

FINANCIALS & BUSINESS PLANNING GUIDELINES

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As coaches for The New Enterprise Forum, we usually see Financials as an important part of a start-up's presentation to investors. Too frequently, these Financials are a single-layered spreadsheet based upon assumptions, with forecasts, simply derived from percentages of totals or year-on-year percentages. And when investors ask questions about the Financials, the discussion becomes one of supporting these percentages rather than talking about the business basis for the numbers. As a result, the investor's confidence in the numbers and, more importantly, the founders' understanding of their business are dashed.

The solution to this problem is to ensure that Financials are based upon the supporting plans that drive the business. The most critical of these supporting plans are: 1) Revenue, 2) Hiring & Payroll (the largest component of G&A), 3) Product Development (and R&D), 4) Sales & Marketing, and 5) The Milestones that bring plans together. Let's take a look at how these supporting plans look and how they are used to 'add up' to the Financial Plan.

THE REVENUE PLAN:

A Revenue Plan should look something like this:

Note that this Sales & Revenue Plan has its own assumptions and generates annual totals that are carried forward into the Financial Plan. Like other supporting plans, this Plan may/should be developed on a monthly basis for the first 2-3 years and needs to be reconciled with other supporting plans and business/investor milestones. Other characteristics of the Sales & Revenue Plan:

- The Plan is based upon unit sales expanded into revenue based upon both growth and pricing assumptions. In some industries, it is also important to include potential 'churn' – e.g., the number of subscription customers who let their subscription lapse.
- The Plan is separated into strategic and tactical market segments that are consistent with go-to-market plans.
- If possible, COGS should also be separated by market segments so that product line analysis can be performed.

	Sales & Revenue					
	YR1	YR2	YR3	YR4	YR5	
Revenue						
Beachhead - No. of Units	0	0	0	0	0	
Churn - No. of Units	0	0	0	0	0	
Net Units	0	To Financial Projections				
Price Per Unit	\$0	\$0	\$0	\$0	\$0	
Beachhead Revenue	\$0	\$0	\$0	\$0	\$0	
Growth Segment - No. of Units	0	0	0	0	0	
Churn - No. of Units	0	0	0	0	0	
Net Units	0	To Financial Projections				
Price Per Unit	\$0	\$0	\$0	\$0	\$0	
Growth Segment Revenue	\$0	\$0	\$0	\$0	\$0	
Total Revenue	\$0	To Financial Projections				\$0
Cost of Goods Sold						
Direct Commissions	\$0	\$0	\$0	\$0	\$0	
Production Costs	\$0	\$0	\$0	\$0	\$0	
Material Costs	\$0	\$0	\$0	\$0	\$0	
Incremental Services / Expenses	\$0	\$0	\$0	\$0	\$0	
Etc.	\$0	\$0	\$0	\$0	\$0	
Total COGS	\$0	To Financial Projections				\$0
Gross Margin	\$0	\$0	\$0	\$0	\$0	
GM%	0%	0%	0%	0%	0%	

THE HIRING & PAYROLL PLAN:

A Hiring & Payroll Plan should look something like this:

Name	Position	Annual Salary	Area	Yr 1 Pct.	Yr 2 Pct.	Yr 3 Pct.	Yr 4 Pct.	Yr 5 Pct.	Year 1		Year 2		Year 3		Year 4		Year 5	
									No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
TBD	President	\$140,000	G&A	100%	100%	100%	100%	100%	0	\$0	0	\$0	1	\$140,000	1	\$140,000	1	\$140,000
Co-Founder 1	COO/CFO	\$120,000	G&A	25%	50%	100%	100%	100%	1	\$30,000	1	\$60,000	1	\$120,000	1	\$120,000	1	\$120,000
TBD	Accounting/Bookkpg.	\$40,000	G&A	100%	100%	100%	100%	100%	0	\$0	0.25	\$10,000	1	\$40,000	1	\$40,000	1	\$40,000
Total G&A									1	\$30,000	1.25	\$70,000	3	\$300,000	3	\$300,000	3	\$300,000
Founder	Founder & CEO	\$140,000	Pdct.	50%	75%	100%	100%	100%	1	\$70,000	1	\$105,000	1	\$140,000	1	\$140,000	1	\$140,000
Co-Founder 2	CIO/CTO	\$120,000	Pdct.	25%	50%	100%	100%	100%	1	\$30,000	1	\$60,000	1	\$120,000	1	\$120,000	1	\$120,000
TBD	Project/Technical Mgr.	\$100,000	Pdct.	100%	100%	100%	100%	100%	0	\$0	1	\$100,000	1	\$100,000	1	\$100,000	1	\$100,000
TBD	Product Dev. Mgr	\$100,000	Pdct.	100%	100%	100%	100%	100%	0	\$0	0	\$0	1	\$100,000	1	\$100,000	1	\$100,000
TBD	Programmers	\$80,000	Pdct.	100%	100%	100%	100%	100%	1	\$80,000	1	\$80,000	3	\$240,000	6	\$480,000	12	\$960,000
TBD	Quality & Support	\$60,000	Pdct.	100%	100%	100%	100%	100%	0	\$0	0	\$0	1	\$60,000	1	\$60,000	2	\$120,000
Total Pdct. Dev.									3	\$180,000	4	\$345,000	8	\$760,000	11	\$1,000,000	18	\$1,540,000
Co-Founder 3	CMO	\$120,000	S&M	25%	50%	100%	100%	100%	1	\$30,000	1	\$60,000	1	\$120,000	1	\$120,000	1	\$120,000
TBD	VP mktg/Biz Dev.	\$100,000	S&M	100%	100%	100%	100%	100%	0	\$0	1	\$100,000	1	\$100,000	1	\$100,000	1	\$100,000
TBD	Sales Eng'r/Pre-Sales	\$100,000	S&M	100%	100%	100%	100%	100%	0	\$0	0	\$0	1	\$100,000	2	\$200,000	3	\$300,000
TBD	Sales Rep.	\$70,000	S&M	100%	100%	100%	100%	100%	0	\$0	0	\$0	2	\$140,000	4	\$280,000	8	\$560,000
Total Sales & Mktg									1	\$30,000	2	\$160,000	5	\$460,000	8	\$700,000	13	\$1,080,000
Total Wages									5	\$240,000	7.25	\$575,000	16	\$1,520,000	22	\$2,000,000	34	\$2,920,000
Payroll Taxes & Ins.										\$24,000		\$57,500		\$152,000		\$200,000		\$292,000
Benefits										\$60,000		\$143,750		\$380,000		\$500,000		\$730,000
Total Labor Costs										\$324,000		\$776,250		\$2,052,000		\$2,700,000		\$3,942,000

Note that this Hiring & Payroll Plan has its own assumptions and generates annual totals that are carried forward into the Financial Plan. Like other supporting plans, this Hiring & Payroll Plan may/should be developed on a monthly basis for the first 2-3 years and needs to be reconciled with other supporting plans and business/investor milestones. Other characteristics of the Hiring and Payroll Plan:

- The Hiring Plan is based upon hiring needed to perform both administration and other activities essential to delivering the results shown in other Plans.
- The Hiring Plan shows if/when people are expected to be paid less than their total salary of record. This takes into account both part time management and the intention to replace salaries with equity participation.
- The Hiring Plan shows all expected members of the organization and when they are expected to be needed. This timing needs to be consistent with other Plans, major investor milestones, and funding requirements.

THE PRODUCT DEVELOPMENT (AND R&D) PLAN:

A Product Plan should look something like this:

Note that this Product Development Plan has its own assumptions and generates annual totals that are carried forward into the Financial Plan. Like other supporting plans, this Product Development Plan may/should be developed on a monthly basis for the first 2-3 years and needs to be reconciled with other supporting plans and business/investor milestones. Other characteristics of the Product Development Plan include:

- Dollars are based upon the activities that generate the costs.
- The timing of activities must be consistent with the timeframes associated with Sales & Marketing activities, product announcements/availability to customers, and investor milestones/funding.
- Total dollars includes all Payroll related to Product Development – from the Hiring Plan.
- If possible, costs should be broken down further by specific product lines so that additional product line profitability analysis can be done as actual costs are collected.

	Product Development Plan				
	YR1	YR2	YR3	YR4	YR5
Activities					
	Prototyping/POC				
		Beachhead/MVP			
			Go-to-Market/Growth		
Prototyping/Proof of Concept	X	(X)			
Beachhead/MVP Product	(X)	X	(X)		
Go-to-Market Products		(X)	X	X	X
Product Development					
Research & Development	\$0	\$0	\$0	\$0	\$0
Prototyping	\$0	\$0	\$0	\$0	\$0
Systems / Product Development	\$0	\$0	\$0	\$0	\$0
Testing	\$0	\$0	\$0	\$0	\$0
Consulting Fees	\$0	\$0	\$0	\$0	\$0
Outsourced Services	\$0	\$0	\$0	\$0	\$0
Etc.	\$0	\$0	\$0	\$0	\$0
Product Development Payroll	\$0	From Hiring & Payroll Plan - Pdct.			\$0
Total Product Development	\$0	\$0	\$0	\$0	\$0

THE SALES & MARKETING PLAN:

A Sales & Marketing Plan should look something like this:

Note that this Sales & Marketing Plan has its own assumptions and generates annual totals that are carried forward into the Financial Plan. Like other supporting plans, this Sales & Marketing Plan may/should be developed on a monthly basis for the first 2-3 years and needs to be reconciled with other supporting plans and business/investor milestones. Other characteristics of the Sales & Marketing Plan include:

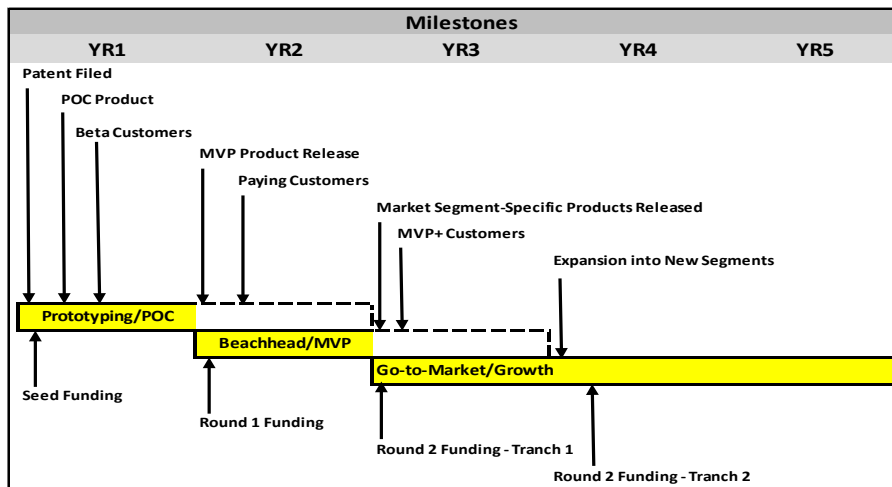
- Dollars are based upon the activities that generate the costs.
- The timing of activities must be consistent with the timeframes associated with Product Development activities, product announcements/availability to customers, and investor milestones/funding.
- Total dollars includes all Payroll related to Sales & Marketing, other than sales commissions paid, which are part of Cost of Goods Sold.
- If possible, costs should be broken down further by specific product lines so that additional product line profitability analysis can be done as actual costs are collected.

	Sales & Marketing Plan				
	YR1	YR2	YR3	YR4	YR5
Activities					
	Prototyping/POC				
		Beachhead/MVP			
			Go-to-Market/Growth		
Direct Sales & Marketing	X	(X)			
Marketing Program Development	(X)	X	(X)		
Growth Execution		(X)	X	X	X
Sales & Marketing					
Marketing Materials	\$0	\$0	\$0	\$0	\$0
Trade Shows	\$0	\$0	\$0	\$0	\$0
Advertising	\$0	\$0	\$0	\$0	\$0
Publications	\$0	\$0	\$0	\$0	\$0
Sales Travel & Expenses	\$0	\$0	\$0	\$0	\$0
Etc.	\$0	\$0	\$0	\$0	\$0
Sales & Marketing Payroll	\$0	From Hiring & Payroll Plan - S&M			\$0
Total Product Development	\$0	\$0	\$0	\$0	\$0

COORDINATING THE PLANS WITH THE 'ASK': MILESTONES

Since these supporting plans need to come together into a single, coordinated, and consolidated plan, it is frequently useful, for presentation purposes, to graphically show the relationship of the supporting plans to major funding milestones. The process that coordinates the various Plans with investor/valuation milestones is a critical process for the start-up to address as the basis for presenting to investors. As you get going on fundraising, the key milestones should be the places where you will receive an increased valuation for the business. The milestones will typically be based upon customer counts and revenue goals.

An example of how this can look is:



THE RESULTING FINANCIAL PLAN:

The resulting Financial Plan, with totals carried forward from the supporting plans, should look something like this:

	Financial Projections (\$000)				
	YR1	YR2	YR3	YR4	YR5
No. of Units - Market Segment 1	0	From Revenue Plan			0
No. of Units - Market Segment 2	0	From Revenue Plan			0
Revenue	\$0	From Revenue Plan			\$0
Cost of Goods Sold	\$0	From Revenue Plan			\$0
Sales & Marketing	\$0	From Sales & Marketing Plan			\$0
Product Development	\$0	From Product Development Plan			\$0
Operating Margin	\$0	\$0	\$0	\$0	\$0
General & Administration	\$0	From Normal G&A Planning			\$0
EBITDA	\$0	\$0	\$0	\$0	\$0

[Note: Some industries (e.g., Manufacturing) will expect to also see a row for Gross Margin.]

[Note: 'Normal G&A Planning' includes non-Product Development and non-Sales & Marketing payroll expenses.]

RESULT: AN IMPROVED DISCUSSION WITH INVESTORS:

As a result of having supporting plans feed the Financial Plan, the conversation with Investor's changes dramatically. Instead of attempting to address weakly-based assumptions within the Financial Plan itself, questions related to each line item turns to a business discussion of the Plans that are a basis for the Financials. This boosts Investor confidence in both the plans and the founders. This creates a level of understanding and credibility that is the basis for getting funded.