



What You Should Know About...

Small Business Ownership

- ▶ BUSINESS PLANNING
- ▶ MARKETING
- ▶ FINANCIAL RESOURCES



Perhaps you've wondered about starting your own business some day because you've wanted to be your own boss, increase your income potential and achieve your dreams. Perhaps you own a small business that you'd like to expand. While being in business for yourself can be a challenge, it can also provide great personal and financial satisfaction. But starting a business is not something you want to tackle without serious thought and careful planning.

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A Business Decision

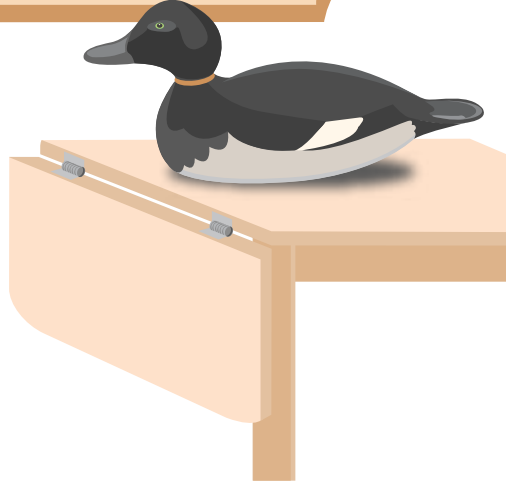
As part of deciding whether it's time to go into business for yourself, you'll want to evaluate your reasons, analyze your strengths and be honest about the potential challenges you face. You might start by asking yourself some hard questions about:



Your reasons. Your motivation to start a business may depend on any number of factors, such as a drive for personal fulfillment, a need for greater financial and personal independence, or simply a perceived niche in the business world that you think you can fill. Fully understanding and acknowledging your motivation can be important as you evaluate your potential for success in your business.



Your professional background. Where you're coming from when you start your business has a big impact on the experience you'll have. For example, if you're a lawyer giving up your career to start a bakery, you'll face a different learning curve than a former pastry chef. As a lawyer you may be familiar with the legal aspects



of running a bakery but new to the actual business of baking. As a pastry chef, you may be forced to learn some legal and business tasks, while turning out delicious desserts might be second nature.



Your time and financial commitment.

What you bring to the table in terms of your time and money will determine a lot about your business. If you're a stay-at-home mom sandwiching your small business in among playdates and field trips, you have a much different approach than someone who can devote

60 hours per week to a business and is willing to sacrifice her personal life. Likewise, if you have a million dollars in outside capital to invest, you're in a much different situation than someone financing a new business with personal savings.



Your concept: Where did you get your idea? You may be basing your business concept on the fact that four baseball card stores have opened in your town and you think there's an obvious trend here and room for one more. Or you may have a completely new idea and business concept, and will be positioning your business on the fact that it's totally different and unique. Both concepts might succeed, but the one you choose will determine how you create and manage your business.

The federal government's Small Business Administration (SBA) is a great resource for reading about starting, managing and financing your small businesses. Check its website at www.sba.gov. You can also find valuable information on loans and other services that may be available to you.

Defining a Small Business

What's a small business? There's no simple answer to this question. There were nearly 23 million businesses in the U.S. in 2002, the most recent year for which the Census Bureau has records. Small businesses represented 99.7% of all employers and employed 50.1% of the workforce (U.S. Small Business Administration). While these small businesses earn money in different ways, employ different numbers of people and generate different revenues, they also have a lot in common—the fact that they require commitment and resources.

Business Planning

Once you have your business idea, you need to develop a **business plan**. You may revise your plan over time as your company grows, the demand for your product or service changes or new competition enters the marketplace. But without a plan, or a blueprint to follow, it's hard to build your busi-

ness and easy to lose sight of what you're trying to accomplish.

You might think that a business plan needs to be very long and complex. In fact, it's just the opposite: the simpler the better. Regardless of what your business does, your plan should cover some basic elements. At a minimum, you should plan on addressing these topics:

- The **product** or **service** your company will provide, and what is different or unique about your product or service compared to those already in the market.
- How much you'll **charge** customers for your product or service.
- How you plan to **market** your company's product or service.
- Where you'll get the **money** to start your company.



Financial Resources

At the heart of any business plan is **capital**—the money you'll need to get the business started and keep it

running and growing. Here are some key questions to ask yourself:

- Will you generate enough revenue to cover your expenses and reach your goals? Revenue is the total money your business has coming in from sales of its products or services, and you calculate it by multiplying the number of product or service units you sell times the price per unit.
- What financial resources of your own do you have to put into the business?
- Will you be able to get outside financing?



If you need to borrow money, one of the first things any lender will want to see is your financial analysis of the business. Your financials must be realistic—and must show in great detail, often on a month-by-month basis, where you expect income to come from and your anticipated monthly expenses. This information, along

with a review of your personal credit history, will help a lender analyze the risk of extending a loan to you and assess the likelihood that your business will succeed.

A good resource for help with a business plan can be found at www.sba.gov/starting_business/planning/basic.html.



Starting with a Franchise



To start a business, you might consider a franchise arrangement. This gives you the right to sell the products and services of an established company, or franchiser, such as a fast food chain. Franchising can be a great opportunity to experience being a business owner while taking advantage of the support, services and training that the franchiser will provide. You need to read the fine print of the franchise agreement carefully to understand the extent of the financial commitment you are making, the restrictions under which you may have to operate and what happens if the business doesn't succeed.

Running a Business

There's a lot more to running a business than getting up in the morning and showing up for work. As a business owner, you're responsible for all aspects of the company. You negotiate agreements with clients and service providers. You train your employees

Survival Rates

U.S. Census Bureau data shows that half of new businesses survive more than four years, and about one-third of the businesses that closed before then were successful when they shut their doors.

and set the standard for customer service. You withhold income and Social Security taxes and forward the money to the government, while also making sure that you've paid your business taxes on time. True, you might have employees or outside professionals do some of this work, but at the end of the day, you are the owner and the buck stops with you.

Location

Where you decide to set up your business will depend on the type of company you have, whether customers come to you or you go to them, and, very often, what's available and what you can afford.

If you're providing a service such as home repair or construction, gardening or plumbing, your

primary concerns may be cost and convenience—you need a place to store equipment and keep your records. But if you have a retail shop, then location becomes critical—people need to be able to get to your store easily, and you want as much visibility as possible to attract attention and possibly get some walk-in business.

It may also be possible to work out of your home, provided you have room for any equipment or office space you'll need. In some areas, though, it may not be legal to operate a business out of your home. So be sure to check any local zoning ordinances before you set up shop at home, plus check whether any state regulations apply. For example, you may need a certain amount of space to operate a children's daycare center.

Very Small Business

Within the small business space, there are also categories known as micro businesses or micro enterprises. While some small businesses have as many as 500 employees, micro businesses usually have fewer than 10 employees and generate less than \$250,000 in revenues each year.



Equipment

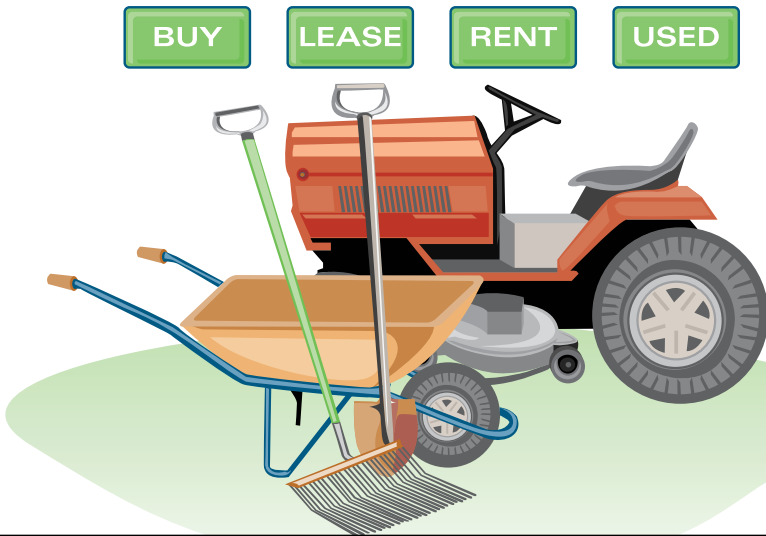
Virtually every business requires special equipment, whether it's a pizza oven, a panel truck or a set of mechanics' tools. And that's in addition to the basics, such as telephone service, a copier, a fax machine and a computer with an Internet connection. One thing to keep in mind is striking a balance between having enough equipment to operate efficiently and spending more than you have to.

Once you've identified the equipment you need—or must upgrade or replace—you might consider a leasing arrangement where you pay for the item over time, often with an option to buy it when the lease expires. That way, you can use the money you're not spending on an outright purchase to pay for other operating expenses, or to make other improvements to your business.

Inexpensive Equipment

And don't forget to search for and price your equipment purchases online, where you might be able to buy what you need more cheaply. You might consider starting out with second hand or used tools or furniture, which can often serve your business well, but which may cost many times less than equipment that you purchase new.

If you need autos, trucks or other machinery to run your business, you may also consider leasing rather than buying, or buying used vehicles. It's an added expense, but you'll also need to be sure you have adequate liability insurance. The state where you operate may require special drivers licenses for certain vehicles, and there may be zoning rules that restrict where you can park or store commercial vehicles.



Employees

While some small businesses are owned and operated by one person, most have a number of employees, including some that may work part-time.

Employees are often the “face” of your company—representing your company’s values and how your organization is perceived by others. So finding and retaining good employees is a major issue for companies of all sizes. It’s particularly important for a small business, since employees play such critical roles. For example, if there are five people in your company and two leave, you’ve just lost 40% of your staff. So picking the right employees, and providing them the right incentives to stay with you, is a top priority. Remember that your employees can help you win new customers, or lose existing ones, depending on their skill level and attitudes.

Making Employee Choices

Often the best way to find the right employees is to ask your current staff for referrals. You can also find employees by advertising in local papers or placing ads on job search websites that specialize in the type of business you operate. When interviewing potential employ-



ees, try to determine if they have the skills you are looking for and are likely to get along with your other employees. Be sure to check references from former employers, too. In a small company, flexibility is especially important, so you’ll want to know that anyone you hire will be part of the team and is prepared to handle several different duties if the need arises.

Remember Regulations

You must also be aware of local, state and federal regulations concerning employees, what protections—like workers compensation—you need to

Ladies First

According to the U.S. Census Bureau, women-owned businesses grew 20% from 1997 to 2002, which is twice the national average. These nearly 6.5 million businesses generated more than \$940 billion in revenue in 2002, up 15% from 1997.

provide, the different payroll filings you need to complete, and the amounts you need to pay for things like FICA (Social Security) and unemployment insurance.

It pays to work with a tax professional or accountant to be sure you avoid any penalties. You may want to outsource your payroll function and filing to a payroll service to help you comply with the regulations.

Working with Professionals

No matter how small your business is, you probably want to establish a working relationship with professionals who can help you navigate the world of regulation and finance. Networking via trade association memberships, attendance at seminars, or through trade industry directories or other publications, can help you identify and become acquainted with various professionals and the services they offer.

- **Legal Help** Since your business is a legal entity, you should have a lawyer make sure that all the paperwork is completed and has been filed with all of the required agencies.



For more information on the different ways you can set up your business go to www.yourmoneycounts/examples/business_types.html.

Your lawyer can also help you protect the business name, a special logo or trademark, or other proprietary material, and help you evaluate any potential liabilities or legal responsibilities you may have as the result of conducting your business. If your business involves intellectual property that should be patented or copyrighted, your lawyer can handle those filings as well or show you how to complete the paperwork.

Surety Bonds

If you are in certain businesses, such as construction or paving, you may find that you need a surety bond to bid on a particular job. The bond is a guarantee by an outside party, called the surety, that your business will meet the financial or performance obligations included in the contract and complete the work. The Small Business Administration (SBA) backs some surety bonds for eligible small businesses.



- **Tax Help** An accountant or tax professional can help make sure you file all necessary tax returns and reports. He or she can also help you determine if there are any special tax treatments for your business that could save you money, or if there are additional reporting requirements to avoid penalties. Your accountant can also be sure you make the required workmen’s compensation insurance payments to your state.



- **Insurance Help** An insurance professional can help you choose an insurance policy to cover any potential liability you might encounter while running your business. While not all small business owners need this type of insurance, many do. You’ll want to be sure to check where you fit. You may also need property and casualty insurance for your office and equipment, and perhaps disability insurance for yourself.



Product or Service Quality

As the owner of a small business, you are ultimately responsible for the quality of the product or service you and your employees produce. That means part of what you do every day is follow up with customers to make sure that they are pleased and would do business with you again. One advantage of a small business, after all, is that you can have this kind of direct contact.

If problems arise—and they inevitably do—you have to weigh customer service against the cost of redoing some or all of the work, or replacing a product. Customers know that mistakes happen, and they’re usually forgiving if you address the problem quickly and fairly. For example, you might

reduce the cost somewhat, or offer to provide an additional service at a discount—or if it’s small enough, for free.

There are no hard and fast rules for deciding how to accommodate someone who is unhappy, but remember it’s harder and more expensive to get new customers than to keep the ones you already have. Word-of-mouth advertising can either help or hurt your business. So once you’ve established a reputation, good or bad, it stays with you for a long time.

Marketing Your Business

People tend to buy products and services that they know and are comfortable with, that fill a particular need, or that they have heard about and are interested in trying. The role of marketing is to get the word out so people know about your business, set your company apart from the competition and continually reinforce the value of your products and services. When you market your business, be sure to address the “four Ps”:

- **Product**
- **Price**
- **Place**
- **Promotion**



Finding Resources

Federal and state agencies are a valuable resource for small business owners. If you want more information about specific aspects of small business, you might want to start with www.mymoney.gov or some of these other Internet resources:

Association for Enterprise Opportunity (www.microenterpriseworks.org)

My Own Business, Inc. (www.myownbusiness.org)

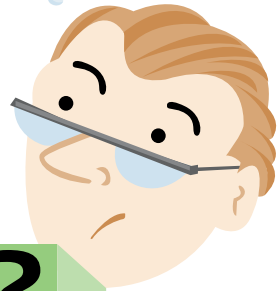
National Association of Women Business Owners (www.nawbo.org)

National Black Business Council (www.nbbc.org)

Product

To market your business, you need to be able to communicate exactly what your product or service is. One of the keys to business success is offering something that differentiates you from your competitors—even if at first glance what separates you might not seem that important. Perhaps in addition to mowing lawns, you offer a flower planting service that lets clients choose annuals to fill containers or line a walkway from an assortment you show them.

Another key to success is filling a need that the customers you're targeting may not even realize they have until you offer a solution. Then you have to be sure that those customers know why your business is the one to use. For example, maybe your dry cleaning business offers a drive-up window instead of requiring clients to walk into the shop to drop off or pick up their clothes. An advertisement that tells prospective dry cleaning customers about your drive-up service can set you apart from your competitors.



Price

One challenging aspect of running a business is figuring out how much to charge. You'll need to consider the direct costs of the supplies and equipment you use to make your product or deliver your service. But you also need to figure your indirect costs, or **overhead**—what you pay for space, employees who don't create the product or service, professional services you may use, such as a lawyer or accountant, plus what you pay yourself.

Obviously, price is important. But when you market your business, your message doesn't have to

be that you're the least expensive. In fact, if you're selling a product, it's difficult to be successful if you try to compete on price alone. A larger local company or a big chain can almost always charge less. That may make it hard to generate enough revenue with a discounted pricing structure to build your business.

In contrast, perhaps your company can charge a slight premium if you're offering an added service, like planting flower boxes or fertilizing bare patches in the lawn in addition to mowing lawns. Of course, if extra service is your point of differentiation, you do have to be sure that you can deliver what you've promised. If your customers are happy, they may be less concerned about the cost.

Know Your Customers

The type of customers you are trying to attract will also have an impact on how you talk about price. Some people put more emphasis on exceptional quality than on price. Others feel just the opposite. So you have to know which group you are trying to reach.

Equally important, you'll need to assess what your competitors are charging. If your prices are too high, you may have a hard time

attracting customers. And if they're too low, you may get the customers but not make enough profit to support your business. The key here is flexibility. You need to be ready to adjust your prices to reflect your costs, to stay competitive and to attract and keep customers.

You do have to keep your eye on whether your competitors are raising or lowering their prices, too, and how they're positioning those changes in their own marketing. That won't necessarily change what you're charging, but if other firms' prices are going up, it might be easier to position your own increases.

Place

Where you offer your product or service will influence how many customers you attract and who those customers are. Of course, it's pretty clear that it would be hard to build a successful business if you market snowplowing in Florida. But you have to make a number of



decisions that, while they aren't as obvious, can have a major impact.

If your business depends on clients coming to you, where it's located sends a message to the market segment you're trying to reach even if you don't emphasize location in your marketing materials. An address can provide a message of its own.

Place Matters

What's more, you have to be in a place where customers can find you—or better yet a place that they pass all the time. If your flower shop is on a side street off a pedestrian mall, you are likely to have less walk-in traffic than if the shop were located next to a popular bakery or right across the street from the local hospital.

Similarly, if customers drive to reach you, you'll want to ensure that there is enough parking. And if you're in a city, you'll want to think about where the nearest public transportation is unless your goal is serving the immediate neighborhood.



If you deliver your product or have it delivered, or if your service involves making house calls, place plays a different role. If you're in the construction business, for example, your clients probably don't care where you park your trucks. But having an area code that matches the code of the clients you're trying to reach suggests you're accessible. It may be worth the extra cost of a second line or an 800 number if you're located in the next county or across a state line.



Promotion

You may offer the best product or service at the best price in the area where you establish your business, but people need to know about it. You have to reach out to potential customers so they know what your business is, how it can meet their needs and why it's a better choice than the competition. Getting the word out is called promotion, and it's essential to your success.

Promotional Materials

One of the ways to tell prospective customers about your business is to prepare promotional or marketing materials that can be handed out, mailed or picked up from a store or office. Often, all you need to get started is a small brochure that describes your company, lists your products or services—perhaps including a price list—and tells people where to reach you.

Marketing materials don't have to be expensive. But since they may be the first impression you make on a prospective customer, you should be sure these materials present your company in the way you want. It probably pays to work with a professional who can write and design the material, though you can produce some very handsome brochures using a computer program and local printer.



As your business grows, you'll want to be sure to keep your promotional materials updated, especially if you include pricing, so customers know what to expect if they call or stop by your store.

Advertising



A traditional and effective way to gain awareness for your business, and attract the customer segments you've identified, is to advertise. Consider placing ads in local newspapers, community newsletters and other publications that your potential and existing customers are likely to see. Additionally, think about advertising online. It's a rapidly growing way to communicate with a target audience and promote your products or services to new customers.

Key Message

Focus on one key message that you want people to know about your business, and make that point. Ads

that are cluttered or wordy, or have too many different design elements, can obscure your message. And don't forget to include a "call to action"—why and how someone should respond to your ad and how they can do it, including your address, phone or fax number, or your website address.

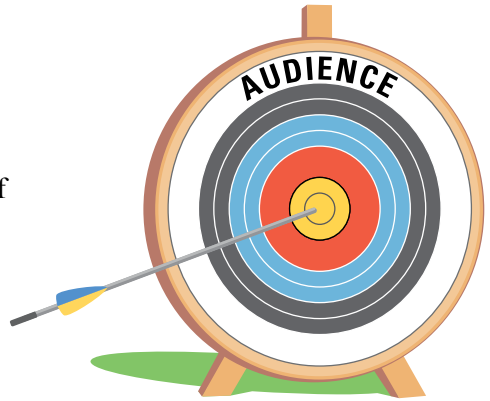
Also be sure to take advantage of your location. You can list special prices or sales in store windows, on walls or counters in your shop, on vehicles you use for business and on signs where you're delivering a service. And if you're participating in a community event or sponsoring youth athletics, see if there's an opportunity to display a sign or poster with your company name on it.

And don't forget basics like the local telephone book or yellow pages. They're still often the first places that people look when they need a service or want to buy something.

Waste Not

Remember that when you advertise, you'll want to be sure that your advertising dollars are targeted to the right audience—both in your message and how you say it, but also by the advertising method you choose. You want to

make sure you are not wasting money promoting your business to consumers who are not interested in your products or services.



Website

Increasingly, in addition to the yellow pages, people look for information on the Internet. So as part of your business plan, you should budget for creating a website that tells people about your company.

The website doesn't have to be complex or flashy—but it should describe your company, what makes it special, and how and where to get in touch with you, or the location and hours of your shop. Ideally, your website will include a picture or graphic to give people a sense of your business, and perhaps quotations, or testimonials, from people who have been extremely happy with your busi-



ness. Just be sure to get their written permission before you quote them or use their names.

There are tools available online to help you build your own website. But it may pay to contract for this work with someone experienced in website development. You can start by asking around for references, by checking the yellow pages or by visiting a website sponsored by the area you live in. And don't overlook local schools where you may find a number of students with these skills. Once your website is up, plan to refresh it from time to time as your business grows and as you offer new services.

Direct Marketing

For some businesses, direct marketing is another traditional way of reaching clients. It involves sending promotional pieces through the mail, making phone calls or sending email messages directly to your potential customers. Be sure that you know what you want



the direct marketing campaign to achieve—for example, to get people to try out a new product you're introducing, visit your shop for discounted or free merchandise, or receive an additional service for no extra charge by acting within a certain time period.

One of the hardest things about direct marketing is narrowing your target list and ensuring the names and addresses on the list are up-to-date. It's also important to keep track of your response rate, or the percentage of people who act on your offer. That way, you can compare the amount you spent on the direct marketing campaign to the amount of new business you attracted. This will give you a good sense of the cost of acquiring new customers using this kind of marketing.

Touchpoints with Customers

Marketing is not one thing or another, but the total impression you make on customers and prospects. Every time someone comes in contact with your business—from the colors, design, and words on a window sign or your website, to how an employee answers the

phone—is a customer touchpoint. Each touchpoint provides you with an opportunity to market your product or service, enhance your reputation or build awareness.

For many small businesses, keeping a high profile in community events can really pay off. Many people like to support local businesses, and your presence at school functions, neighborhood activities, community service programs and even local sporting events can help create a positive impression of your business. A small amount of time and money invested in your community can sometimes pay big dividends for your business.



Marketing is also the way you present yourself and your company—how you answer the phone and what you say, even how quickly you pick up—or the appearance of your shop, or the language you use in a letter or mail campaign. While covering all of these bases may be a challenge at first, in the end, the effort you put into marketing may prove to be one of the most critical factors in the long-term success of your business.

Segmenting the Market

The most effective marketing is targeted to the people who are most likely to buy your products and services. Within that group, there is a range of customers, from those who might be interested to those who are most likely to buy from you. This refining or subdividing of customers into different groups is sometimes called **market segmentation** or **customer segmentation**.

And even within the smaller group of good prospects, there are those you especially want to attract because they represent greater revenue opportunities if they become customers—for example,

because they have an ongoing need for your product or service and will purchase from your business repeatedly. The revenue from such customer loyalty is sometimes referred to as the “80/20 rule”—that 80% of a business’s revenues are generated by 20% of its customers.

To run a successful business, it’s important to know not only which customers make up this 20%, but also to continually ensure they remain satisfied. For example, if you run a pizza shop and a customer who usually orders from you every Friday night calls with a complaint about a late delivery, you may wish to offer free delivery next time, or perhaps even send a free pizza. The point is that it’s important to protect the loyalty of your best customers.





One Eye on the Competition

Part of your marketing strategy should be to pay careful attention to your competitors. For example, are they introducing new products or services, doing special promotions and gaining greater customer recognition?

Knowing what your competitors are doing might help you consider some innovations that they haven't thought of. For example, can you stage a special event in your shop that will attract certain customers, keep different hours that are convenient for working families, suggest new ways for using your product or service, tap a current fad that ties in with your business or offer a special service for repeat customers?

Never underestimate your competition, but don't assume that what a competitor is doing will

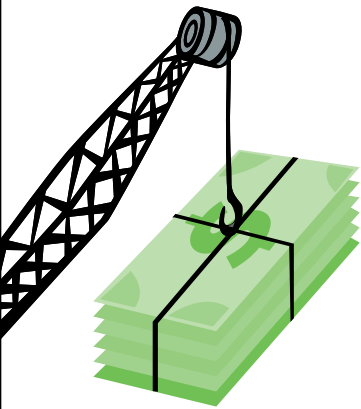
work for your business as well. You can beat your competition by planning, listening to your customers and anticipating the things they'll need or want—in other words, by looking forward, and not back over your shoulder.

Raising Capital

Many businesses fail, often within the first two years, for one simple reason: They are undercapitalized. That means they don't have enough money to get their business started or through some rough patches. So raising enough money, or **capital**, to start, maintain or expand your business is always a top priority.

Paying Back Counts, Too

If you have to pay back too much of the capital you've raised within a short time, or if the interest you're paying on the amount you borrow is very high, you may find that too much of your money is going to repay the loan, rather than keeping your business going.



Figuring What You'll Need

The amount of money you'll need to start your business will depend largely on the type of business you're in.

For example, if you have to rent storage space, you'll typically need money for a security deposit and possibly up to three months of rent plus equipment, furniture and communications set-ups, including fax, phone and computer. You'll have utility bills, too. If you're in a retail business, you'll need to figure out how much inventory you'll need on hand.

And for any company, of course, you'll have salary expenses, marketing expenses and other costs of doing business, ranging from insurance to transportation (you might need a van or truck) to garbage collection. In making these calculations, you may want to be conservative, assuming that some costs may go up and there are likely to be circumstances that you didn't anticipate.

One rule of thumb is that when you start a business you should have enough cash on hand to operate it for a year. And you should have enough to pay yourself a salary. If you don't have income from your business, you won't be able to pay your personal bills.

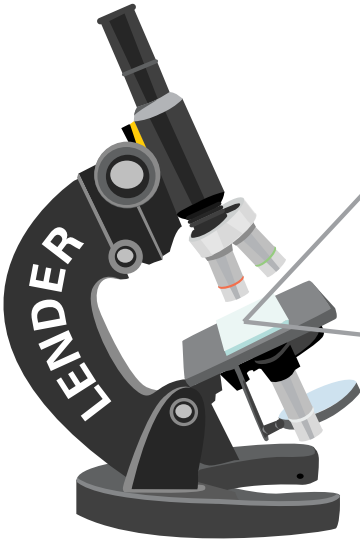
What Lenders Look For

Once you've listed your costs and determined the amount of funding you have and how much more you'll need, the next step is to prepare a presentation for potential lenders, such as a commercial bank, agency or other financial company that makes loans to small businesses.

In deciding whether or not to make a loan, lenders are assessing their risk: What is the likelihood that you will pay back what you borrowed? To make that determination, the lender will look at how much you say you need, what you are using it for, how realistic your cost and revenue estimates are and how long it will take you to repay the loan.

Information to Provide

In the case of a small business loan, the lender will normally ask you to provide collateral, or



security, in case you can't repay the loan. The collateral may be assets of the company, like equipment you purchase. But a lender might also ask for a guarantee that pledges your personal assets, including your savings and investment accounts and any real estate you own, such as your home, as collateral. Lenders also want to know how much of your own money, or equity, you have invested in the business. They believe that the more equity you have, the more committed you are to the business, and the better chance it has of succeeding.

In reviewing a loan application, lenders will also review your personal credit history to see if you have paid off previous loans on a timely basis or ever filed for bankruptcy. They also want to know if you have owned or operated

other businesses in the past, and what happened to them. That's one reason it's so important to check your own credit report and credit score before applying for a business loan. The FACT Act allows you to get one free copy of your credit report from each of the three major credit reporting agencies once a year. To request your report, go to www.annualcreditreport.com, or call 877-322-8228. While your report is free, you'll have to pay a small fee for your actual credit score.

Sources

There are a number of sources to consider for raising capital. You might begin with the bank where you keep your personal accounts and already have a working relationship. Most banks have a special department for small business loans, and they can provide guidance on how much you can reasonably expect to borrow and how to apply.

You might also use the assets you already have as the basis for a loan. For example, you might consider taking a home equity



SBA Special Loans

Special loans are available to small businesses owned by women, minorities, ex-military personnel and other groups. Check www.sba.gov to see if you qualify for one of these loans and how to apply.

loan, which could be substantial if your house has increased in value. The risk you run, however, is that if you default on the loan because your business fails, you may lose your home as well. If you borrow the money from family or friends, be sure that you have a formal agreement in place, ideally reviewed by a lawyer, so that the repayment terms and conditions are clear to everyone.

One source you should always check for loans, and for helpful information about small businesses in general, is the Small Business Administration (SBA), and particularly its website, www.sba.gov. There you will find information about the types of loans available, who qualifies for them and the procedures for filing your loan application.

SBA Funding

In 2005, the SBA funded approximately \$19 billion in loans. During the year, the SBA gave access to capital to more than 28,000 start-up businesses, or 12,000 more than it did in 2004.

Financial Management

No matter how good your product or service, or how effective your marketing is, if you don't have good financial controls in place, your business is far less likely to succeed than one that runs its finances well. That's because you can usually project your expenses, or what you will have to pay out, but cannot always predict your revenue, or the money you have coming in.

Carefully monitoring your expenses, as you do with a household budget or personal checking account, should be one of your primary concerns as a business owner. There are software programs that can help you track and monitor your company's expenses. Because they also help keep your records organized, using a program like this can come in handy when it's time to file taxes for your business. You can ask your accountant for a recommendation and search online for small business accounting software.



Basic Banking and Credit

A bank checking account, especially one designed for small businesses, serves many purposes. It gives you a simple way to pay bills, get cash, deposit payments you receive and cash checks. This kind of account also provides basic recordkeeping, since your statement shows amounts you've paid and to whom, as well as amounts that you've deposited.

As an added benefit, you'll be able to view your account status online at any time, receive wire transfers and electronic deposits—which is important if your business accepts credit cards—and transfer funds electronically between your checking and other bank accounts, such as savings and money market.

In addition to a business bank account, you might consider getting a company credit or charge card, since it provides a convenient way to pay for supplies and services for your business, especially

if you don't have the cash on hand. What's more, you don't have to pay for the things you charge until the credit card bill comes due, so you can use your cash for other things in the meantime. Further, keeping your business expenses on a business credit card can assist in tax preparation, as you need to keep such expenses separate from your personal expenses.

Recordkeeping

Good recordkeeping is the foundation of good financial management.

It probably pays to have some sort of electronic bookkeeping system, even if you use an outside bookkeeper or accountant to oversee your financial records and prepare and file your tax returns. That's because the accountant or bookkeeper will depend upon the records you provide and a software package can help you keep and organize the information you need.



While an accountant may seem like a luxury if your business has limited cash available, remember that a professional can often help you save money by identifying specific tax breaks you may qualify for. An accountant can also provide an outside, objective perspective that can guide you in making key financial decisions, such as whether you should lease or buy a piece of equipment.

Financial Reports

You might think of financial reports as a series of X-rays or scans that look at your business from different perspectives. While larger companies may produce dozens or even hundreds of reports, there are just a few really critical ones that any business needs.

Balance sheet: A company's balance sheet shows its assets, liabilities and equity at a specific point in time.

- Company assets include cash on hand and accounts receivable, or amounts you are owed from customers, as well as fixed assets, like equipment, less the depreciation or costs you write off against revenue you earned from using the equipment.



- Company liabilities include accounts payable or amounts you owe to vendors, loans from your bank, as well as any taxes that are due.
- The company's equity is the amount of your own money you put in plus all profits the company made over time.

A balance sheet is a bit like a financial health report. If your liabilities are greater than your assets, or you have negative equity, the business's financial health is probably poor. But if you have little debt compared to your assets and you own most of those assets, the business is probably in good financial health. However, the balance sheet is only part of the story.

Income Statement: Your income statement, which is commonly known as your profit and loss statement, shows how well your company is doing, and, specifically, whether your business

is making a profit. The statement reports how your company makes and spends money, shows your total sales or revenue, costs of sales, gross profit, other expenses and net income for a period of time. Your **gross profit** is the total amount of your sales minus your direct costs in terms of labor, supplies and other expenses to generate those sales, while your **net profit** is your gross profit minus all the other expenses of running the company, such as rent, advertising, interest or income taxes.

Cash Flow: Almost any small



business owner will tell you that the number-one concern, day in and day out, is cash flow, or ensuring that there is enough money in the bank to meet expenses, and ideally, money left over as a profit. Even companies that are profitable may have cash flow problems, since you may need to purchase inventories or supplies, pay employ-



ees and keep loans current before you receive payments owed by your customers.

You can help to improve your cash flow situation by collecting payments due into the company as quickly as possible, and extending payments you owe as long as you reasonably can without incurring late charges or hurting your credit rating.

Cash Flow Forecast: This report should be the lifeline of your company. It is a history of the cash you've received as well as a forecast of your cash needs for at least the next three months. Preparing this report will help you predict how much cash you have in reserve, when you can purchase new equipment and manage repayment to lenders or yourself. It will



also help you recognize a potential shortfall and the need to borrow money or put your own cash into the company. By reviewing your actual sources and uses of cash over a period of time, you'll be better able to predict the future.

Sound Billing Practices

One way to get money you are owed on a timely basis is to accept cash or credit card payments where possible, since you can bank this money very quickly, even if you have to pay the credit card company or network (such as MasterCard, VISA, Discover and American Express) a small percentage on the credit card receipts. Once you send an invoice to a customer, be prepared to wait 15, 30 or even 45 days or longer to get your cash. To reduce this time, you may want to offer a discount if the bill is paid before a certain time, like 2% if paid within 10 days of the invoice date. You may sometimes see this described as "2/10, net 30," which means you can take a 2% discount if the bill is paid in full within 10 days, otherwise the full bill is due within 30 days.

To reduce payment delays, especially for long-term or recur-

ring services, you may want to ask for an initial payment up front, and a series of installments as you go along. Remember to send your bills out promptly. The longer it takes your customers to receive their bills, the longer it may take you to get the payments.

If you perform a service on a regular basis, be sure you get paid on a regular basis—say, weekly, every two weeks or monthly—so customers don't get too far behind in their payments. A stream of income on a regular basis can dramatically improve your cash flow situation.



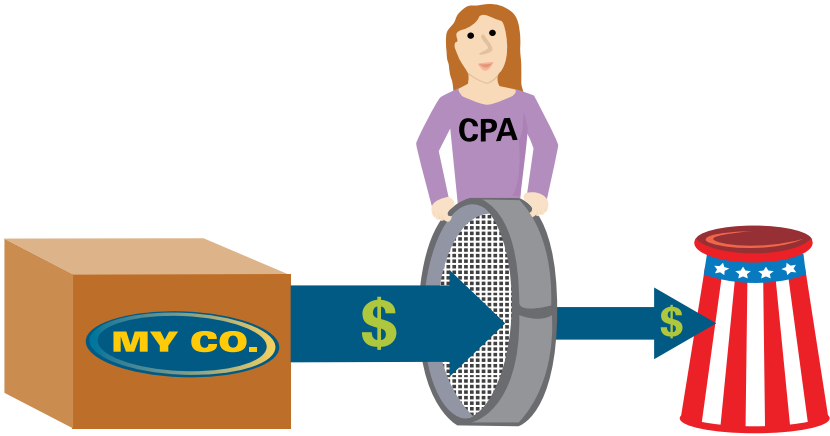
Cash Float

On the flip side, you want to find ways to stretch out your payments as much as possible. In many cases, you can reasonably delay paying some bills—such as inventory or supplies—for up to 30 days, depending on the agreement you have with your supplier. However, if your cash situation is strong and you qualify for a discount by paying up front, you can often realize a savings by paying early.

And if you charge certain expenses on a credit card, you won't have to pay until the payment due date. Let's say that your credit card statement closes on the 15th of the month, and payment is due on the 6th of the following month. So, for example, if you charge supplies on your card on April 17th, after the closing date, the payment for those supplies won't come due until June 6, giving you a float of more than six weeks. Of course, you need to be careful to stay within your line of credit, and avoid charges that you can't pay off when they're due since that could result in finance charges.

Taxes

Your small business is not only a potential source of revenue for you—it's also one for Uncle Sam and the local taxing authorities. There are fairly strict filing requirements for registering your business, getting a tax identification number and preparing a number of tax documents in the course of the year. Failing to file these forms on time and paying any amounts due can lead to difficulties with the IRS and other agencies, and can be a costly hassle to resolve.



Preparing and planning for taxes is one area where it pays to get professional help, since tax laws and regulations can be complicated. And since your company’s taxes may also affect your personal income tax, depending on the type of company you have, it may be best to work with a Certified Pub-

lic Accountant or other tax professional when it comes to taxes.

Filing the Right Forms

Your accountant will identify the different agencies you have to file with, and will know the different forms you have to file and when they are due. He or she can also show you the kind of records you’ll need to keep, and help you set up a system for keeping them. The cost of paying an accountant can more than offset the larger cost and aggravation of ongoing tax problems.

One decision you’ll have to make is what your company’s tax year will be. While you pay personal income taxes based on a calendar year, some businesses select another 12-month period, such as July 1 through June 30. Your accountant or tax adviser can explain the advantages and drawbacks of your options.

Employer Identification Number

When you pay taxes as an individual, you use your Social Security number as your taxpayer identification number, which tells the IRS who you are. But when your business pays taxes, it uses an **employer identification number**, or EIN—sometimes called a federal tax identification number. You apply for an EIN when you start your business.

Conclusion

Whether your small business is already a going concern or a dream you are working to turn into reality, you can benefit from the expertise and experience of others who have taken this path. And you are in good company. More than 70% of all businesses in the United States are small businesses.

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