equipment	_____	_____	_____
Licenses	_____	_____	_____
Contingency	_____	_____	_____
Subtotal	_____	_____	_____
PROFIT BEFORE TAXES	_____	_____	_____
TAXES (EST.)	_____	_____	_____
NET PROFIT	_____	_____	_____

Worksheet: Balance Sheet - January 1, 2000

ASSETS

Current Assets

Cash	-----
Accounts Receivable	_____
Inventory	_____

Fixed Assets

Office Equipment	_____
Vehicle	_____
Shop Equipment	_____
Accumulated Depreciation	_____

Total Assets _____

LIABILITIES

Current Liabilities

Accounts Payable	_____
Notes Payable (vehicle)	_____

Long-Term Liabilities _____

Equity

Grant	_____
-------	-------

Total Liabilities/Net Worth _____

Sample Financial Statements

Jane's Smart Shop* Balance Sheet - January 1, 2000

ASSETS

Current Assets

Cash	\$ 8,000
Accounts Receivable	
Inventory	35,000

Fixed Assets

Equipment	12,000
-----------	--------

Total Assets **\$ 55,000**

LIABILITIES

Current Liabilities

Accounts Payable	17,000
------------------	--------

Owner's Equity	38,000
----------------	--------

Total Liabilities/Net Worth **\$ 55,000**

* From: *The Beginner's Guide to Developing a Small Business*, Dale L. Lane, Micro Business Development Program, Burlington, Vermont, June 1996.

Sample Financial Statements

The Hatch Jewelry Shop Statement of Cash Flow*

Account Item	Annual Amount
Net Income After Tax	\$73,480
Plus: Depreciation/Amortization	6,300
Accounts Receivable	(10,997)
Prepays	(1,438)
Other	(1,960)
Accounts Payable	4,573
Accrued Expenses	654
Other Current	(298)
Other Non Current	333
Operating Cash Flow	70,647
Fixed Assets	(5,000)
Investing Cash Flow	(5,000)
Cash Flow Before Financing	65,647
Notes Payable Bank	0
Long-Term Debt	(7,000)
Financing Cash Flow	(7,000)
Overall Cash Flow	58,647
Beginning Cash	1,000
+/- Overall Cash Flow	58,647
Ending Cash	59,647

*From *Developing a Winning Business Plan*, Montana Microbusiness Finance Program, 1996.

Sample Financial Statements

The Hatch Jewelry Shop Break Even Analysis*

How much sales do I need to just break-even?

- 1) Determine the amount of your fixed and variable costs
- 2) Divide your variable costs by the sales for that period to determine your variable cost percentage
- 3) Subtract your variable cost percentage (CV%) from 100% to determine your contribution margin
- 4) Divide your contribution margin percentage into your fixed costs.

Sample Break-Even Analysis

Projected Sales	\$100,000	100%
Projected Variable Costs	\$60,000	60%
Contribution Margin		40%
Fixed Costs	\$24,000	
Break-Even Sales	\$24,000/40%	\$60,000

How much in sales do I need to make a certain profit?

Answer this question by adding your desired profit to the amount of your fixed costs and dividing the total by your contribution margin percentage.

$$\text{Sales} = \frac{\text{Fixed Costs} + \text{Profits}}{\text{CM \%}} \qquad \text{Sales} = \frac{\$24,000 + \$30,000}{40 \%}$$

\$135,000 in sales would be needed to generate a bottom line profit of \$30,000 given my current fixed and variable costs.

How much additional a sales do I need to make the same profit if fixed costs increase?

$$\text{Sales} = \frac{\text{Fixed Costs} + \text{Increase} + \text{Profit}}{\text{CM \%}}$$

Divide your fixed costs by the unit contribution margin (the price per unit minus the variable costs per unit).

$$\text{Unit break-even} = \frac{\text{Fixed Costs}}{\text{Unit Contribution Margin}}$$

For example, assume that the owner of the Hatch Jewelry Shop has determined through competitor analysis that she can charge up to \$50 for the new lapel pins she is adding to her product line. She has also determined the following with regards to his variable costs per unit:

Variable Cost per Unit Sold	
Labor (1.5 hours @ \$10/hour)	\$15
Materials – Gold	\$10
Materials – Stones	\$3
Total Variable Cost	\$28
Operating Costs per Month	
Rent	\$500
Utilities	\$60
Phone	\$50
Office Supplies	\$50
Insurance	\$40
Advertising	\$150
Promotion	\$150
Total Fixed Costs	\$1,000

	Option 1	Option 2	Option 3
Price	\$45	\$50	\$75
Variable Cost	\$28	\$28	\$28
Contribution Margin (price - var. costs)	\$17	\$22	\$47
Break-Even in Units (total fixed expenses - contribution margin)	59	45	21

Assuming that the market would bear the higher price, the jeweler would likely want to select price option number 3. However, the market may not bear the higher price unless the lapel pin is particularly unique.

A thorough understanding of your costs is the most important element in making pricing decisions.

*From *Developing a Winning Business Plan*, Montana Microbusiness Finance Program, 1996.

Business needs capital to operate. Even the smallest venture requires money. Your organization will need to determine what sources can provide you with the funds you need.

Business capital comes from two sources and both require that the initial investment be paid back with a return:

Source of Capital and Method of Payback

	Source of Capital	Method of Payback
Equity	Ownership in the business is sold in segments (shares, stocks, memberships)	Through dividends, increased ownership, or convertible to a loan
Debt	Funds are borrowed and must be repaid with a return to the lender	Through repayment of loan with interest and possibly additional fees.

A new business may be able to obtain financing from various lending sources depending on, among other things, how mature the organization is. The financial community recognizes a business life cycle that contains stages of maturity. Different kinds of financing is available to businesses at varying stages. As you review the various business life cycle stages and sources of capital, assume you've completed your feasibility study and business plan and it looks very probable that the venture will succeed.

Most ventures start as an idea or concept. Some never make it past the conceptual stage. Nonprofits have an advantage at this level. Many are highly skilled at soliciting funds from outside sources that place no obligation on the organization to repay and no subsequent loss of ownership. Grants, gifts and donations are part of the nonprofit's cash support system. You may need to accumulate or have already accumulated a pool of cash to finance your venture for at least a year. A commercial lender may make an exception for a personality, a known product family or a strong parent group. There is virtually no chance of payback on the debt unless payback is guaranteed by the principals seeking a loan or mortgage. If you can sufficiently demonstrate that nonprofit funds are guaranteed (for example, through a government guaranteed contract or proceeds of a trust) you may be able to obtain a small loan. For many nonprofits, the conceptual stage of a venture can be supported by a combination of grants, donations, the organization's own human resources and community network support.

Development Stage

Once the concept has been developed, it needs to be put into action. The organization is spending all of its time in developing the new business and either of two conditions exist:

- Planned principal operations have not yet begun.
- Planned principal operations have begun but there has been no significant revenue.

Opportunities for obtaining capital open up at this stage because the idea is fully developed.

At this stage, it is necessary to set up the means to produce the product or service and to begin related activities to start up the operation. The enterprise will be devoting most of its efforts to financial planning, raising capital, exploring for natural resources, developing natural resources, research and development, establishing sources of supply, acquiring assets (property, plant, equipment or other operating assets such as mineral rights), recruiting and training personnel, developing markets and start up of production. As a result, outsiders can see exactly what the business hopes to accomplish.

Investors with a vested interest (usually ownership) are more willing to take the risk of investing at this stage. Venture capitalists and other risk capital institutions may participate at this point, but they will demand an interest, often a combination of ownership and debt. The actual length of the development stage will vary greatly depending on the type and scale of the business. Because of these factors, the principals in the business may remain the primary source of capital. The actual cost to the principals is in paying higher interest rates and the possible relinquishment of management control.

development in the private sector (for example, computer software) and a favorable market, may attract investors or lenders.

Growth Stage

The venture has reached a point when it has attained a reasonable sales volume with a break-even point in sight. This is a critical time for a venture. Young businesses with little or no "track record" of earnings still have not reached the point to obtain traditional institutional debt financing. Capital may be available through specialty lenders or investors because the venture has begun to acquire sales, generated accounts receivable and established an inventory. Financing of inventory and accounts receivable does not require profitable operations. More traditional lending institutions require a minimal level of profit prior to lending this type of loan. Specialty lenders are less interested in profits because they charge higher interest and are structured to closely monitor the borrower's situation. Banks still may not be interested in lending at this stage -- they're more interested in establishing a deposit relationship while the group is maturing.

The venture is usually in a very strong position at this point; it is a prime market for investors. A strong and positive relationship with a bank makes loans possible.

Mature Stage

A mature business is well established and firmly entrenched in the market. Usually the business has grown with the market in which it operates; if the market grows slowly, so may the company. Sales are stable, profit margins are good, and internal cash needs are met by profit generated by the business. Experience gained from years in the market results in working capital being fairly well managed. Rapid expansion is no longer a factor because of size and strength in the market place: the mature business can now ensure that accounts receivable collections do not slow down and cause a financing problem. The business does not need to borrow frequently, instead, surplus cash is generated. Borrowing needs at this stage center around one-time acquisitions and introduction of new products. The most options for financing are available to a business at this point.

Deciding on the Source

It is important for a nonprofit to identify where the venture is in its stages of growth. Time and resources can be wasted in approaching a lending source with proposals when the group doesn't match the lender's criteria.

Now that you've identified your organization in terms relating to its level of maturity and experience, you have a sense of what type of capital you can expect to attract and secure. Nonprofits can raise money from primary or secondary sources depending on

a strong image in the community would keep you from securing a loan from a stage-two source if you are at stage-one. The following chart groups major sources of funds into stages. The probability of attracting certain types of funding sources is matched to each stage of the business life cycle.

The list is not exhaustive of the sources of capital that may be available to a nonprofit. It is not intended as a shopping list. It should be approached through an organized process, analysis, research, and decision making with the intent of discovering the most appropriate sources. Your business plan should fit the method of financing.

Decision strategy forces a group to maintain objectives and accurate judgments. It is a tool used to make a thorough and complete analysis of your own situation in the context of the loan and investment sources. It is used in the banking community and you will need to become comfortable with it.

Decision strategy has three elements: Purpose, Repayment, and Structure. (These elements closely resemble elements of a business plan). To arrive at a decision strategy, we suggest asking, thinking about, and answering these questions.

Stage	Method of Funding	Primary Sources of Funds	Secondary Sources of Funds
Conceptual	Solicitation through grants, gifts, donations	Foundations, government programs, philanthropists, private citizens	Individual investors, investor groups (tax shelters), commercial banks, US Small Business Administration
Development	Exploitation of own resources through economizing and prioritizing, redirecting cash flow, leveraging, fundraising	Volunteers, centralization of functions, cost benefit measures, selective prioritization, shared costs, private citizens	Individual investors, investor groups (tax shelters), commercial banks, US Small Business Administration, Savings and Loan Associations, government programs, finance companies, venture capitalist, Small Business Investment Corps.
Growth	Relinquishing part of ownership, sale of stock/share/member-ships, partnerships	Individual investor, venture capitalist, investor groups (tax shelters), Small Business Investment Corps. (Minority Enterprise or Community Development Corp.), Commercial Banks, US Small Business Administration	Insurance companies, development authorities, Employee Stock Ownership Plans
Maturity	Loans, mortgages, bonds	Commercial banks, credit unions, loan & mortgage companies, insurance & pension trust plans, venture capitalist, economic development corps., Local Initiative Support Corps., industrial & development bonds, state & local special fund pools, state & federal economic assistance sources, foundation program-related investment funds, service corporations, local/community development corps., local & private groups and brokers.	

A Decision Strategy for Financing

Use the following questions to organize your business and determine the most likely sources of financing.

Purpose

What is the specific financial requirement?

Does the request match the requirement?

What is the cause of the requirement?

How long will the funds be needed if borrowed and how long will the equity funds be used if invested?

Repayment

Is the business strategy well conceived?

Is the management skilled and experienced?

Does the parent have a balanced financial position?

Will the business have sufficient cash to repay the loan or provide for a return on investment with the proposed schedule and in the proposed manner?

What are the major strengths and weaknesses of the loan and/or investment?

Structure

What will the interest rate, terms, collateral, restrictions and disbursement method be for the loan?

What rate of return, debt repayment, control questions, buy-out provisions, return schedule, disclosure requirements apply for an investment?

What documentation, other approvals, and reporting are required on both?

Borrowing

Many nonprofits have experience in borrowing -- especially in tight cash flow situations. Community Action Agencies in some states are allowed to keep interest earned on Fuel Assistance Program deposits and thus accumulate the necessary interest payback on an accounts receivable loan.

A good basic introduction to the art of obtaining loans is the US Small Business Administration's *ABC's of Borrowing*. Working through it is good preparation for developing an essential part of the business plan.

A chart was presented a few pages back that listed various types of capital sources. We think it's worthwhile taking a closer look at a few of them. Because these sources are more familiar with, and have a greater understanding of how a nonprofit organization can contribute to the economic and social health of a community, they have more potential as prospective sources of capital. Included are specific loan programs that have sprung up especially for the purpose of assisting nonprofits in bridging their cash flow gaps. This trend is likely to grow in the future as more and more private sector interests are encouraged to fill a philanthropic role.

To get a loan approved, it is helpful to have a graphic understanding of the steps involved, the lender or investor criteria and how to fit elements of your nonprofit profile into the loan picture. The chart on the next page pulls those elements together with the loan review process. Incidentally, those steps closely follow steps made in acquiring equity capital.

It is evident how critical the proper execution of a business plan is to success in securing a loan or investment. On this page, compare the lenders/investors criteria and your project. Do you discover that your project sharply differs with the prospective lender's criteria? If so, that source of capital should be placed in a lower priority to approach at a later date. With such a simple review of feasibility you can quickly anticipate your prospects.

	Nonprofit Profile	Lender/Investor Criteria
Purpose		
Loan/Investment request reviewed by the source		
Policies, explicit and implicit, of the source		
Borrowing/offering cause		
Terms of loan/investment		
Repayment		
Business review		
Management review		
Analysis of financial statements		
Cash flow analysis		
Summary and initial recommendation		
Structure		
Loan/investment negotiation		
Approval, documentation, reporting		

"Teaching Them How and Where to Get Money"

Arthur Lipper, III, Chairman, Venture Magazine, New York, New York

Who does invest in entrepreneurial activities in new businesses? According to David Birch, who really is the authority in these areas, there are about 1,200,000 new enterprises started each year in the United States. Something over 600,000 new incorporations, about 100,000 partnerships and about 500,000 unincorporated proprietorships. The venture capital community is insignificant as far as most entrepreneurs go. The venture capital community consisting of about 1,300 identifiable units managed by about 700 management groups invest in fewer than 500 new companies a year.

Who does invest? Well, the entrepreneurs, their savings and their abilities to borrow represent about 80 percent. You add to that three sources of equity: cradle equity, that which comes from the parents; pillow equity, that which comes from the spouse; and bend over equity, the pile of unpaid bills. And that's really how businesses are financed in the United States.

How to get the money is a function of understanding the needs of the provider of the money. Where to get money? I believe the best source of capital for any privately-owned company is from an individual who started his or her own company successfully. I do not believe that, by and large, they're going to get money from institutionalized sources.

Failure rates are very low in the United States. Now that's different than I know you all believe and have heard, but there were only 62,000 bankruptcies last year in the United States. Those are failures. There were over 400,000 business discontinuances, 62,000 of which were the result of the bankruptcies. I prefer to use the term disappointment for the discontinuances.

Venture Capital is a growing source of loans and more plentiful when economic times are good and the stock market expanding. There are some basic ground rules to keep in mind when approaching venture capital firms: they are very selective and they prefer applicants with a sound business plan in hand. Venture capital is considered the most glamorous type of financing available. These perceptions grew out of the 1970's when venture capital was available to hi-tech entrepreneurs; Steve Jobs and Steve Wozniak starting Apple Computer, etc. The 700 or so venture capital firms invest in only about 2,000 ventures a year.

This does not include the typical restaurant start-up, which is financed by a doctor, a lawyer and a restaurant person. Rich people make personal investments in businesses every day.

Social Venture Partners Using the Venture Capital model, Social Venture Partners seeks to pool its financial resources and professional expertise to invest in long-term solutions to the social challenges facing our community. SVP partners may give time, money and expertise through partnerships with the agency that starts the venture.

Loan Programs geared toward human service organizations or other nonprofits have a purpose other than being a source of funds to bridge a cash flow gap. They can help establish a credit history. Criteria will differ among programs; most loans require payback within six months to one year. Many do not require interest be paid but collect an administrative fee. If interest is charged, it may be at market rates or at a lower, subsidized rate. Technical assistance on money management assistance is often available. Most programs require security or collateral for a loan. You will usually need to show evidence of managerial stability, to supply financial data showing the capacity to pay back the loan, that other available commercial financing cannot be obtained, and that your request meets the loan program's other policies.

Grants are still available though scarcer to find. "Alternative Foundations" or community foundations sometimes provide grant funds to small nonprofits.

Research on foundation grants can be done with the help of a number of organizations and resources. Most of those listed here have a presence on the Internet and can be found via links from the Roberts Enterprise Development Fund web page at www.redf.org and the Community Wealth web page at www.communitywealth.org.

Other Thoughts on Outside Money. Whatever the source of outside financing you are seeking, skepticism can be overcome by the organization's capacity, management team, business plan, financial statement and the aggressiveness, and fairness of any negotiating processes.

Assume there is no agreement until the deal closes. Don't plan on the funds, commit the organization to future proceeds, or expect the funder to honor any informal commitment or agreement. Don't spend the money until you've got it. Look at the funder's criteria as general indicators that may change and be prepared to show how the deal will work. Show you're willing to make the effort to make adjustments or changes to fit any reasonable contingency or requirements. .

The cost of the loan or investment isn't the most important factor being considered. If your success actually turns on the difference between a 6% and an 8% interest rate, you aren't going to succeed anyhow.

The owners and Board of a new venture or business should expect to give personal guarantees or co-sign loan agreements.

Anticipate the lender or investor has the same expectations that you bring to the negotiating table; the other side wants the greatest amount of gain with the most advantageous terms for the least amount of risk and exposure.

Giving a business plan to a banker can get you free feedback and consultation – whether you actually plan to close on the loan or not. Bankers have experience you can use and they typically send business plans out to other experts for comment. If they say “Here are four problems in your approach....” you should pay attention!

Grab your bootstraps...

Foundation Research and Links to Other Web Pages

The Roberts Enterprise Development Fund utilizes a venture philanthropy approach to support development of social purpose businesses in the San Francisco area. The fund has a portfolio of eight nonprofit organizations operating twenty-four for-profit businesses. Although they do not fund a large number of new ventures, they are a good source of information on related topics.

PO Box 29906, San Francisco, CA 94129-0906

415-561-6533

live4punk@aol.com, jemerson@well.com, www.redf.org

National Network of Grantmakers (NNG) is a membership association of funders committed to supporting progressive social change. As an organization, NNG is committed to the goal of increasing resources, financial and otherwise, to organizations working for social and economic justice.

1717 Kettner Blvd. #110, San Diego, CA 92101

619-231-1348, 619-231-1349 fax

547 Ponce de Leon, Suite 100, Atlanta, GA 30308

404-874-6703, 404-874-0296 fax

Neighborhood Funders Group is a membership association of grantmaking institutions. NFG provides information, learning opportunities, and other professional development activities to their national membership, and encourage the support of policies and practices that advance economic and social justice.

6862 Elm Street, Suite 320, McLean, VA 22101

703-448-1777

Foundations that Fund Entrepreneurial Ventures

The Entrepreneurs' Foundation (EF) is a nonprofit organization created to strengthen the Silicon Valley/Bay Area's community infrastructure by establishing community reinvestment as an integral part of the entrepreneurial culture. EF intends to translate the extraordinary successes of the technology industry into a platform for long-term community investment and prosperity.

The Ewing Marion Kauffman Foundation is an operating and grantmaking foundation that works toward the vision of self-sufficient people in healthy communities. Its mission is to research and identify unfulfilled needs of society and to develop, implement and/or fund breakthrough solutions that have a lasting impact and offer people a choice and hope for the future. The Kauffman Foundation's work is focused on two areas: Youth Development and Entrepreneurial Leadership.

4801 Rockhill Road, Kansas City, MO 64110-2046
806-932-0100

Peninsula Community Foundation A permanent charitable institution dedicated to addressing the changing needs of the San Francisco Peninsula. The foundation specializes in building partnerships between strategic givers and our most effective leaders in government, schools and nonprofit organizations to make their dreams for the community's future come true.

1700 South El Camino Real, Suite 300, San Mateo, CA 94402-3049
650-358-9369, 650-358-9817 fax

The **Pfizer Foundation** Supports entrepreneurial nonprofit organizations seeking innovative ways to break the cycle of poverty. The program focuses on fostering individual self-reliance and helping to bring new jobs and capital to low-income areas. The site provides a discussion of venture philanthropy in their online magazine. See www.pfizer.com/pfizerinc/philanthropy.

Robin Hood Foundation

111 Broadway, New York, NY 10006
212-227-6601

The Surdna Foundation grantmaking activities are concentrated in four programmatic areas: environment, community revitalization, effective citizenry and a small program in the arts that is by invitation only.

www.surdna.org, request@surdna.org

Social Venture Network Doing Well While Doing Good, SVN provides a variety of forums for businesses, businesses people and a variety of "community" players to work toward the pursuit of enlightened capitalism.

The Trillium Foundation has an excellent executive summary from a major report they did on commercial ventures being undertaken by nonprofits in Canada.

Calvert Community Investments

Calvert Foundation

1-800-248-0337

www.calvertgroup.com/foundation

Checklist for Going Into Business

Questions you should ask yourself --

The same questions other people will probably ask you!

What is your product or service? What does it look like? What needs does it meet?
What quality is it?

The Customer...

Who are your customers? What is the age, sex, income level, lifestyle, needs and taste of your customers?

What are the benefits they want from this product or service?

Are people buying more and more of this product/service or less and less? Is there a steady demand for it throughout the year, or is it seasonal?

The Competition...

Do you know the other people who are in this business?

How do their profits look?

How near in location is your nearest competitor?

What makes you think their customers will leave them and come to you instead?

How much are they selling the product or service for right now?

Can you beat the big guys? They buy in volume and have good credit lines with the suppliers. What kind of edge do you have over them?

Would you be aware of new techniques that might make your business more efficient and more competitive?

The Company...

How much are they willing to pay for your product or service? Do people absolutely need it, or is it something they can do without?

Does the style in the product or service change rapidly? Can you adapt as readily?

How will people know about you and your product or service?

How are you going to produce and distribute it?

Can you pretty much predict how many sales you will make on an average day, an average week, an average month?

What is the image you will try to project in the marketplace?

Forewarned is Forearmed

A nonprofit will find that the traditional sources of capital such as banks and lending institutions are not very interested in a nonprofit group seeking money for their for-profit venture. If you seek outside funds, you will have to convince a lender or investor that your group is real, the proposed venture is viable and can be economically justified. Being aware of the misconceptions that exist in the minds of potential lenders or investors will help you develop a strategy and a business plan for changing their views.

Some commercial lending sources see a nonprofit parent organization as becoming separated from the needs it was established to serve and competing unfairly with other businesses. Your lawyer and accountant can show that you are playing by the rules.

Disproving the fictions will be a necessary part of your approach.

Fiction: Nonprofits can overwhelm local businesses.

Fact: A nonprofit's own purpose and efforts to provide services is a limiting factor on the size of an enterprise.

A nonprofit undertaking a for-profit enterprise channels private resources into business and the community; business and nonprofits are economically dependent -- nonprofits do business with business.

Fiction: Nonprofits can't attract funds.

Fact: Nonprofits do attract human and cash resources (grants, donations, volunteers, materials, or goods).

A profit making enterprise can also serve customers who are other businesses.

Fiction: Nonprofits are unable to attract talented management because they cannot offer the career paths, compensation, or recognition comparable to the business sector.

Fact: Nonprofits attract talented, creative individuals whose skills are developed and transferred into other career areas along the individual's career path.

Fiction: Nonprofits are not single-minded enough or as adaptive as for-profit firms.

Fact: Continuity in a nonprofit's own purpose and strength of community and political support is comparable to customer loyalty.

Nonprofits have a history of flexibility to changing community needs and developing or adapting innovations.

Fiction: Underlying the general perception of non-profits as a threat to business is a fear that nonprofits cannot survive in the business world without government protection. And that the protection provides an unfair advantage to the nonprofit as it operates the venture.

Fact: Federal and State policies were created to permit business operations but to set boundaries around nonprofits operating businesses.

On the local and community level, the issues are more immediate. The nonprofit has to change misconceptions at this level through contact with community leaders. The law permits a much wider range of activity that most members of the public are aware of. There is a real community education job to be done here.

APPENDIX A: Human Services Futures: A Strategic Vision

By Jim Masters, Center for Community Futures

The book titled *An Incomplete Guide to the Future*, by Willis Harman, provides significant insight about how American society is changing and how those changes will shape the need for alternative types of work, including social enterprises. This paper:

- Projects how those changes are driving and reshaping human services;
- Suggests a model for projecting which services have healthy futures and which others will die on the vine; and
- Speculates on some new roles for nonprofits.

This chapter is divided into three major sections.

Section I. Work and the future nonprofit mission in relationship to work roles.

We suggest five goals.

Each has one or more assumptions underlying it, and some examples.

Section II. Trends creating winners and losers in human service programs.

Applying the methodology of the Boston Consulting Group to human services.

Section III. Proposed organizational structure for the future.

How to group the functions in your organization to maximize your success.

Section I. Work and the future nonprofit mission in relationship to work roles

Goal 1. Develop real numbers about the available jobs and education levels needed, and use them to demythologize planning for WIA, vocational education, and education.

Assumption 1. Employment in meaningful work is symbolic of having a place in the social order. When on a geographic or professional frontier, or building something new, even routine tasks have meaning. When people talk about meaningful work, they mean the central purpose of the work has significance, not that the specific tasks do.

Assumption 2. Advanced industrialized societies do not provide enough work roles to meet the needs of its members. There are a lot of complicated reasons for this, but there will never again be enough of the KINDS OF JOBS THAT OUR PARENTS AND MOST OF US THINK OF AS "real jobs."

Assumption 3. The percent of the workforce needed for agricultural production has declined to about 3%. For industrial production--of all of our consumables from cars to computers to cans to canvas--we are down to 25%. So -- work as the method for paying people for their contribution to increasing the material wealth of society and needed consumables is relevant for only about 40% of the population. This percentage will continue to decline, because capital used for production purposes will continue to move offshore where labor is cheaper (steel, cars, clothing, electronics, etc. etc. etc.). Work opportunities of this sort will continue to become more scarce.

As this happens, educational levels for the remaining jobs continue to rise. For most jobs they are already far beyond what is needed to do the job. The education gate is primarily a tool for reducing the pool of eligible applicants to a manageable size. This trend will continue, and additional education will have a negative effect on people who are unable to find work that makes use of their enhanced training. e.g. the consequences of most adult education and job training--focused on finding a job in the industrial sector of society--will be counter productive. "The myth of education as a sure route to increased status, power and income has been exploded. It is estimated that from two to three million college graduates will be competing for blue-collar jobs during the next decade" (p. 55). Education and training for one of the new "experimental" roles (described later) may have a positive benefit for some.

Assumption 4. The social function of work is a "legitimized role in the activities of society." Self esteem comes from "having a social role that others judge to be useful." The task then is to define new social roles which are perceived to be useful, and which provide a basis for the transfer of income to the practitioner.

Assumption 5. "Thus although full employment is not needed from a production standpoint, full participation is essential from a social standpoint." The process of production absolutely fails to provide enough roles as vehicles for the fulfillment of the income-distribution task facing society. The nonprofit and private sectors are both places where new roles for participation can be developed and tried out.

Goal # 2. There are four types of jobs. Find ways to increase the number of acceptable social roles in job types three and four. STOP trying to push people in the ever decreasing categories one and two.

Assumption 6. There are basically four types of jobs, or four sectors of the economy

1. primary (agricultural, mining)
2. secondary (production)
3. services
4. learning, knowledge industries, arts, religion

The first two have too many people in them now. There is some opportunity in types three and four.

Goal # 3. Find ways to increase the number of people in transfer payment categories a, b, and c, while reducing the number of people on d.

Assumption 7. Transfer payments are made for four types of recipients:

- a. membership category (wives, children, veterans).
- b. social investment (research grants, scholarships; subsidized student loans, housing).
- c. need, conditional. Based on past status as a worker or on current behavior. Aid to Disabled. Elderly. Farmers. Employees and supplies of major US corporations that have failed to advance with the times (Chrysler, U.S. steel, etc) Unemployed who lost their jobs through "trade displacement." Payments based on national service.
- d. need, unconditional. Welfare. (Although more than 60% of the total population are supported by transfer payments, most of the scapegoating and stereotyping is focused on occupants of this category -- which is only about 5% of the total.)

Example # 1. Expand the number of scholarships, student loans, stipends, sabbaticals, for people who want to pursue any purpose -- no matter what it is -- but preferably related to jobs in the areas of services and knowledge.

Example # 2. Shift people from transfer payment type d to transfer payment type c. Call it workfare, job experience, or anything. Go all the way. LET THEM PICK THEIR OWN TASKS. That is the way the Local Initiatives Program works in Canada. It does not have to be in an "agency" or a "factory." Let those who are self-starter define their own roles. Picker- upper-of-aluminum-cans. Sweeper-of-neighbors-steps. Visitor-of-the-elderly. Domino or bingo-leader-at-park. Who cares? Avoid bad publicity or illegal activities, but the premises are that (1) anything is better than nothing at all, and (2) we need a period of experimentation to find new roles that will be perceived as legitimate reasons for giving people money, and (3) as those emerge they will be the basis for new social patterns that move people from transfer category d to a, b, or c.

Example # 3. In England and France. About 35,000 people a year now take six or twelve months worth of their "welfare" or unemployment checks in a lump sum and use it to capitalize a new "business" venture, i.e. anything they think they can earn money at. This approach is not suitable for everybody, but it has produced 63,000 new jobs!

Example # 4. How about "worker enhancement." Somebody who has demonstrated they can produce in a structured job--on the assembly line--they have "earned" their place in society. They take an enhancement grant and do something "to carry out some other project of manifest social value" including learning, community work, etc. We pay farmers for not growing crops, why not pay assembly line workers for doing something different for a while. This would also free up another structured job for the a person who needs it. This is what VISTA, ACTION, and the Peace Corps are all about. We need to find more reasons for existing work roles to be "enhanced" into some other form.

Example # 5. Any social enterprise.

Goal # 4. Start at least one Social Enterprise each year. If you can, legitimize role for nonprofit agencies as test sites where ventures can fail. If you can't sell it, bury it. If you can't bury it, create a new agency that you can afford to lose. But do it!

Assumption 8. The public good can not tolerate a City or County Government losing credibility through a high-profile failure. So they are far too cautious -- and this arena demands boldness, not caution. Who is uniquely suited to explore these new social roles? To provide the test sites? Nonprofits. They can provide the framework and process for analysis, dialogue, and experimentation. Let them proliferate. Set up a bunch of them -- a new test site for each new idea. We can afford to "lose" a nonprofit that runs a program that fails.

Goal # 5. To make sure that a "fair share" of jobs, and employment and training opportunities go to each major population group, e.g. minorities, women, etc.

Assumption 9. Although there will not be "enough" jobs for all who want them, there is an equity or distribution issue where nonprofits can play a role. To make sure that various population groups have equal access, that eligibility criteria do not discriminate, and some proportion of the slots go to all eligible. This advocacy function across several projects will probably get you into many disputes, but may be very effective from a social perspective. This is the "allocation" department.

Section II. Human Service Program Winners and Losers

Now we're going to shift to a discussion about trends in the underlying social values that shape the framework for human services, and take a look at which of them offer promise and which are losers for the coming decade -- because these may identify sectors where we want to do a social enterprise. Or, not.

The Boston Consulting Group got famous for their assistance to businesses in determining which product lines or "stars" they should invest new money in, which of the maintainers they should they should "milk" but not put any substantial effort into, and which were "dogs" that should be dumped. Their recommendations are based primarily on two factors, rate of growth of the market for the product and the percentage of market share held by the company/product. In addition to those two elements, for our purposes I would suggest adding other factors:

1. Rate of growth of sector over past five years
2. Percentage of market share nonprofits now hold vs. public agencies
3. Breadth and type of political support (score plus one point for each major social constituency; plus two for each major business sector supporting it e.g. farmers for food stamps, doctors for Medicaid; minus one for each type D transfer payment population who are more than 50% of the recipients)
4. Levels of political support (Fed Executive Branch support= plus two, Fed Executive opposition minus two; Congressional support plus one, Congressional opposition minus five and goodbye); local = 0; state=plus one.
5. Intensity of constituency--will they go to the wall? (Zero to plus three.)
6. The competition in the delivery system, i.e. ease of penetrability or their ability to resist new delivery agents taking part of the pie, (other nonprofits, plus one, state government=0, county government=minus 2)
7. Degree to which conceptual frame is perceived by public as attached to obsolete versus modern principles. (e.g. civil rights confrontation politics versus children, self help. (Minus two to plus two.)
8. Consistency with other megatrends--from centralization to decentralization, from youth to aging, etc. (Minus two to plus two.)

So a scoring system like this could also come up with three categories, (a) programs that are long term decliners or clear cut losers (b) "cash cows" that are "maintainers" but that are programs in flux, with it not clear where they will come out, and (c) "stars" where investment in future growth should take place. Using the BCG criteria, here are my guesstimates on how current programs fit into those categories.

This does not speak to the moral worth, merits or effectiveness of any of these programs. It only describes their relationship to the current “drivers” of program expansion or contraction. So “losers” in this context means “losing out” over time because they are less consistent with the driving trends. And “winners” means the are expanding because they are more consistent with the driving trends.

“Losers.”

Section 8

JTPA Title III -- displaced workers, JTPA for Adults for Job Types 1 and 2

AFDC,

Alcohol/Drug Treatment Prevention Programs

Vocational Education for "underemployed"

Free food. The cheese supplier to the poor

TANF, welfare to work

Apprenticeship Programs in Trades

Adult Basic Education for First or Second Sector Jobs

"Traditional" Economic Development, attract a factory/ build an industrial park.

Public Housing

Maintainers, but in flux or transition.

Adult Basic Education

Vocational Education for entry-level positions. (School to Work)

Pre-voc, job readiness

Weatherization

Youth

CSBG development/administration of other programs

Halfway Houses

WIC

Alcohol/Drug Treatment Services as ancillary to other health service delivery

SSBG Day Care

Future Growth Areas/Stars/Winners

SSBG Senior citizens

Child Protective Services

Head Start

Family Development

E&T for Adults, but only for job types 3 and 4 (services/knowledge)

Adult Day Care. Long Term Care and Protective Services

Homesteading/low-income co-op conversion in buildings where acquisition cost is in the \$1 category, i.e. in rem buildings or acquisition cost partly or totally written down

CDBG for Third and Fourth Sectors of the Economy

Child Care/all forms, especially where parent/employer pays part of cost

Business incubation

Earned Income Tax Credit

Food Stamps Work Requirements

National Service

Transfer Payments (Development, recruitment, screening, administration of payments for loans, scholarships, grants, for transfer payment types 1,2, and 3)

Senior Housing/Centers/Transportation

Title XIX, Medicaid, Home Health Care, Home Attendant Services

Services to Handicapped or Developmental Disabilities

WIA/TANF support for entrepreneurs/conversion of hobbies to income producing jobs, experimenting with "new occupations"

Middle income weatherization partially or wholly supported by utilities.

Demand-side management), utility restructuring

Senior citizen employment

Workfare, something required in return for general assistance, other type four transfer payments.

Section III. Organizational Structure for the Future

My theory is that the agency getting ready for the future should group its functions into the following six divisions:

1. The old division. Where the "clients" are. This division administers the "categorical" programs which are defined by people someplace else who decide what will happen to whom under what circumstances. You can identify these programs by the amount of time clients spend passive, such as waiting-in-line, waiting for the clerk, listening to explanations of the program's rules, waiting for the job opportunity, waiting for the cheese, etc. Many people will never be able to be anything but clients, but the systems should be focused and the pressure kept on to move people out of client status. A five year limit to welfare? A sunset clause terminating any social program after ten years?

2. The empowerment real-life vision building division. Where the "participants" are packed into crowded rooms yelling about their problems, the neighborhood, the community, and what should be done about them. This division is charged with recruiting new people--people who are perplexed, but are willing to act in the "Do something, even if it's wrong" mode. People in transition from being clients to being citizens.

3. The equity/allocation/fair share division. Monitor eligibility criteria, intake, placement, to make sure various population categories get a "fair share" of the four types of jobs, of opportunities for training and other public programs.

4. The debunking division. Fight myths with facts. Deal yourself into JTPA, Voc Ed, Education planning with facts and figures about the current and future reality of life in American society.

5. The future program division. Punching, digging, dealing, and selling your way into the cash flow on the programs listed that will be "stars," through contracts for administration (recruitment, screening, check processing) or as a vendor of goods and services that is supported largely or wholly by transfer payment type a, b, or c.

6. The business incubation and social enterprise division. Where the "citizens" are engaged in self-help of the usual and most unusual types. Where new social roles are created and tried out--with the foreknowledge that most will not take in the general society--but where the willingness to try and act is defined as socially useful. Many people here are defining the purposes of their activity. Many pick off of "idea lists" created by others. Most are self-directing in the performance of those activities, some

need structure and supervision but that is only for the people who are seeking entry into the "structured" economy.

The activities are on a wide spectrum of "real" social usefulness. Outside most of the "normal" hierarchy, policies, and procedures. You will have to fight tooth and nail to get waivers, or more gradual wind-downs, of existing policies that "tax" the person who is successful at developing an income stream for a high percentage of their new created earnings by cutting off Medicaid, transfer payments, services.

Perhaps the citizens have an equity position in this division through "sweat" equity, or purchase of \$50 in stock by borrowing the money from the agency, and that they then have to work for their company--which empowers them to try new work patterns.

Redefine transfer payments so that recipients do have to do something to receive the money, get your agency or a new nonprofit recognized as the entity that will identify the "something," do not get tapped into the usual "workfare syndrome" that the jobs have to be real, closely supervised, leading to permanent employment, which is myth layered onto misperception.

Argue that the work must only be socially useful, and that some work is better than no work, and that you don't know what forms the work will take, and much of the work will be you providing support for such self directed activity, and that many of the new forms of work you will try will not be traditional, and that there are no real jobs out there for most of these folks anyhow. But you will improve their social productivity--and social productivity is a new concept that is as important as economic productivity.

Remember! The goal for this division is not to find "real" jobs for people, nor is it to leave them in a client status where they are vilified by the transfer payment system and the public. The goal of Division 6 is to find new roles (1) in which people feel like they are participants in society, roles that produce self-esteem, and (2) for which society will authorize a transfer payment to them. So you take the list of new roles, activities and outcomes back to the city council, the welfare department, or whomever, and find out which ones are accepted. And you have started to redefine and to create the real future of American society. Isn't that what nonprofits are for?

APPENDIX B: Examples of Ventures By Nonprofits

You now have a good idea of assets you have on hand, what you can sell and an inkling there may be a market. Take a look at the categories of industry and the range of businesses to stimulate your thinking. You can translate an asset analysis to fit those businesses most closely related to the business you think your agency will start.

The "Range of Businesses" list includes shoe-string operations and more costly enterprises started by or bought into by nonprofit agencies. An estimated start-up capital range is included for some of the examples. This information, taken from current franchise listings, closely approximates the amount needed even if you aren't in the least interested in franchise. If you have location, equipment, cash or personnel, start-up costs for your business will be lower. If your agency is considering a franchise, franchise fees are separate costs (in parentheses), be sure to check all facts and figures before you buy. Federal franchise law imposes strong limitations on what a franchiser can propose to you.

Business Models

We've examined significant process and business elements and suggested practical tools and approaches for establishing a profit making business. You may wonder what was the process like for other organizations, what were the results, what did other organizations encounter or learn in the process.

This section centers on models or examples illustrating the development of profit making ventures and entrepreneurial activity by nonprofit agencies. A listing of other business ventures by nonprofits is included. We urge you to contact these groups and talk to those who have gone through the process. Finally, a list of low investment start-up businesses is provided.

Examples of Possible Business Ventures by Nonprofit Organizations

Possible business ventures by non-profit organizations:

- Art (production, rental, sales)
- Automobile repair
- Bicycle repair/rental
- Bookstore
- Catering services
- Childcare/education services
- Consulting services to other nonprofits (corporations, politicians, etc.)
- Credit union
- Educational Software (books, programs, designs, consulting)
- Financial investment
- Furniture repair/manufacture (used office furniture, donations).
- Gas station operation/oil distribution
- Grocery store (sales, delivery)
- Housing (home improvement, construction, rehab, management)
- Janitorial services
- Landscaping services
- Laundry services (pickup, delivery, laundromat)
- Lodging services
- Manufacturing (compost, topsoil)
- Print shop operation
- Publications (newsletters, reports, manuals)
- Real Estate (rentals, leases, sales)
- Recycling (paper, glass, plastic, aluminum, oil)
- Restaurant
- Security services
- Social services
- Specialty stores (herbs, body lotions, etc.)
- Thrift shop operation
- Travel agency
- Weatherization (products, services)

The following pages will be real examples of these businesses.

Low-Investment Businesses

Business	Minimum Start-up Investment	Average Net Profit Before Taxes	Stability	Risk	Prospect for Industry Growth
Auto Detailing	\$13,000	\$100,000	Mod.	Mod.	Very Good
Bridal Consulting	\$4,000	\$40,000	High	Mod.	Very Good
Business Plan Consultant	\$10,500	\$110,000	Mod.	Mod.	Excellent
Day Care Service	\$13,500	\$58,000	Mod.	Mod.	Very Good
Computer Consultant	\$3,000	\$40,000	Mod.	Low	Very Good
Co-op Mail Service*	\$7,000	\$40,000	Mod.	Mod.	Very Good
Damage Restoration*	\$9,000	\$150,000	Mod.	Mod.	Excellent
Environmental Services	\$7,000	\$65,000	Mod.	Mod.	Excellent
Event Planning	\$12,500	\$100,000	Mod.	Mod.	Very Good
Financial Aid Services*	\$14,500	\$98,000	Mod.	Mod.	Good
Freelance Writing	\$5,000	\$25,000	Mod.	Mod.	Fair
Freight Broker	\$12,000	\$40,000	High	Mod.	Very Good
Gift Basket Service	\$11,000	\$42,000	Mod.	Low	Very Good
Graphic Design	\$9,500	\$26,000	Good	Low	Very Good
Home Health Care Agency	\$7,000	\$300,000	High	Mod.	Excellent

Low-Investment Businesses - Continued

Business	Minimum Start-up Investment	Average Net Profit Before Taxes	Stability	Risk	Prospect for Industry Growth
Home Inspection	\$11,000	\$45,000	High	Low	Excellent
House Painting	\$13,500	\$25,000	Mod.	Mod.	Fair
Import/Export	\$13,000	\$120,000	Mod.	Mod.	Excellent
Information Broker*	\$7,000	\$72,000	High	Mod.	Excellent
Janitorial Service	\$12,000	\$27,000	High	Mod.	Very Good
Language Translation	\$11,500	\$92,000	Mod.	Low	Excellent
Lawn Care	\$7,000	\$22,000	High	Low	Good
Maid Service	\$4,000	\$28,000	High	Mod.	Very Good
Mobile Disk Jockey	\$7,000	\$55,000	Mod.	Mod.	Good
Multilevel Marketing	\$6,000	\$40,000	Mod.	Low	Excellent
Multimedia Services	\$14,500	\$227,000	Excellent	Mod.	Very Good
Personal Shopper	\$3,000	\$20,000	Low-Mod.	Mod.	Fair
Children's Books	\$15,000	\$54,000	High	Low	Very Good
Professional Organizer	\$7,000	\$55,000	Mod.	Mod.	Good
Property Tax Consultant	\$4,500	\$100,000	Mod.	Low	Very Good
Specialty Advertising*	\$5,500	\$33,000	Mod.	Mod.	Fair

Low-Investment Businesses - Continued

Business	Minimum Start-up Investment	Average Net Profit Before Taxes	Stability	Risk	Prospect for Industry Growth
T-Shirt Printing	\$5,000	\$140,000	Mod.	Mod.	Good
Bill Auditing*	\$7,000	\$55,000	Mod.	Mod.	Good
Vending Machine Business	\$13,000	\$90,000	Good	Low	Good

* Notes on Businesses:

Co-op Mail Service: A business that redeems coupons for other businesses.

Damage Restoration: A business that helps people cope with property damage due to natural disasters.

Financial Aid Service: A business that assists students find academic scholarships and loans.

Information Broker: A business that uses high technology to do research for other businesses.

Specialty Advertising: A business that manufactures promotional products for other businesses.

Bill Auditing: A business that monitors and audits utility and telephone bills for other businesses.

Information derived from: *The Top Low-Investment Businesses for the 90's*, Entrepreneur Magazine Group, 1995.

APPENDIX C: Sources of Information - Organizations

The Center for Community Futures

PO Box 5309, Berkeley, CA 94705.

510/339-3801, www.cencomfut.com

Offers workshops and publications for nonprofit organizations considering for-profit business enterprises.

National Economic Development and Law Center

2020 Broadway, 7th floor, Oakland, CA 510/251-2600

Provides business planning, research, and legal assistance (some of it free over the phone) to nonprofit community-based developers. They have targeted the second-hand, resale, and recycling industries and have several experienced staff members and a set of research papers on this subject.

US Small Business Administration

www.sbaonline.sba.gov

800/8-ASK-SBA

The Small Business Administration has a network of Small Business Development Centers (SBDC) and Business Information Centers (BIC) that can assist entrepreneurs with business plan development and financing. The BICs have a full library of start-up information. There is a listing of all BICs in the appendices.

Materials for the Future Foundation

Presidio Building 1016, Suite 222

PO Box 29091, San Francisco, CA94129-0091

Contact: Erica Adshead415/561-6530; Fax: 415/561-6474

Email: mff@igc.apc.org

MFF helps nonprofits start recycling, reuse, and remanufacturing projects. They offer mini-grants up to \$5,000 in two yearly cycles specifically for market study, business planning, and related research studies, and larger grants for business capitalization and operations (RECLAIM program). MFF staff also provides free technical assistance and information referrals, as well as a newsletter and conference/workshops to all interested groups.

Social Enterprise - Thrift Shops

NARTS

National Association of Resale & Thrift Shops

P.O. Box 80707, St. Clair Shores, MI 48080-0707

Phone: 1/800-544-0751, 810/294-6700

Fax: 810/294-6776

Email: webmaster@narts.org

Web site: www.narts.org

NARTS is the only national trade organization representing the Resale Industry. Founded in Chicago in 1983, they now have over 1000 members, representing thrift, resale, and consignment shops throughout the country. NARTS offers member services including a catalog of books, national conference, 1 and 2-day training workshops held in different cities each year. They also publish a list of members, available for \$3.00.

Books distributed through NARTS:

Sold Gold Success Strategies for Your Business. The book includes personal and business strategies for sales, planning, and customer service. Offered through NARTS. 211 pages. \$16.95

1001 Ideas to Create Retail Excitement. "A Storehouse of practical suggestions that show small-to-medium sized retailers how to attract new customers and keep them coming back." Offered through NARTS. \$19.95

101 Big Ideas for Promoting a Business on a Small Budget. 97 pages. \$12.95.

Starting & Operating a Business series. A separate manual for each state to guide you through the state and federal regulations. 68 pages. \$24.95.

Katydid Press

2592 York Road, Columbus, OH 43221

Contact: Kate Holmes

614/487-0709 (voice & fax)

Email: katetgtbt@aol.com

URL: <http://www.tgtbt.com>

Catalog for the Professional Reseller

To Good to be Threw. Newsletter. Also publishes numerous pamphlets on marketing, promotions, advertisement samples, etc.

To Good to Be Threw: the Complete Operations Manual for Consignment Shops. Columbus, OH: Katydid Press, 1997.

Step by step instructions and advice from successful consignment store operator on choosing a location, setting prices, determining costs and the break-even stock; advertising, hiring and training employees, planning for future growth. 202 pages. Price: 69.96; NARTS members \$59.95, plus shipping.

Entrepreneur Magazine Group. *Consignment/Resale Clothing.* Entrepreneur Business Startup Guide No. 1229. Irvine, CA: Entrepreneur Media, Inc. (Business Report Division) 1993.

Notebook format, with sections on conducting a market study, selecting location; planning the facility, equipment, inventory, hiring and training personnel, legal requirements, advertising/promotions; operations; fashion trends, and startup issues such as preparing a business plan and applying for a business loan. Most of the information is generic to all types of very small retail businesses. Includes computer diskette for business planning spreadsheet.

The Resale Connection

Box 562

Palm Harbor, FL

34682-0562

813/768-7047

A monthly newsletter published since 1985; over 1,000 subscribers. \$28/year. Contact: Millie Shafer, Publisher.

Contains: Advertising tips & ad designs, Marketing ideas & promotional ideas, Annual financial survey, Tax tips, Trends

Window design, Shop management (employee manuals, business structures, shoplifting deterrents, etc.)

Harris Publications

PO Box 297

Sonoma, CA 95476

707/939-9124

Email: rtnc@sonic.net

<http://www.secondhand.com>

Publishes a free bimonthly newspaper--Rummaging through Northern California (RTNC); 17,000 copies distributed free at 400 Bay Area locations. For 6 issues of paper plus Resale Directory, \$5.95/year. Web page contains links to other helpful publications and resources.

Internet Resale Directory

Featuring web pages for secondhand, consignment, flea markets, thrift shops, collectibles, & surplus businesses on the World Wide Web. Web Inserts/Listings, \$40/year; individual Web pages; \$150/year.

American Business Directories, Inc.

5711 South 86th Circle, PO Box 27347

Omaha, NE 68127

800/555-6124, 402/593-4600

Publishes the following directories: Clothing Used Directory, Consignment Service Directory, Furniture Dealers - Used Directory, Thrift Shop Directory

CALMAX - California Materials Exchange

Published in print and on the Web at <http://www.ciwmb.ca.gov/mrt/calmax/calmax.htm>

While building materials predominate, there are listings for fabric, textiles, and rags, as well as electronics and other durable goods such as office equipment and lighting fixtures. The web version offers instant listing for free to buyers and sellers, donors, and donees. The print version comes out quarterly. California Waste Management Board, Sacramento, CA.

Second Chance Week. Oct. 18-26.

The Local Government Commission, of California, is sponsoring a week of events through public agencies, universities, school districts, reuse and repair businesses. The idea is to publicize and promote yard sales, collection and donation drives, reuse and repair workshops, thrift and consignment store sales, and reuse art contests.

The promoters will provide a planning calendar, guidebook posters, Public service announcements, brochures, and logo.

US Small Business Administration

www.sbaonline.sba.gov

800/8-ASK-SBA

The Small Business Administration has a network of Small Business Development Centers (SBDC) and Business Information Centers (BIC) that can assist entrepreneurs with business plan development and financing. The BICs have a full library of start-up information, including the *Entrepreneur Magazine* series. Look for Entrepreneur Business Guide No. 1229, "Consignment Clothing Store."

Franchises

Once Upon a Child and Play It Again Sports

4200 Dalhalberg Dr.

Minneapolis, MN 55422-4837

800/445-1006, 612/520-8500, www.ouac.com (Once Upon a Child)

800/592-8049, 612/520-8500 (Play It Again Sports)

Consignment sporting goods franchise.

Terri's Consignment World

1826 W. Broadway Road, No. 3

Mesa, AZ 85202

800/455-0400, 602/461-0400

Consignment home furnishings franchise.

CA Directory of Reuse & Repair Programs and Organizations

Local Government Commission

1414 K Street, Suite 250, Sacramento, CA 95814

916/448-1198; Fax: 916/448-8246

Email: lgc.waste@bbs.macnexus.org

Discovery Shops

An American Cancer Society Enterprise

1/800-854-4ACS

URL: <http://www.ca.cancer.org>

National Recycling Coalition/California Resource Recovery Association

4395 Gold Trail Way, Loomis, CA 95650

A membership organization addressing issues of expanding markets and products for recycled materials. They address state and national policy issues.
Contact: Gary Liss, 916/652-4450.

Materials for the Future Foundation

Presidio Building 1016, Suite 222

PO Box 29091, San Francisco, CA 94129-0091

Contact: Erica Adshead 415/561-6530; Fax: 415/561-6474

Email: mff@igc.apc.org

MFF helps nonprofits start recycling, reuse, and remanufacturing projects. They offer mini-grants up to \$5,000 in two yearly cycles specifically for market study, business planning, and related research studies, and larger grants for business capitalization and operations (RECLAIM program). MFF staff also provides free technical assistance and information referrals, as well as a newsletter and conference/workshops to all interested groups.

APPENDIX D: Sources of Information: Books and Magazines

General

Kamoroff, Bernard. *Small-Time Operator: How to Start Your Own Business, Keep Your Books, Pay Your Taxes, and Stay Out of Trouble*. Laytonville, CA: Bell Springs Publishing, 1998.

This book/workbook is updated annually and a very good resource for those new to business. Available in bookstores.

Caftel, Brad. *Business Development by Charitable Organizations: Legal Structure Issues*. Oakland, CA: The National Economic Development and Law Center, October 1995.

DuRand, John. *The Affirmative Enterprise*, MDI Press, 670 Pelham Blvd, St. Paul, MN 55114 282 pages. A "big" book!

Gottrey, Heather. *Profit or Perish: Non-Profit Social Service Organizations & Social Entrepreneurship*. Georgetown Journal on Poverty Law & Policy. Summer, 1999 Volume VI Number 2. Pp 249 – 276. Comprehensive overview of the legal issues.

Hammack, David C. and Dennis R. Young, eds. *Nonprofit Organizations in a Market Economy: Understanding New Roles, Issues, and Trends*. San Francisco, CA: Jossey-Bass Publishers, 1993.

The Roberts Foundation. *New Social Entrepreneurs: The Success, Challenge, and Lessons of Non-Profit Enterprise Creation*. San Francisco, CA: The Roberts Foundation, 415-561-6533.

Shabecoff, Alice. *Strategy Alert - Can this Business Succeed? Nonprofits and Community Economic Development*, Fall/Winter, 1996, Issue #48. Washington, DC: Community Information Exchange.

Shore, William H. *Revolution of the Heart: A New Strategy for Creating Wealth and Meaningful Change*. New York, NY: Riverhead Books, 1995.

Skloot, Edward, ed. *The Nonprofit Entrepreneur: Creating Ventures to Earn Income*. New York: The Foundation Center, 1998.

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Good list of questions prospective thrift store operators will need to answer in order to develop a viable business: project goals, type of store, legal requirements, staffing, types of pricing, management tasks; how to generate inventory; segment of market (income levels); competition, etc.

Power Pack: 20 Proven-effective Letters, Forms and Contracts for Dealing in Distressed and Surplus Goods. Seattle, WA: Career Research Institute, ND.

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TVI, Inc. & Value Village Stores, Inc. *Commitment to Innovation.* TVI, Inc. Washington, DC.

Describes the TVI Value Village second hand department stores, inventory, and its partnerships with nonprofits to purchase donated clothing in bulk.

Ware, Henry Holdship. *Starting and Managing a Swap Shop or Consignment Sale Shop.* Washington, DC: Small Business Administration, [for sale by the Supt. of Docs., US Govt. Print. Off.], 1968. Series title: Starting and managing series ; v. 15.

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Practical advice to the new trader on setting up businesses and buying and selling in general; flea markets, auctions, books, real estate, getting loans, etc.

APPENDIX E: Recent Articles

“Benefactor Venture Philanthropy.” Mark Dowie. *Worth*, p. 68 (February 1999).
Describes George Roberts’ social entrepreneurship ventures.

“The Business of Doing Good.” *Worth* (March 1996). Interview with Bill Shore.

“Business Ventures for Nonprofits – Finding the Right Legal Structure.” Brad Cafel. *The Grantsmanship Magazine* (Winter 1997).

“Charities Change Roles by Turning a Profit.” Bill Shore. *USA Today* (March 26, 1996). Corporate sponsorship of charities.

“Cultivating Alternatives For the Poor.” Kevin Fagan. *San Francisco Chronicle* (December 22, 1996). The work of Building Opportunities for Self-Sufficiency (BOSS).

“The New Dog-Eat-Dog Nonprofit.” Donna Fenn. *Inc.* (July 1995).

“Entering Another World.” Susan Gray. *The Chronicle of Philanthropy* (April 9, 1998). Supporting charities to run for-profit businesses.

“Enterprising Nonprofits.” J. Gregory Dees. *Harvard Business Review* (January/February 1998). Benefits and costs of corporate sponsorship of nonprofits.

“Famous Last Words of the Failed Social Entrepreneur.” Jed Emerson. *The Grantsmanship Center Magazine* (Summer 1996).

Filthy Rich & Other Nonprofit Fantasies: Changing the Way Nonprofits Do Business in the 90's. Richard . Richard Steckel, Berkeley: Ten Speed Press, 1989.

A primer for thinking about the way nonprofits can undertake profit-making ventures. There are a number of other books written by Steckel on the same topic. Available in bookstores.

“Harvard Webheads Aim to Save the City and Show a Profit.” Thomas Petzinger, Jr. *Wall Street Journal* (February 13, 1998).

CitySoft Inc. in Boston offers inner-city people employment creating websites.

“Is This Any Way to Run a Cheese Museum?” Eggers and O’Leary. *Governing* (November 1995).

“It’s Not How much You Give, It’s How You Give It.” Bill Shore. *The New York Times* (September 27, 1997). Nonprofits are joining with business partners as an alternative to donations.

“Handle With Care: Choosing a Corporate Partner.” Richard Steckel. *Entrepreneurial Nonprofit Leader*, p. 1 (May 1997).

“Health Clubs Cry Foul as Y’s Go Upscale.” Liz Neporent. *New York Times* (February 2, 1999).

Looking at Income-Generating Businesses for Small Nonprofit Organizations. Berea, KY: Duncan, William A. The Mountain Association for Community Economic Development, June 1982.

“The New, Dog-Eat-Dog Nonprofit.” Donna Fenn. *Inc.*, p. 45+ (July 1995).

“The New Social Entrepreneurs.” Heather R. McLeod. *Who Cares* (April 1997). The Entrepreneurial Development Institute (TEDI) and others.

New Social Entrepreneurs: The Success, Challenge and Lessons of Non-Profit Enterprise Creation. San Francisco: The Robert Foundation Homeless Economic Development Fund, September 1996.

This free publication documents the work of the Roberts Foundation in assisting nonprofit organizations undertake profit-making businesses. Excellent case studies. Roberts Foundation, PO Box 29266, San Francisco, CA 94129, 415-561-6680. The prefer you download it off their web page at : www.redf.org.

Non-Profit Agency Tries its Hand at Entrepreneurship.” Rick Romell. *Milwaukee Journal Sentinel* (WI) (October 19, 1997).

The Center for the Deaf and Hard of Hearing sells and services equipment for people with hearing loss.

“The Nonprofit Entrepreneur: Creating Ventures to Earn Income” Edward Skloot, Ed. New York: The Foundation Center, 1988.

Nonprofit Organizations in a Market Economy: Understanding New Roles, Issues,

and Trends. Hammack, David C. and Dennis R. Young, eds San Francisco: Jossey-Bass Publishers, 1993.

“Nonprofits That Turn a Profit.” Bill Shore. *The New Democrat* (November/December 1997). Creating community wealth.

“Profits for Nonprofits: Find a Corporate Partner.” Alan R. Andreasen. *Harvard Business Review* (November-December 1996). Cause-related marketing.

“PTA Getting Lectured About Office Depot Deal.” Tamara Henry, *USA Today* (September 2, 1998).

Criticism over the PTA allowing Office Depot to use its name and logo in back-to-school advertisements.

“Putting Charities in Business.” Vince Stehle. *The Chronicle of Philanthropy* (October 3, 1996).

The work of the Roberts Foundation in San Francisco that advances businesses owned by nonprofits.

“A Recipe for Sweet Success.” Vince Stehle. *The Chronicle of Philanthropy* (February 20, 1997).

The Greyston Bakery in Yonkers, NY that makes brownies for Ben & Jerry’s ice cream.

“Should Not-for-Profits Go Into Business?” Edward Skloot. *Harvard Business Review*.

“Social Entrepreneurs: Nonprofit Executives are Finding New Ways to Merge the Profit Motive with Moral Imperatives.” Jerr Boschee. *Across the Board* (March 1995).

“Surviving Success: An Interview with the Nature conservancy’s John Sawhill.” Alice Howard and Joan Magretta, *Harvard Business Review*, October 1995.

“What Do You Do When Traditional Sources of Funding Fall Short? Enterprising Nonprofits.” J. Gregory Dees. *Harvard Business Review*, p. 55+ (January-February 1998).

Thrift Articles

These articles were found in the Business & Industry Index, an extensive database cataloging articles from newspapers, journals, and international news services compiled by KR Information Ondisc (TM) and the Digital Library Systems. This list was supplemented with ProQuest, an index by UMI Company. Infotrak is another widely available database of this kind and is available at many libraries. Recommended key words include: used merchandise; second-hand stores; thrift stores; resale; vintage clothing; used equipment; used goods; consignment; charities.

“American Park 'n Swap Gets Contracts.” American Park 'n Swap, flea market operator, won 3 new contracts to manage markets in Virginia, Pennsylvania, Arkansas. *Amusement Business*, Vol. 108, n. 15, p 16 (April 8, 1996).

American Park 'n Swap, a division of Delaware North Companies, Inc., Buffalo N.Y., has signed a long-term lease for operation of The Super Flea Market in Richmond, Va. Plans for the market include new signage, entertainment and renovation of existing facilities. The Super Flea mascot will be introduced as a promotion and entertainment feature of the market. In Pittsburgh, American Park 'n Swap will operate The Super Flea Market at Eastland Mall in North Versailles. The Richmond and Pittsburgh properties are leased from Benderson Development Corp., Buffalo, N.Y.

American Park 'n Swap has also signed an agreement with the Arkansas Livestock Exposition to manage the Quality Flea Market in Little Rock on the fourth weekend of each month at the Little Rock Fairgrounds. American Park 'n Swap manages flea markets and antique markets selling new and used merchandise and produce. Their operations bring in revenue to facilities such as convention centers, exhibition halls, racetracks, malls and stadiums.

“Antique Malls Fill Shoppers' Desire For Choice, And Choices Are Growing.” Mike Billips. *Macon Telegraph* (GA), May 1, 1995.

Abstract: The Big Peach Antique and Collectibles Mall (Byron, GA) has over 100 booth spaces for antique dealers, with 55 presently rented. The antique mall is housed in a 30,000 sq ft metal-framed former peach-packing warehouse. Phase 1 of its development will use about 16,000 sq ft. Future development will include a mezzanine level. The owner plan to add a diner and a false-front Western street with craft shops. They believe that Interstate 75, the stream of tourist gold that runs by their place, will pay for that and more. Antique malls are one way of taking advantage of the antique shopper's tendency to go from shop to shop. Georgia state tourism officials have been marketing Middle Georgia as a mecca for antiques and collectibles shoppers for the past two years with the Georgia Antiques Trail. The trail winds from Covington to Milledgeville, to Macon and south to Perry, and back north through Barnesville and McDonough, picking up other towns along the way.

“Appliance recycler seeks to expand.” *Waste News*, 1,33:6 (April 15, 1996)

Minneapolis -- Appliance Recycling Centers of America Inc employs 40 and has combination appliance recycling and retail sales centers in Austin, Dallas, Bryan, and Houston. In 1995 they bought Appliance Distributors, a recycled appliance company employing 320 and operating in the Southwest and Gulf Coast markets. Appliance Distributors also exports appliances to Central and South America.

“Bank to Open a Spruced-Up Pawn Shop in Its Rural Georgia Town.” *American Banker*, Vol. 162, n. 70, p. 8 (April 14, 1997).

Abstract: Citizens Bank of Vienna, GA, plans on opening Exchange Pawn, a pawn shop, in an attempt to fill a niche market, according to Daniel Speight Jr, chief executive officer of the small Georgia bank with \$99 mil in assets. The pawn shop will give people another way to borrow money, according to Speight. The shop is part of Citizens Bank's strategy of creating different levels of lending in its town to increase its loans. Citizens Bank is hoping to dispel the image of tacky pawn shops. Its shop will be a high-end business. Georgia regulators have approved the pawn shop.

“Boulder County, Colo., Used Clothing Stores See Gold In Dated Fashions.” Ericka Gonzalez. *Daily Camera* (Boulder, CO) (September 10, 1996).

Excerpt: "The number of people entering the used clothing industry is climbing nationally.... According to a survey by G.A. Wright and Associates in Denver and Dun & Bradstreet, between 1989 and 1993 the number of thrift shops nationally increased by 30 percent, climbing from 41,898 in 1989 to 51,926 three years ago. Despite growth in the used clothing business, Gary Wright, president of G.A. Wright and Associates, says the industry hasn't really affected traditional retailers who offer only new merchandise. "I'm not sure that they're offering any meaningful competition to normal retailers," Wright says. The majority of thrift/vintage shops, according to the 1993 survey, for example, are generating individual revenue of \$1 million or less annually. Being an industry where multimillion-dollar sales are not typical can be tough, especially in a city like Boulder where retail rents can run as high as \$40 per square foot."

“Building a Biz.” Paul Consiglio. *Small Business Opportunities*, Vol. 7, n. 3, p. 54-5 (May 1995).

“Buyers Like The Lower Cost Of Quality Used Goods At Resale Shops.” Cecilia Deck. *Detroit Free Press* (MI) (May 8, 1995).

Resale is growing at faster rate than general retail, according to U.S. Census Bureau figures and to anecdotal accounts from the Grosse Pointe, Michigan-based National Association of Resale and Thrift Shops. In Michigan from 1987 to 1992, sales at resale stores grew by 47 percent, while overall retail sales were up 27 percent, according to the U.S. Census. The number of resale stores in Michigan grew from 425 to 537. "Consumers are becoming more aware of reuse and recycling," says association spokesperson Adele Meyer. "Conspicuous consumption is out."

Children's Orchard is a resale store that sells secondhand dresses. They're tagged with bar codes, like dresses at new clothes stores, and they're fully returnable. Resale, once looked down on as garage sale trash, now has become the darling of a growing number of retail chains that cater to middle- to upper-income shoppers. These chains locate in strip shopping centers, display their goods like new-product retailers, have consistent pricing and offer product guarantees and return policies. Franchisees say they try to price items at 50 percent of what they would cost new. "Ultra-high-value resale" is what Michael Moe, a stock analyst with Lehman Bros. in New York, calls it.

Other franchised resale stores include Michigan-based Children's Orchard, and two chains that sell new and used interactive computer games: Funcoland and Game Power Headquarters. Mike Seavitt, franchisee at the Once Upon A Child shop in Southgate, says the advantage of a franchised company is getting computerized lists showing best-sellers and prices for standard brands. "We look for clothing that was at higher price points to begin with," he says. The problem is that a used-clothing store that sells higher-priced items needs a population base of about 70,000 to 80,000 families from which to buy clothing. The chains started opening in the Detroit area in 1990, and already they're starting to overlap. The article further details other stores selling secondhand clothing.

"For Play It Again Sports, which has been franchising since 1988 and is the oldest of the franchised resale chains, the challenge is not a competing chain but trying to buy used merchandise at its peak popularity, when people aren't yet ready to sell. "You can't control your inventory of used equipment," says Dave Bone, franchisee for Play It Again's Ann Arbor and Ypsilanti stores. "The things you want most, you can't get enough of." He mentions in-line skates, hockey helmets, adult softball gloves and power treadmills, the current rage in exercise equipment. Play It Again makes up for the lack of used inventory by stocking new items in many categories, priced competitively with major chains. Its product mix has evolved to about 70-percent new merchandise, Bone says. "If I had my druthers, we'd sell more used. But since we can't, we offer the best prices we can on new." The chain's sales at more than 500 stores topped \$200 million last year. Its biggest seller is hockey equipment, most of which is sold used. Bone estimates it would cost \$350 to outfit a 6-year-old

in new hockey equipment, but only \$200 to \$250 using a combination of new and used equipment from his stores."

"Can You Get it Used?" Ronaleen R. Roha, *Kiplinger's Personal Finance Magazine*, Vol. 51, Issue 8, p. 174-9 (August 1997).

Abstract: Much of the resale industry is moving upscale, and advice is given for finding used computers, cameras, watches, sports equipment, musical instruments and kids' stuff.

"CD Warehouse Picks Up Fellow Used-CD Firm Disc Go Round." Don Jeffrey. *Billboard*, Vol. 110, Issue 26, p. 10+ (June 27, 1998).

Abstract: Jeffrey reports on CD Warehouse's acquisition of Disc Go Round, a franchised chain of used-product stores, for \$7 million cash. CD Warehouse plans to open 40 to 50 stores this year.

"Charity, Retailer Team Up For Trade-In Promotion: Goodwill Industries joins Service Merchandise for a national trade-in promotion rewarding Service Merchandise customers who bring in household items." *Promo*, Vol. 9, n. 9, p. 10 (August 1996).

Abstract: Goodwill Industries is joining Service Merchandise for a national trade-in promotion rewarding Service Merchandise customers who bring in household items. A discount will be given to them off similar items that are new. A 32-page direct mail piece will explain the promotion that will be mailed to 12.5 mil homes. The items collected by Service Merchandise will be donated to Goodwill Industries.

"Children's Orchard to open 5 new north suburban stores in Chicago area." *Crain's Chicago Business*, Vol. 19, n. 7, p. 42 (February 12, 1996).

The Chicago-area franchisee for Ann Arbor, Michigan-based Children's Orchard Inc. plans to open five new north suburban stores. The 56-store retail chain that sells used children's clothes, toys and equipment has stores in Arlington Heights and Lake Zurich.

"Computer-Friendly Charity." John Gibeaut. *ABA Journal*, Vol. 84, p. 100 (June 1998).

Abstract: The ABA's Technology Exchange Project accepts donations of used computers and gives them to various programs that provide free legal services to the poor. This is crucial to legal aid programs facing funding cuts.

"Computer Resale Shops Offer Buyers Alternatives." Michael Maurer. *Crain's Detroit Business*, Vol. 11, n. 14, p. 11 (April 1995).

"Cost-conscious shoppers seek secondhand." *USA Today*, p.1 (March 8, 1996).

"Outlets offering used items ranging from furniture to sporting goods and tools are increasing, with patrons increasingly coming from the mainstream of society. Such stores include second-hand stores, flea markets, pawn shops and even garage sales."

Goodwill Industries International in 1995 expected an 11% increase in retail revenue to \$500 million up from the previous year with \$470.3 million. To serve the growing number of higher income shoppers, it plans to renovate 150 of its 1,300 stores. TVI (Bellevue, WA), which has 100 used clothing and furnishing stores, says the average income of customers is around \$35,000, up from around \$12,000 in 1989. According to Susan Whittaker, president of the National Association of Thrift and Resale Stores, revenue at used-item stores rose around 10% in 1995.

Currently, women's clothes make up 58% of thrift-store sales, but furniture is a growing area in second-hand shopping. In sporting goods, Play It Again Sports, with 650 stores, is the largest chain of used sporting goods in the US; parent company Grow Biz has also opened 45 Computer Renaissance stores selling used computers. In the area of automobiles, used car sales grew 5% in 1995 while new car sales dropped 3%. Other areas seeing growth are sellers of used bridalwear and compact discs.

"Emphasizing Customer Service: Play It Again Sports." *Small Business Success*, Vol. 10, p. 17 (1997).

Profile of a successful Play It Again Sports franchisor in California.

"Find the Best Toy Bargains." Ruth Richman. *Good Housekeeping*, Vol. 225, Issue 1, p. 143 (July 1997).

Abstract: Toy bargains can be found at shops that sell "gently used" merchandise. Tips for shopping for these items are offered.

"Finding Resale Opportunities." *Nation's Business*, Vol. 85, Issue 7, p. 53 (July 1997).

Abstract: Various Web sites that contain resale listings for franchises are listed.

"First-Rate Growth With Second-Hand Goods." Cash Converters USA buys and sells used products in three 3,000-sq foot stores in US; it is part of Cash Converters Int'l, which has 300 stores worldwide. *Boston Globe* (MA), p. G4+ (January 19, 1997).

Abstract: Cash Converters USA Inc. (Delaware) buys and sells used products in three 3,000-square-foot stores in the US. It is part of Cash Converters International Ltd. which has 300 stores worldwide and profits of \$3 million on revenues of \$12.8 million in 1996. The stores are located in Chicago, Seattle and New England; 1,000 more are planned to be built within five years. The stores offer an alternative to purchasing expensive new products which can be outdated quickly such as computers, portable phones or answering machines. The franchise fee is \$250,000. Lance S. Haver, education director of Consumers Education & Protective Association International (Philadelphia, PA), cited the company's market as the working poor and the middle-class but warned consumers that used products are not covered by their original warranties and consumer protection laws. Cash Converters however, offers a 30-day warranty on its products. Their store owners determine how much they will pay for merchandise that they will sell based on condition and demand. Todd Zukowski, co-owner of the New England store in Ashland, hopes for \$1 million in sales in 1997. A product in his store is a 19-inch color television with remote control which was acquired for only \$60 and will be sold for \$119. His products include guitars, power tools, computers, jewelry, exercise equipment, video cameras and stereos.

Portable electronics are fast sellers while televisions, computers and entertainment centers are not. Competitors of Cash Converters include Grow Biz International Inc. and Play It Again Sports stores. Cash Converters USA operated at a loss during its first year of operation in 1996.

“Glamour Thrift Shops.” Janet Forman. *Family Circle*, Vol. 111, Issue 13, p. 14 (September 15, 1998).

Abstract: The Colleagues Gallery in Santa Monica, CA specializes in second-hand clothing from celebrities like Jimmy Stewart and Nancy Reagan. Proceeds from the merchandise go to benefit Children's Institute International.

“Goodwill Delivers Computers To The Inner City: Goodwill Industries hopes to sell 500-1,000 used personal computers by the end of 1996.” *Minority Markets Alert*, Vol. VII, n. 12, P. 8 (December 1995).

Inner city residents nationwide will be able to get personal computers through Goodwill Industries, the nonprofit organization where many shop for furniture, clothing and other household goods. John Brier, Director of Information Services for Goodwill Industries in Pittsburgh, urges individuals and corporations to donate used computer to Goodwill. Old equipment, much of it viable for word processing, spread-sheet use and access to the Internet, is being refurbished and offered to those in need for under \$100 for a simple set-up to \$125 for a full system of monitor, keyboard, mouse and modem. For those really in need, the equipment

may be available for as little as \$10, with the Buhl Foundation picking up the rest. Carnegie Mellon University has joined the program, and Brier says he hopes to be moving 500-1,000 PCs by the end of '96. Persons wanting computers submit applications that are assessed on basis of need by a selection board. [Source: Goodwill Industries of Pittsburgh, John Brier, 2600 E. Carson St., Pittsburgh, PA 15203; phone: 412/481-9005; fax: 412/481-2091.]

“Grow Biz: Good as new - Grow Biz International's operating income rose from \$774,000 in '92 to \$4 mil in '96.” *Discount Store News*, Vol. 36, n. 9 (May 5, 1997)

Abstract: The largest and most visible of the companies in the second-hand retail segment is Grow Biz International (Minneapolis, MN). Grow Biz controls separate resale chains in five product categories. The five chains are: Play It Again Sports, Once Upon A Child, Computer Renaissance, Disc Go Round, and Music Go Round. Grow Biz revenues have rocketed from \$27 mil in 1992 to \$92 mil in 1996, while total retail sales zoomed from \$60 mil in '92 to \$415 mil in 1996. Operating income rose from \$774,000 in '92 to \$4 mil in '96. On a year-to-year basis, system-wide sales grew 24% to \$113 mil for the first quarter of 1997.

Today Grow Biz operates close to 1,200 stores in the United States, Canada, Europe and Australia, rolling out new stores at 200 per year. Play It Again Sports retails about \$350 mil and is the fifth largest specialty sporting goods chain. Computer Renaissance will break into the ranks of the top 50 computer retailers in 1997. Each chain uses an everyday low price strategy. Grow Biz has done little or no national advertising but remains focused on building brand awareness. Contracts call for franchisees to spend 3% to 5% of sales on local promotions. Competition comes on a variety of fronts not least from charity operations. Goodwill Industries International had 1996 sales of \$550 mil from 1,350 stores in North America. The Goodwill stores are expanding, upscaling and moving into better neighborhoods. The article continues and discusses more specific information about the competitors, and prototypes across all Grow Biz formats and others issues relating to Grow Biz stores.

“Grow Biz International: Building on a Used Foundation.” *Stores*, p. 26 (May 1996).

Grow Biz International (Minneapolis, MN) had almost 1,000 stores operating at end-1995. It had \$100.2 mil in 1995 revenues and had awarded 1,311 franchises at end-1995, with 965 stores in operation, including 157 Once Upon a Child, 662 Play It Again Sports, 44 Computer Renaissance, 94 Disc Go Round, and 8 Music Go Round stores. Once Upon a Child retails used and new children's apparel, and Play It Again Sports sells used and new sporting goods.

“Growing Up.” Holly Celeste Fisk, *Entrepreneur*, p. 157 (March 1997).

Profile of a franchise, Children's Orchard, seller of used children's clothing.

"Half-Price Books plans fourth Indianapolis location; privately-owned company has total of 55 book stores and sales of over \$50 mill/yr," *Indianapolis Star* (IN) (February 5, 1997).

Abstract: Half-Price Books (Dallas, TX) is scouting for a fourth Indianapolis location to accommodate its strong and steady growth. The company, headed by president Sharon Wright, is privately-owned, has 55 book stores, 6.5 million items in its inventory and annual sales above \$50 million. Wright said the company is doing well in the fiercely competitive world of bookselling. Half-Price opened its 55th store in its eighth state in 1996. Its share of the market is concentrated on used books, used magazines and used CDs and a percentage of new books. The company was founded by Pat Anderson and Ken Gjemre who vowed never to sell a book for more than half of its cover price. The company never deviated from its original concepts such as never fall into debt, stock a variety of items and keep prices low. It also encourages its employees to have a broad range of interests. The company has a firm policy of internal hiring and requires anyone who aspires for a management level position to work in a store first. It also adheres to a controlled compensation philosophy such that Wright receives only five times the lowest paid employee's salary and the same share as everyone when the company distributes 30% of its pre-tax profits to employees each year. Half-Price stores also support social and environmental programs around the country and donates money and books to schools, libraries and literacy groups. Article provides additional information on the company.

"Insight: Direct Resale of Computers and Peripherals." Jeanne C. Lee. *Fortune*, Vol. 136, Issue 1, p. 92-4 (July 7, 1997).

Abstract: Insight has grown into a \$373-million-a-year direct reseller of computers, peripherals, parts and programs.

"New Money in Old Goods." Anne D. Robinson. *Small Business Opportunities*, Vol. 8, n. 3, pp. 46,8 (May 1996).

"Nigeria-Economy: Flourishing Market For Second-Hand Goods." Toyé Olori. *Interpress Service*. Jul. 11, 1996.

Abstract: "Select Markets or Bend-down Boutiques" have become popular one-stop shops for extremely cheap, second-hand goods, including clothes, household items, books, and cars. As the goods flow in mostly from Asia and Europe, poor Nigerians welcome the trend with relief, and see the flourishing trade as the new employer in a country where 10+ mil people are out of work. Bargain prices at these markets attract people from all classes. Besides the "Bend-down Boutiques," major streets in Lagos have been converted into open markets for the sale of second-hand household appliances. The second-hand boutiques have popped up not just in the capital, but all over the country. But

some environmentalists in Lagos are not so keen about the boom in second-hand appliances because they may pose health and environmental hazards. Local manufacturers are facing hard times, due to the popularity of second-hand goods, high cost of foreign exchange, high inflation, shortage of raw materials, and rising cost of utilities.

“Not a Mall, and a Lot Cozier.” Elaine Louie. *The New York Times*, Sec. 9, p. 1 (May 31, 1998).

A description of the vintage clothing shops in New York’s neighborhood north of Little Italy.

“The Pawn of a New Era is Upon Us.” Bruce B. Auster. *US News & World Report*, Vol. 123, Issue 22, p. 64 (December 8, 1997).

Abstract: Pawnshop chains are transforming the business with new markets, new customers and a new image. Cash America is the biggest of the new chains, which make money from the interest on loans rather than the resale of pawned goods.

“Pre-owned Profits.” Kay D. Vanier. *Income Opportunities*, Vol. 30, n. 2, pp. 112-4 (February 1995).

“Putting Used Goods to Good Use.” Susan Kolnitys. *Income Opportunities*, Vol. 29, n. 7, pp. 76+ (July 1994).

“Ready to Wear.” Amy H. Berger. *Income Opportunities*, Vol. 30, n. 8, pp. 112+ (August 1995).

“Resale Retailing’s Rebirth.” *Childrens Business*, Vol. 11, n. 11 (November 1996).

Abstract: Like the secondhand clothing it profits from, the resale business has been resurrected, with two rapidly growing franchise operations largely responsible. Thanks to the efforts of leading franchise chains, The Children’s Orchard and Once Upon a Child, it has become more efficient--not to mention socially acceptable--for consumers to make and save money (on average 50% off original retail) by trading in and buying up gently used children’s clothing, toys and juvenile products. Since the advent of these trailblazing merchants in the early '80's, resale retailing has been charting particularly strong and steady growth. According to a report prepared by the US Census Bureau for The Children’s Orchard, resale accounted for \$5.2 billion in sales in 1987. In 1995 that figure nearly doubled to \$10 billion. During that time, regular retail sales only grew 52%. The Children’s Orchard is headquartered in Ann Arbor, MI, and has more than 60 stores coast to coast. Over each of the last three years, the

company has witnessed a 20% growth in sales, reaching \$11 mil annually. Once Upon A Child is based in Minneapolis and now boasts 177 franchise locations across the US and Canada. In 1995 sales, were \$37 mil, with projections for this year to reach \$48 mil. This is an extensive article that goes into great detail about the franchises and the industry.

“Resale thrift shop sales rose to \$13 million in 1995.” *About Women & Marketing*, Vol. 10, n. 2, p. 5 (February 1997).

The National Association of Resale and Thrift Shops has seen its memberships increase 20% a year since 1993 to 1,000 members. A survey of subscribers to The Resale Connection reports that [their overall sales] sales rose from \$9 million in 1993 to \$13 million in 1994. Source: *Boston Globe*, Boston, MA, February 9, 1996

“Salvation Army launches superstore concept; new 19,000-sq-ft store opens in Chicago area.” *Chicago Tribune*, p. 4 (February 5, 1996).

As part of a new strategy to raise money for its charitable causes, the Salvation Army has launched a new superstore concept with a handful of stores across the US including a new 19,000-sq-ft store in Bridgeview, IL, a suburb of Chicago. The charity has invested \$250,000 in the concept, and is managing the stores in the same way that one would manage other large retail stores. The store, which employs 22, sells used merchandise for an average price of \$2.50 per item. The Salvation Army claims to spend up to \$4 mil per year on charitable causes including offering clothing, meals and housing to the needy.

“Secondhand Success.” Frances Huffman. *Business Start-Ups*, Vol. 7, n. 2, pp. 74-7 (February 1995).

Profile of children’s consignment shop owners.

“Success At Florida's Goodwill - Suncoast A Lesson To Traditional Businesses.”

Goodwill Industries-Suncoast Inc, which had revenues of \$8 mil from retail sales, is adapting its training methods to former welfare clients. *St Petersburg Times* (FL) (January 20, 1997).

Goodwill Industries-Suncoast Inc. (St. Petersburg, FL) retails donated used merchandise such as clothing. Its stores generated sales of \$8 million in 1996, up 12% from the previous year. Store sales account for 62% of the company's revenues. Many of its employees, some of whom are handicapped or disabled, have not had prior work experience. The company's success is attributed to the strict but fair treatment accorded to the employees by Gina Weiss, the company's plant supervisor. The plant handles 37 ½ tons of merchandise a day, or \$1

million worth of goods a month. Traditional businesses are advised to emulate Goodwill's policies as up to 20,000 former welfare recipients in Hillsborough and Pinellas counties are expected to re-enter the labor force due to new restrictions on welfare eligibility. Article provides additional information on the firm.

“These Thrift Shops are Classy--and Doing A Booming Business.” *Wall Street Journal*. 3 Star, Eastern (Princeton, NJ Edition) Vol. 229, n. 13, p. A20 (January 20, 1997).

Abstract: Upscale thrift shops are the latest hot retailing trend, one which, according to Howard Davidowitz, chair of Davidowitz & Associates (New York, NY), a retail consultant, has tremendous growth potential. The National Association of Resale & Thrift Shops states its membership rose 12% during the past year to 1,000. Grow Biz International Inc (Minneapolis, MN) owns 19 corporate stores, has 1,000 franchises and intends to add 250 more franchises in 1997. Second Time Around (Boston, MA) had sales of \$575,000 in 1996, and represents the upper 5% of all sale stores. The owner, Jeffrey Casler, recently opened another unit on Cambridge, MA's Harvard Square, and contemplates a third outlet. Just 4.7% of resale and thrift stores cater to men, partly because men hang on to their clothes longer than women. Article discusses the trend in more detail, and goes in-depth on Casler's store.

“Thrift Meets Glitz on the Post Road.” Jack Cavanaugh. *The New York Times*, CT Section, p. 1 (June 7, 1998).

The thrift store movement takes root in Westport, Connecticut, that has one of the twenty Goodwill Stores in the state.

“Thrift Score / The Ultimate Consignment & Thrift Store Guide.” Bette-Lee Fox. *Library Journal*, Vol. 123, Issue 1, p. 114 (January 1998).

Book review of Al Hoff's *Thrift Score* and Carolyn Schneider's *The Ultimate Consignment & Thrift Store Guide*.

“Upscale Thrift Shopping Valued Highly.” Karen Alexander, *The Seattle Times*, p. D10 (May 1, 1992).

Description of TVI, Inc. and Value Village's buying bulk donations from nonprofits and reselling them at their 65 stores.

“What a Deal! Save \$100's on Practically Everything.” Nancy Dzija. *Family Circle*, Vol. 110, Issue 4, p. 36-9 (March 4, 1997). Abstract: Stores that sell used equipment are popping up all across the US and offer customers quality products at bargain basement prices. The advantages and disadvantages of buying used items and information on selling the consignment way are discussed.

“Why Thrift Shops are a Must.” Robert MacKenzie. *New Choices: Living Even Better After 50*, Vol. 37, Issue 4, p. 49 (May 1997).

Abstract: Thrift shops, stores where shoppers can purchase second-hand clothes, appliances, furniture or jewelry for discount prices, can make shopping more enjoyable. Several reasons why include shoppers and employees are usually friendlier, prices are lower, shoppers may find a hidden treasure and the money often goes to a good cause.

APPENDIX G: SBA Resources

Download these from their web page at <http://www.sba.gov/>

US Small Business Administration - Management Aid MP-11
Business Plan for Small Service Firms

US Small Business Administration - Financial Management Aid FM-4
Understanding and Controlling Cash Flow

Ramin C. Maysami
Assistance Professor of Economics
Sangamon State University
Springfield, Illinois

Resource Directory for Business Management
Directory of SBA Publications Available for Purchase

Appendix H. Business Development Process for Nonprofits

Here is an outline of a process to work your way through consideration of a venture. Not every organization will have to do every step, but it does help you to identify possible issues.

I. Review Mission and Goals

A. DETERMINE WHY diversified/extended business options should be considered.

What is profit making?

Why profit making?

Where are we now?

Compare your agency with other nonprofits.

Fears and realities -- make them explicit.

Making the decision to try it.

B. REVIEW POSSIBLE EFFECTS of profit-making activity.

Who are your current markets? Your other publics? For what?

What are the opinions on your Board of Directors?

Twenty questions to ask (and answer) before you begin, about:

organizational structure

personnel

finances, fiscal system

current programs and services

What you want from this venture -- what are your expectations. (These become part of your venture funding criteria.)

C. PREPARE THE ORGANIZATIONAL CLIMATE.

Organizational Culture. Is it ready?

Organizational support for intrapreneuring.

What does the agency want from the intrapreneur?.

What does the intrapreneur want from the agency?.

II. Conduct S.W.O.T. Analysis -- Strengths, Weaknesses, Opportunities, Threats

A. ASSESS TRENDS that help identify possible products/services...

Social, demographic, economic, political, etc.

Human services by Frank Benest

"Innovation..." by Peter Drucker

B. ANALYZE EXISTING SERVICES

Analyze your existing assets.

Unbundle existing services

Start a business with existing programs, functions people, property.

Buy a business? Franchises. Is this of any interest?

C. DETERMINE YOUR FINANCIAL GOALS for the new venture.

What is the fantasy rate of return? What is a realistic rate of return?

D. SCREEN THE OPTIONS. Select 2 -3 that have the best fit with strengths, risk tolerance, resources.

E. IDENTIFY THE PROJECT MANAGER or VENTURE MANAGER. Is the project manager the person who thought up the idea? Or somebody else?

Identify characteristics needed.

Identify candidates...hopefully people will volunteer -- you can't "appoint" an entrepreneur..

Evaluate candidates.

Negotiate compensation, expectations and other ground rules.

Select early, so s/he can help do the feasibility analysis.

III. Conduct Preliminary Feasibility Analysis

Review each potential venture to determine its possible impact on continued tax exemption, structural issues, other criteria.

A. LEGAL CONSIDERATIONS (YES IT IS legal to run a business and make a profit!)

Related versus unrelated businesses.

Implications for your tax exemption.

Taxable Income.

Is it profit or program income?

B. BUSINESS STRUCTURE

Separation issues, do you want this business to be in-house or out-of-house.

Control issues. How much do you want?

Forms of ownership.

C. ANALYZE THE COMPETITION

What are their benefits? Other key success factors?

Charges of unfair competition.

Anticipates ways to deal with charges of unfair competition.

Knowing and beating the competition.

Positioning through names.

Positioning: The Battle for Your Mind

D. IDENTIFY AND DESCRIBE THE CUSTOMER GROUPS

The Ps of Marketing.

PUBLICS.

Twenty-two market segments

Customer Profile Statement Examples

PRODUCT

Make explicit its **benefits**.

Give it positive tangibility.

PLACE.

The distribution system.

IV. Do Written Feasibility Study.

This is a detailed description the business products or services, business structure, competition analysis and implementation issues. This may be only a few pages long.

A. PREPARE A FORMAT FOR YOUR BUSINESS PLAN

Short? Long? Is it cheaper to "just do it" and reality test it that to plan, plan, plan?

B. CONTINUE WITH CUSTOMER ANALYSIS.

Low-cost market research techniques.

Do Market Planning Analysis

The Short Version

The "SBA" Version

Prepare your marketing strategy and plan.

Promotion: how will you get your message to the customers?

TEST the proposed business with potential customers.

C. SET PRICES.

Greg Newton's pricing rules.

D. BUSINESS STRUCTURE, LOCATION.

E. ASSESS FINANCING NEEDS.

Prepare pro forma financial statements,
start-up, one-year, three year.

Review business life-cycle funding methods.

Review types and sources of financing.

Meet with your banker. Get out your credit cards. Grab your bootstraps....

V. Checkpoint

- A. REVIEW AGAINST VENTURE FUNDING CRITERIA
- B. REVISE FOR BETTER FIT, MEASURE AGAIN
- C. DECISION TIME -- YES OR NO?
- D. IF YES, MOVE TO START-UP PHASE.

VI. Start up and operations

Loosen up! Move Fast! Ready Fire Aim!

Bennis & Nanus. "Manager versus Leader"

Harlan Cleveland. "Mindset for Leadership"

Rosabeth Moss Kanter. Change Masters

Arthur Deming's 14 Points for Managing Change and Quality

Tom Peters. "Thriving on Chaos"

Peters and Waterman. "In Search of Excellence."

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