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Starting a Small Business in Your Retirement-
Reviewing Your Options

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There can be no question that more and more retirees are starting their own small businesses. In fact, according to a 2003 AARP survey, about 15% of baby boomers expect to own a business in retirement. Often new businesses begin out of a unique idea, hobby, opportunity, or the desire to begin a new stage in an individual's career following retirement. Sometimes the reason is financial need or simply boredom. Whatever the motivation, starting a small business can be an exciting and rewarding opportunity.

The Business Plan

In any event, however, good solid business planning is an essential first step for all would-be business owners. A business plan should include, at a minimum, a description of the business and how it will be marketed, financed and managed. A business plan is not only an essential requirement for bank financing, but even in a case where a bank will not be involved, it is the exercise by which the business owner can truly examine the feasibility of the business being profitable.

Whether or not the business owner has any prior business experience, he or she should consult and review the business plan with all available resources, including accountants, lawyers, and even friends, family or colleagues with business experience. Often the necessary objectivity comes from the outside when asking the truly difficult questions that measure the potential success of a business, such as, "Isn't the retail price too high for the market?" or "Will you be able to sustain three years without profitability?"

Which Business Model to Choose

There are essentially three primary ways to start a business, purchase and existing business, become a franchisor, or start a business from the ground upwards. Each of these models has both positive and negative considerations.

The benefit of purchasing an existing business is that the business is (hopefully) a proven business model. The existing business will have financial records showing its historical revenues, and will have employees, equipment, contracts and relationships with vendors, all of which will be transferred along with the purchase.

The downside to purchasing an existing business is that the cost is often significant and may well require a source of institutional (e.g. bank) financing. Financing through a bank would result in the requirement for the new business owner purchasing the business to make monthly financing payments to the bank, in addition to the other payment obligations of the business, and could certainly limit cash flow for some period of time.

Similar to purchasing and existing business, buying a franchise is purchasing an existing business model, with a proven track record. Purchasing a franchise allows the franchisee to purchase the right to own and operate a franchise, licensed for use by the franchisor. The franchisor often provides some level of assistance to help the franchisee with operational or other issues to attempt to ensure profitability and smooth operation.

Many franchises are lucrative and successful, (including many fast food restaurants.) That said, franchises come with a number of considerations that should be evaluated. First, franchises are generally costly to purchase. Often the franchisee must pay the franchisor an initial franchise fee, with royalty, and sometimes additional marketing fees to be paid over time. Secondly, since franchisors desire uniformity of their operations, franchisees are often subject to significant restrictions on where the business is located and how the business is operated on a day-to-day basis.

Starting a new business 'from the ground up' requires a solid, well-considered business plan, as unlike purchasing an existing business or a franchise, there is no prior roadmap by which the business owner can forecast successes and pitfalls. However, by starting a new business, the owner can enjoy 100% of the success without the payment of large debt servitude and/or franchise fees as discussed above.

Financing

Inevitably, any new business will require a source of start-up capital. Whether the purchase of an existing business, (including a franchise,) or the start of an embryonic business, some amount of initial funding will be necessary. Most new businesses have little credit and have no proven track record, and accordingly, financing from a bank is generally not an option. In addition, as discussed above, bank financing likely requires substantial monthly payments that could seriously impede the business' cash flow.

In this case, new businesses often rely on 'bootstrap financing,' which means minimal external financing. Perhaps the most frequent source of bootstrap financing is from the business owner's own financial reserves, from that of friends or family. In any such event, the business owner should ensure that the business plan provides for, and takes into consideration, the prompt return of the initial capital investment. Other ways to finance a start-up business include negotiating favorable trade credit from vendors, allowing 30, 60, or 90 days.

Once a business has demonstrated some level of success, it may be more attractive and have the cash flow to sustain some form of institutional (e.g. bank) financing, including those guarantied by the Small Business Administration, (known as SBA loans.)

Entity Formation

When starting or running a small business, the business owner must consider the type of entity, (the form of organization,) for legal and tax distinction. This consists of several types, but a couple of them are especially suited to small businesses.

In its simplest form, a business may be a *sole proprietorship*, meaning that it operates under the name of its owner. Forming a sole proprietorship requires no legal formation; it simply commences at the start of the business activities. This form of business entity, while cost effective, in that it requires no initial registration for formation, also exposes the business owner to unlimited liability relative to the operations of the business. This means that liabilities of the business will extend to the personal assets of the sole proprietor.

Conversely, unlike sole proprietorships, limited liability entities, such as a Limited Liability Company (LLC) or Corporation, afford some level of limited liability for its owners. This means that, with limited exceptions, the owner of the business will be protected from the liabilities of the business. Forming a corporation or LLC requires registration with the Secretary of the Commonwealth and should be done only after consultation with an attorney and/or accountant, to maximize both asset protection and tax planning, as different types have different tax implications.

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