

# **AN INTERPRENEUR'S JOURNEY**

**The Birth of a  
*New Economy Business***

Tom Eckmann



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### **The Birth of a *New Economy* Business**

by Tom Eckmann

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## 1 — Partridge Radiant Heating *... a better way to heat your home*

Bill shifted his position in the chair and looked around the lobby. Aside from the receptionist who he could barely see over the tall counter, he was alone. He scanned the room and noted the almost perfect coordination of neutral tones—off-white walls, off-white ceiling, creamy beige carpet, wood laminate table, light tan sofa and matching side chair. The only elements of color were an unremarkable landscape on the wall behind the sofa and a brochure lying on the table, emblazoned with the logo of Mount Baker Bank. He picked up the brochure and thumbed through the pages. The back cover listed their services, including “SBA-guaranteed loans.” That’s why he was here. He had a two o’clock meeting with Art Jones, Assistant Vice President of Mount Baker Bank, the man who handled their SBA loans.

Bill had arrived ten minutes early. He was unfamiliar with the building and didn’t want to be late. The receptionist had politely told him she would let Mr. Jones know he was here. That was fifteen minutes earlier.

He had scheduled the meeting a week ago, when he had dropped off his application at the branch office. Since then, he’d been going over in his mind the questions Mr. Jones might ask, and rehearsing his answers. Bill badly needed this loan. His credit cards were maxed out, his home was mortgaged to the hilt, and his savings were going fast. He had even borrowed money from his parents. Yet here he was, desperately in need of even more money to keep his business afloat.

The bank where he had his commercial account had already turned him down. They said he was carrying too much debt and the business wasn’t showing a profit. Not able to

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take no for an answer, he had gone to several other banks; but after glancing at his financials, they politely told him the same thing.

His accountant suggested he look into the Small Business Administration and their loan guarantee program. This program enabled banks to loan money to struggling businesses that might not otherwise qualify. "Struggling" certainly described him! With such a guarantee, he couldn't imagine why the bank wouldn't loan him the \$50,000 he needed. After all, his business had great potential. The only thing needed to unleash it was a little working capital.

A small group of people came through the lobby door, interrupting his thoughts. They disappeared into the sea of cubicles in a large room behind the reception desk. Bill noticed how even the people who worked there matched the office decor, dressing in muted tones.

He looked at his watch. It was now 2:10. Where *is* this guy, he wondered.

A wave of anxiety rushed through him. Would this bank really be different from the others? Was an organization as conservative as this likely to loan money to a fledgling business, even with a government guarantee?

Bill glanced down at the arms of his chair. He had been rubbing his thumbs up and down the seams and now he noticed how frayed they were. It was obvious he wasn't the first to sit there waiting for an audience with a loan officer. He moved his hands to his lap and shifted his position.

He *had* to get this loan. Then he could hire new sales people and get sales ramped up. As soon as he hit ten systems per month, he could start buying his materials directly from the manufacturers. He would be able to eliminate the distributors and their twenty percent markup. Then the business would start making a profit, and he could stop



writing personal checks to the company every month to cover expenses. He could also start taking home a real paycheck. Life would be a lot better, both at work and at home.

He thought about his wife. Olivia had been great this past year, a real trooper. Despite the long hours and financial hardships, she was still his biggest fan and most loyal supporter, and in more ways than one. Since starting the business, her salary had been their only income. As a customer service manager at Fargo Insurance, she was well paid and was able to purchase medical insurance to cover the entire family. But her salary wasn't enough. With a mortgage, credit card payments, and day-to-day living expenses for them and their two teenage kids, they had to dip into savings each month to make ends meet.

With demands from both home and the business, their savings were going fast. They would be able to get by for a couple more months, but then they'd have to start draining their 401(k) accounts. Those would carry them a few months more, but once they were gone, their only option would be to sell their home, and cash out their last bit of equity.

The thing that frustrated Bill the most was that they were so close to success. He had been at this for over a year and had learned a great deal. Sure, he'd made mistakes, but that was part of being an entrepreneur. Now he understood the business and knew exactly what he had to do to turn it around. He just needed this loan to do it.

Bill looked at his watch again. It was now 2:15. So much for his 2:00 appointment. He glanced over toward the receptionist who seemed to have forgotten he was there. He caught her eye and she hurriedly picked up the phone and dialed a number. Bill grumbled under his breath, wondering what was taking so long.

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He continued to fidget in the chair. He wanted to get this over with and get back to work. Lately, with so much time spent looking for money, he had been neglecting his sales duties. And he loved spending time with customers. They understood and valued what he was doing. They knew he was the only one who could put radiant heating into their homes at a price they could afford.

It was a lot more fun talking to them than it was talking to bankers who knew nothing about starting or running a business. Sure, these guys understood financials and what a company looked like on paper, but they'd never been in the trenches dealing with real-life business problems. They didn't know what it was like to jump up in the middle of a family dinner and run across town to pick up a customer's check so that you could make payroll, or pay the rent. They didn't know what it was like to open an envelope and find that a customer who owes you \$10,000 has just filed for bankruptcy and now you're not going to see a penny of it. No, they didn't have any appreciation of what it took to get a business going or move it along as he had, or how frustrating it was to see success so close but have it remain just outside your grasp.

Bill shifted in his chair and again glanced at his watch. Two-twenty. Now he was getting really annoyed. Just then, a balding middle-aged man emerged from the sea of cubicles and walked toward him. He wore a light brown sport coat, tan trousers, a white shirt and nondescript tie, and he was carrying a thick file folder. A beige folder, of course.

Bill avoided eye contact just in case he wasn't the right guy. But the man walked up to him, extended his hand and introduced himself. "Mr. Partridge, I'm Art Jones. I'm an Assistant VP with the bank and handle all the SBA loan applications. Let's meet in here."

He ushered Bill into a small conference room, which was really just an extension of the lobby. It had the same color scheme, and the furnishings were about as sparse—a small conference table, four uninviting chairs, and a cheap print on the wall. Bill got the impression they didn't want you to get too comfortable, or linger too long.

Jones motioned Bill to a chair and then sat across from him. He opened the file, labeled "Partridge Radiant Heating," containing Bill's loan application and supporting documents. The stack of papers was nearly an inch thick, and Bill recalled how much time he had spent pulling it together. The information needed by the SBA wasn't too different from that requested by the first bank he had approached. But of course this was the Federal government, and they insisted on having everything submitted on *their* forms. So Bill had laboriously reworked his information, making sure everything got copied into the right place on the correct form. It wasn't the kind of thing he liked to do.

Jones apologized for running late and then got right to it. "Mr. Partridge, could you please describe your business and why you want a loan?"

Bill was a little surprised by the question. He hadn't rehearsed an answer to this one because it was all right there on the form in Art's hand. He wondered, maybe it's a test! Maybe they want to see if I can remember what I wrote on the application!

Then something else occurred to him—maybe this guy hadn't read his application! No, Bill thought, this guy had to have read it! He was probably just busy and needed to have his memory refreshed.

Bill decided to give Art the benefit of the doubt, and use this as an opportunity to tell his story. He loved telling it, and people seemed to enjoy hearing it. They should: it

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was a great story! He was sure Art would like it too, and decided to give him the feature-length version.

“I was first exposed to the building trades as a child,” Bill began. “My dad and uncle owned a general contracting business and I helped them out after school and during summer vacations. My dad went to work for another company, but I continued to work part-time for my Uncle Charlie during high school and college. Then, after graduating from Cascade Community College, I went to work for him full-time. We specialized in HVAC contracting and did both residential and commercial projects. I handled sales and administration, and Uncle Charlie supervised the work.

“After a few years I decided I needed a bigger challenge, so I accepted a sales position with Templeton Building Supply. At that time, they were one of the region’s leading distributors of plumbing materials and HVAC parts. I established a group that worked directly with architects and helped them select materials for their projects. We were pretty successful and generated a lot of sales for the company.

“In both of those jobs I had a chance to work on projects involving the installation of radiant heating systems, usually in high-end homes. I saw how well these systems worked and was amazed by their low cost of operation. But I was equally amazed at how much they cost to install—usually two to three times more than forced-air or electric heating. Most people couldn’t afford them. This bothered me; I figured a lot more people would use radiant heating if it were more affordable. So I decided to see if there was a way to reduce the cost of these systems.”

Bill tried to maintain eye contact with the banker as he talked. He was only occasionally successful because Art was often staring at his shoes. But when Bill could catch his eye, Art would nod his head appreciatively.

“Over the years, I did a lot of research. I worked with several engineers to learn the theory of radiant heating and how to use it in a home heating system. I identified the key system components and found out who made them and how much they cost. I talked to contractors to see how they went about designing and installing their systems, and I learned about the kinds of problems they encountered. Finally, I talked to people who already had radiant systems to see what they liked and disliked about them. It didn’t take long for me to develop a pretty good understanding of why people liked radiant heating and why the systems were so expensive.

“The reasons for the high cost were actually pretty simple. First, since so few people buy radiant systems, installers couldn’t get good pricing on their materials. Second, also because of the low sales volume, no one took the time to standardize the design or streamline the installation process. Finally, the contractors who did most of this work were plumbers and they paid their workers \$35 to \$40 per hour. All of these things contributed to the high cost of a system, but it became obvious to me that much of the cost was unnecessary. By doing things differently, I could sell these systems for a lot less. I would standardize the design; purchase materials directly from manufacturers; tool-up for assembly and installation; and employ less expensive installers. I believed that if I really worked at it, I could sell a radiant system for about the same price as forced-air. Then, everyone could afford one!”

Bill was on a roll. He knew this was a great business story. No one could help getting caught up in the passion and excitement that crackled in his every word. He took a breath to continue when he glanced over at Art, and froze. The man’s eyes were glazed over, and he was stifling a yawn!

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All Bill could think of was, what a jerk! Here I am, telling this phenomenal story, and this guy is falling asleep!

He decided his next point needed to be told with more gusto. He took a deep breath, raised his fist from the table, and said, "That's when I realized—there *must* be a business opportunity here!"

Coinciding with the word "must," Bill's fist slammed the table. Art was jolted back to full consciousness and rejoined the meeting. He knew he had been busted and smiled meekly. He motioned Bill to continue.

Satisfied that Art was again paying attention, Bill went on. "I got so excited about the opportunity, I decided to quit my job and go into the radiant heating business. That is, until I told my wife. I gave her my best sales pitch, but when I was done she quietly asked, 'What in world could you possibly be thinking?' She reminded me that I had a good job and a future at Templeton Supply. She reminded me that I had a family to support. She wasn't working at the time, and she wanted to know how we would pay the bills while I was off on this new adventure. It didn't take me long to realize that she wasn't too keen on my idea.

"One of the things I love most about my wife is the way she communicates. She never raises her voice, but she also never leaves any doubt as to where she stands. I realized I was outgunned in this conversation and that a full-blown retreat was in order. When I could finally get a word in, I threw myself on the mercy of the court. I told her she was right, it was a harebrained idea, and I'd never bring it up again.

"And that was it. I was cured of 'radiant fever.' I vowed to put the idea on the shelf and go back to being the best sales manager that Templeton Supply had ever seen. And that's what I did for the next six years.

“Then last year, the economy dipped and the building industry got clobbered. Business declined and Templeton’s financial position along with it. Long story short, I was laid off.

“I spent a couple of months looking for another job, but found the pickings to be pretty slim. I realized if I wanted to stay in construction, I might have to relocate to California or somewhere else where the economy was stronger. But I didn’t want to do that, nor did I want to look for a job outside of construction. Just when things were getting bleak, I remembered my idea for radiant heating. It occurred to me this just might be the time to dust off those plans and start that new company.

“I dug out my notes and took a fresh look at the idea. All of the conditions still existed and my findings were still valid. More importantly, no one else had recognized or pursued the opportunity. I realized this was something I could get excited about. It sure beat sitting around waiting for the phone to ring.

“I tracked down a friend of mine who was a design engineer at Templeton. He had also been laid off, and he was happy to help me with the design of a standardized radiant system. Then, I rented some shop space, printed a brochure, and started looking for customers. Within thirty days I’d sold my first system. Now, a year later, we’re averaging five to six system sales per month and I have one full-time employee, one part-time, and several contractors who help with installations.

“But getting the business going has been a real struggle financially. My wife and I have invested nearly \$95,000 and we need about \$50,000 more to get the business firmly on its feet. I want to hire two salespeople so I can double sales in the next six to eight months. Then I can start buying materials

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directly from manufacturers and save at least twenty percent. With these savings, the business will become profitable. I'll use the profits to pay back the loan and further expand the business. My goal is to eventually take the company national and make radiant the number one choice for home heating systems!"

There it was—the story of Partridge Radiant Heating. He glanced at Jones, halfway expecting him to break out in applause. One look told him that wasn't going to happen. Jones was awake, but that was about the best he could hope for.

Jones, realizing that Bill was finally done, straightened up in his chair and thanked him. He picked up the pile of documents in front of him and started flipping randomly through the pages.

Bill thought it a little curious that Art hadn't asked any questions or taken any notes during his talk. Maybe he *had* read his application and knew everything was already included in the package. That was a possibility because Bill couldn't think of anything he had left out.

The SBA application was only seven pages long, and most of that was legal jargon required by the government. What took so much time was preparing the dozens of supporting documents that had to go with it—personal history forms for the owner, personal financial statements, business financials for the past three years (even though his business was only a year old), income and expense projections for the coming year, three years of business and personal tax returns, a written history of the business, a copy of his business license, shop and equipment leases, and on and on.

While he was putting the material together it had occurred to Bill that the real purpose of the application might



simply be to test your endurance. You *really* had to want a loan to go through all this!

He watched Art shuffle through the file, seeming to ignore most of it. Then one of the pages caught the banker’s eye. It was Bill’s Profit and Loss Statement for his first year in business. This page didn’t look too good, and Bill knew it. The company had lost a lot of money.

But in Bill’s mind, the loss shouldn’t come as a big surprise. The company was just getting started, and it wasn’t reasonable to expect them to make money. He’d had to spend quite a bit to get his shop set up and launch his sales and marketing programs. He’d also had to buy materials from distributors instead of manufacturers, which had really hurt his margins. But now he knew how to fix this. All he needed was the loan.

**Partridge Radiant Heating**  
**Income Statement Year 1 Actuals (\$000)**

Sales (35 units)	\$260.0
Cost of Goods	<u>207.1</u>
Gross Profit	\$ 52.9 (20%)
Operating Expenses	
Payroll	\$ 37.3
General & Admin.	54.4
Sales & Marketing	18.2
Debt Service	<u>9.9</u>
Total Expenses	\$119.8
Pretax Profit/(Loss)	(\$66.9)

Art looked over at Bill and said, “Your business lost quite a bit of money last year.”

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Bill nodded, and the banker looked back down at the statement. After a moment he asked, "Do these payroll expenses include a salary for you?"

Bill responded, "Well, yes and no. The expenses do include a salary for me of \$2,100 per month. That's the minimum I need each month to cover expenses at home. Unfortunately, the company didn't make enough money to pay that, so it came out of my savings. I included it in the P&L because my accountant said I needed to provide a realistic picture of the business' profitability."

Art replied, "She's right." He returned to his scrutiny of the P&L. Then he said, "Something that jumps out at me is your gross profit margin. Why is it so low?"

Bill expected this question. "Yes, I know it's low. The reason is we were unable to buy our materials direct from the manufacturers. That was a major setback. You see, direct buying is one of the reasons we are able to sell our systems for less; we cut out the distributors and save about twenty percent. But when I tried to order from the manufacturers, they said I had to buy at least their minimum order quantities. These minimums were more than I needed, and a lot more than I could afford. So I ended up buying from local distributors and paying the markup."

Anticipating the next question, Bill went ahead and answered it. "At that point, I considered raising prices but found myself caught in a chicken and egg situation. My business strategy is based on making radiant heating affordable by selling in volume. By affordable I mean selling radiant heating systems for the same price as forced air. So if I raised prices to offset my additional costs, my systems would be less affordable and it would take a lot longer to build volume. The alternative was to hold the price down and absorb the additional costs; then I could build volume

more quickly and start buying direct. I felt the second alternative was the better way to go. As you can see, we sold quite a few systems last year, 35 to be exact. I attribute our sales growth to keeping our price low.

“The solution to the margin problem is higher sales. We need to sell at least ten systems per month before I can buy direct. That’s why I need to hire two additional salespeople. With their help, we should be there in about seven months. Then our profit margin will go up significantly.”

The logic made perfect sense to Bill, but once again, he couldn’t tell what Art thought. His face remained expressionless as he flipped through the pages. When he got to Bill’s financial projections for the next two years, he stopped. He studied the numbers for a moment and then said, “I see you’re planning some pretty aggressive sales growth. In the coming year, you expect to more than triple your sales. Have you thought about how you’re going to do that and who’s going to install them?”

**Partridge Radiant Heating**  
**Income Statement Projections (000s)**

	<u>Year 2</u>	<u>Year 3</u>
Sales	\$848	\$1,470
<i>Units</i>	(113)	(196)
Cost of Goods	<u>627</u>	<u>1,041</u>
Gross Profit	\$221	\$429
<i>Gross Margin</i>	26%	29%
Operating Expenses		
Payroll	\$ 126	\$196
General & Admin.	51	57
Sales & Marketing	47	74
Debt Service	<u>21</u>	<u>21</u>
Total Expenses	\$245	\$347
Pretax Profit/(Loss)	(\$24)	\$82

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The question surprised Bill. After all, that was the essence of his entire business plan. Maybe his first impression was right—this guy *hadn't* read the plan. But rather than get into the question of whether he had or hadn't, Bill decided to use this as another opportunity to sell its merits.

“Over the past year I've personally handled everything in sales and marketing,” he said. “This has given me a chance to develop a good understanding of the sales process and how to generate leads. As I've described in the business plan, I intend to hire two additional sales reps to work with me. With their help we can cover more ground and pursue opportunities that I just haven't had time to go after. My projections are based on some conservative assumptions as to how fast these sales people will come up to speed. I'm also going to continue to spend all of my time in sales. So, between the three of us, I don't think we'll have any trouble hitting that number.

“As far as installations go, I have an excellent operations manager, a fellow by the name of Tom Clark, who handles assembly of the systems and supervises installation. He's done a great job over the past year. He hires contract labor to do the actual installation work. With the methods Tom and I have developed, our installers don't need a high level of skill. We can hire new people and have them up to speed within a matter of days.

“At the present time, we're installing five or six systems each month. Our plan calls for us to be at thirteen by the end of the year, so we need to double, not triple, our installation rate. With the systems and procedures now in place, I don't think we're going to have any problems here either.”

Bill strained to read Art's face but with no luck. His expression seemed to be fixed regardless of what Bill said or did. He couldn't tell if Art was “wowed” or simply didn't get it.

Art shuffled through the package to find the backup spreadsheets for Bill's P&L projections. These statements broke the annual sales and expense figures into monthly projections. He stared at these for a few moments, and then Bill thought he heard a sigh.

Art slowly straightened the papers and set the file down on the table. He looked at his shoes for a few seconds, apparently deep in thought.

Bill just sat there, not knowing what else to say or do. Finally, Art looked up at him.

"Mr. Partridge, I'm afraid we can't approve your loan application."

Bill was stunned. He didn't think he heard him correctly. He muttered, "What? I ... I don't understand."

Art sighed louder this time. "Bill, I just can't make the numbers work. You lost a good deal of money last year and based on your projections, you'll continue to lose money for at least another seven or eight months. Your margins are low, I think too low to sustain your business. Your whole plan seems to hinge on increasing sales, on the order of two to three hundred percent. That's a very high rate of growth, and it's very difficult to achieve.

"But let's assume you do. Let's assume everything goes right and you sell ... what? 113 systems this year and 196 the following? Even so, when I look at your net profit at the end of the second year, it's only six percent of sales. That's low, especially for a business that expects to grow as fast as you do. There's virtually no room for error. If you miss your sales target by even a little, there won't be enough cash for working capital, or more importantly to us, enough to make your payments on a loan.

"Bill, the bank's criteria for loaning money is simple: can the applicant pay back the principal with interest? We

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look at the company's operating history and financial projections to make sure the business can generate enough cash flow to cover operating expenses and make payments on the loan. We also make sure there is a comfortable margin for error, in case the company runs into problems or misses its sales projections. When I look at your financial performance to date, and your future projections, I see little in profits and virtually no margin for error. I think you need to take a close look at your business model and see what you can do to improve profitability. You either need to raise your prices or reduce your costs."

Bill muttered, "I think my sales projections are conservative and I'm sure we'll sell a lot more than I show on paper. We'll have plenty of cash to make payments on the loan. Besides, as I said in my application, I'll put my house up as collateral. With that and the government guarantee, this loan is virtually risk-free to the bank!"

Art continued to stare at his shoes. "Bill, we appreciate that you're willing to put your house at risk to fund your business. But I'm afraid that's not the point. When the bank loans money, it expects to be paid back. The equity in your home may serve as collateral, but that's only to protect the bank in what should be the very unlikely event of a default. We're not in the business of seizing homes. If we think there's even a small chance you won't be able to pay, the bank won't make the loan in the first place.

"The government guarantee isn't an answer either. On a loan of this amount, the SBA only guarantees 75 percent. That means the bank is at risk for the difference. Also, when we call in a guarantee from the government, it counts against us when the SBA reviews our loan program. If we get too many defaults, they won't renew our certification to make these loans.

“You could always sell your house and invest the equity in your business. But I wouldn’t recommend you do that either. Right now, your business financials just don’t pencil out. You don’t make enough money to fund the business today, and it’s not clear from your plan how a loan will do anything to help that in the future. You may increase sales, but unless you also increase your profit on each sale, your company will always be short of cash.

“Now, I’ve probably already said more than I should. We generally don’t give business advice. I’d like to thank you for considering us, and wish you well. If you’d like to reapply at a later date, when your business is on a little firmer financial ground, we’d be happy to reconsider your application.”

With that Art pushed back from the table, picked up the folder and walked out of the room.

Bill sat there in stunned silence. Now what would he do?

Slowly he rose from the chair, and trudged into the lobby. He put his hand in his pocket and felt the parking stub from the building garage. He walked over the receptionist.

“Do you validate parking?”

“No sir, I’m afraid we don’t.”

Bill snorted in disgust. Great, he thought. Not only didn’t I get the loan, it’s going to cost me ten bucks to get out of the garage!

## An Interpreneur's Journey



## Business Start-up Guide

*This guide is designed for people who aspire to start an interpreneurial or any other kind of business. It outlines important steps to follow and offers general advice about what to do and how to do it. Due to limited space, this guide contains only a summary of each topic. For a more complete start-up guide, please visit the New Interpreneur website ([www.NewInterpreneur.com](http://www.NewInterpreneur.com)).*

### **1. Learning and Using the Internet**

- √ A few short years ago, hardly anyone had heard of the Internet. It was the domain of academicians, researchers and computer nerds. Now the Internet is used by millions of people and is an integral part of their business and personal lives. If you are an aspiring interpreneur, you should develop a good understanding of the Internet and how it works.
- √ The Internet is a powerful research tool and a channel for commerce. As a research tool, you can use it to explore markets, locate suppliers and vendors, investigate competitors, and find lots of other information. As a sales channel, you can use it to reach and transact business with customers literally all around the world. By understanding and leveraging this power, you gain a major advantage over less web-savvy competitors.

Tip for New Interpreneurs: For a good primer on how the Internet works, visit the website “How Stuff Works” ([www.HowStuffWorks.com](http://www.HowStuffWorks.com)) which covers everything from email to search engines to web servers.