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A SYSTEMS APPROACH TO WRITING AND RATING ENTREPRENEURIAL BUSINESS PLANS

This investigation provides the predicate for an intended series of studies in the field of Venture Capital deal screening. At issue is the use of theory-based standards for systematic creation and assessment of entrepreneurial business plans. A systems based approach guided synthesis of research-based principles contained in the literature. Results culminated in the formal articulation and operationalization of 10 principles in the form of a questionnaire (entitled EBPAR, for 'entrepreneurial business plan evaluation regime'). The instrument can serve dual duty as a guide for writing and a regime for rating Entrepreneurial Business Plans. Discussion focused on utility of the assessment regime and future research directions.

Introduction

This paper reports a quest to articulate a relevant assessment regime for the content quality of Entrepreneurial Business Plan. As the primary source of information for the investment screening decision, Venture Capital firms rely almost exclusively on the entrepreneurial business plan: yet virtually no academic research exists on this important tool. On average only 20-40% of the investment proposals selected by Venture Capital firms are winners. A research opportunity exists to improve the deal screening effectiveness of Venture Capital firms by examining one fundamental components of their decision making; the input. Applying an *input-process-output* model from general systems theory can provide new insight. Enhancing the *input* any procedure naturally improves the *process* and *output*; venture capital decision making should be no different. It is possible that improving the primary *decision input* used for Venture Capital deal screening will improve the *decision process* and *decision output*. The decision input could be improved by making the *writing* of entrepreneurial business plans (EBPs) more consistent; and this has the potential of improving the process and decision output of the deal screening. In other words, standardising the *content* and *format* of entrepreneurial business plans has the potential to improve the results of venture capital investment decisions. Three questions must be addressed along the journey toward standardizing EBPs: (1) At a general what are the goals of an EBP? (2) What are the fundamental principles that an Entrepreneurial Business Plan should conform to? (3) How can the principles be measured in a given Entrepreneurial Business Plan?

Definition of Key Terms

Articulating definitions for key terms describing this paper defines its boundaries. Entrepreneurship is an economic phenomenon that has existed since the beginning of society. The American Academy of Social Sciences formally admitted Entrepreneurship as a distinct discipline in 1989. Despite being steeped in history and recently recognition as a discipline, Entrepreneurship has no one widely accepted definition; these researchers use "*the pursuit of opportunity without regard to resources currently controlled*" (Stevenson 1994).

An entrepreneur who engages in entrepreneurship does not let a lack of resources inhibit the pursuit. An entrepreneur needs some sort of plan to successfully exploit an opportunity. Gaining control of financial resources during the process of entrepreneurship is necessary but not sufficient for the entrepreneur to create a new venture to exploit an opportunity; this is achieved through planning. An Entrepreneurial Business Plan is considered the primary planning document for a new venture, defined as "*the formal argument used to secure, from prospective investors, resources for a proposed entrepreneurial process*" (Hindle 1997; p.22).

The process of entrepreneurship is risky. Perspective investors for a new venture need to have an understanding and tolerance for risk. Entrepreneurs endeavouring to control financial resources often choose to seek Venture Capital: defined as "*equity or equity-linked investments in young, privately held companies*" (Lerner 2000).

Venture Capital is risk financing managed by Venture Capital firms. Entrepreneurs initially communicate their proposed venture to a Venture Capital firm by presenting an Entrepreneurial Business Plan; it is used in the deal screening stage of the Venture Capital process. Deal screening is defined as '*the initial decision process by a Venture Capital firm where many Entrepreneurial Business Plans are screened down to a few that are deemed to have high probability of success and warrant further due diligence'.*

Consistency in deal screening is self-evidently desirable. Seeking and using similar information to evaluate an Entrepreneurial Business Plan is an important step towards standardising deal screening in the Venture Capital process. Standardising is *the adoption of a consistent process leading to material improvements in practice and results; it establishes a compromise between state of the art knowledge and practical techniques* (de Vries 1999). Venture Capital firms could potentially benefit from standardizing their approach to deal screening.

Literature Review: New Ventures Require a Plan Distinct From Existing Ventures

Planning generally produces better decisions and financial results than does trial-and-error learning (Ansoff 1991). The intuitive appeal of these and similar arguments has led to the proliferation of academic and practitioner literature stressing the importance of planning, promoting models of the planning process, and offering normative advice on how to effectively design and implement strategic and operational plans. Generally, the objective of planning in business is to minimize uncertainly of future events in the pursuit of a goal.

The nature of planning is distinctly different for new venture as compared to existing ones. A critical review of the business planning literature (Pearce 1987) and a meta-analysis (Schwenk 1993), reveals that firm size and stage of development are critical factors in understanding business planning. Hindle (1997) and McGrath (1995) suggest that planning for new ventures is entirely different from planning for firms in later stages of development. These scholars argue that new ventures begin with a high ratio of assumption to knowledge and inevitably experience deviations from original targets that require fundamental redirection. Thus, new ventures must practice more 'discovery driven planning'. Applying business practices valid for a mature business can cause failure for new ventures (Block 1982; Block 1985; Kanter 1989; Block 1993; Sykes 1995). Greiner (1972) concluded that what works for a mature business will cause failure for an early stage business.

Two related themes are strongly evident in the literature; (1) Entrepreneurial business plans embrace uncertainty, and (2) they must be dynamic.

Entrepreneurial Business Plans Embrace Uncertainty

The amount of uncertainty embraced in an entrepreneurial business plan is markedly greater than a plan for an existing business. The fundamental element underpinning this difference stems from the “liabilities of newness" (Stinchcombe 1965: 148). Liability of newness is a new venture’s greatest nemesis. The entrepreneurial business plan is the quiver that carries the arsenal to overcome this deadly enemy. Mature businesses have already overcome this liability; the role of planning in existing ventures differs.

Framed in terms of a medical analogy, business planning for an existing venture is like an annual check up with the family physician. Blood pressure, cholesterol levels and other indicators are compared against data from previous years. The physician and patient update the plan by evaluating the effectiveness of diet and exercise strategies executed (or not) throughout the year. The patient proceeds to live another year and strive for improved milestones before the next anniversary ‘check-up’. On the other hand, business planning for new ventures is analogous to a midwife aiding in childbirth. Without a business plan, “new ventures are likely to be stillborn through a lack of ability to attract vital physical and financial resources” (Hindle 1997:7). A midwife plans for multiple scenarios during the birth process; an entrepreneurial business plan must represent dynamic strategies for a venture’s startup.

Corporate managers of existing firms are judged against meeting a plan. In growing new ventures, however, strict adherence to ‘the plan’ can lead to business failure. To manage business development risk, entrepreneurs must learn to deal with uncertainty. Whereas managers of mature businesses practice the ethic of predictability, entrepreneurs must follow a learning ethic (Sykes 1995).

Entrepreneurial Business Plans Are Dynamic

Mintzberg, argues that all organizations must deal with uncertainty and that it is therefore dangerous for them to articulate strategies because explicit strategies “are blinders designed to focus direction and block out peripheral vision” (Mintzberg 1990): 184). According to Mintzberg, “setting oneself on a predetermined course in unknown waters is the perfect way to sail straight into an iceberg” (Mintzberg 1987). Planning in business might inhibit changes, and discourage the organization from considering disruptive alternatives (Mintzberg 1994:178). Planning might inhibit creativity, and "does not easily handle truly creative ideas" (Mintzberg, 1994:180). A conflict lies with a desire to "retain the stability that planning brings to an organization ... while enabling it to respond quickly to external changes in the environment" (Mintzberg, 1994:184). The reality that nearly anyone involved in managing and planning actually knows but is hesitant to face, - that initial plans rarely accomplishes what it is intended to do. Mintzberg cites the most devastating example of a planning disaster is the battle of Passchendaele, where military planners formulated tactics suitable for dry land. They had never visited the field where thousands fell to their death in a sea of mud.

Hindle (1997) coined the term “provision of flexible credibility” (p.111) to describe the dynamic nature of entpreneurial business planning. Credibility of an EBP is achieved if the document effectively matches the entrepreneurial team’s (resource seekers) resource needs with the investors (resource providers) expectations and criteria. The credibility quotient is necessary but not sufficient. The EBP must also be flexible and able to adopt and adapt the reader’s criteria. An EBP “which presents a ‘take it or leave it’ set of propositions or has its financial forecasts ‘set in cement’ has a high likelihood of failure” (Hindle 1997: 111).

‘Opportunistic planning’ is described in the strategic planning literature as allowing organizations to be flexible and open to making changes in the planning process.

> *“Organizations need a good combination of formal and opportunistic planning. Organizations that rely exclusively on formal planning could trap themselves in unbearable rigidities. Those who's decision-making capability is entirely opportunistic will be constantly reacting to external forces, without a clear sense of direction" (Hax 1996:35-36).*

Hindle (1997) argues that initially, credibility springs from effectively communicating a compelling case that convinces the audience (investors) that the volume of funds required and the resource control and allocation strategies will achieve the new venture’s objective. Subsequent credibility is built by the plan’s capacity to adapt. In communications terms, “the first version of the written plan now assumes the role of opening address in a constructive dialogue; not final oracular proclamation requiring only assent or dissent” (p. 111).

Relevant Theoretical Contexts

As a predicate to theoretical research, we drew insight from two theoretical domains: general systems theory (Bertalanffy 1951; Ackoff 1964) and the Enhanced Entrepreneurial Business Planning Paradigm (Hindle 1997).

Systems Theory

Consistency and accuracy of human decision-making can improve with a system. ‘Systems theory’ was introduced by Bertalanffy in 1951; he proposed that problems can be solved better if component parts are viewed as integrating to a whole. A system is a set of related components that work together in a particular environment. The use of systems theory in management is a product of the merger of many ideas from scientific management, human relations management and operations management (Ackoff 1964). The input-process-output model is a subset of system theory that originated during the industrial revolution and has been used to great benefit in many domains, from manufacturing to communications and decision-making to computer programming.

The input-process-output model can be used to frame the deal screening process in Venture Capital firms. The decision input could be improved by making the *writing* of entrepreneurial business plans (EBPs) more consistent; and this has the potential of improving the process and decision output of deal screening. In other words, standardizing the *content* and *format* of entrepreneurial business plans has the potential to improve the results of venture capital investment decisions. System theory frames this paper by shining the investigative light on the input: the entrepreneurial business plan.

Enhanced Entrepreneurial Business Planning Paradigm

Hindle (1997) discovered, applied and drew inferences about the utility and applicability of an enhanced paradigm of Entrepreneurial Business Planning. The primary utility of Hindle’s research is “a basis for systematic comparative inquiry and a template for quality assessment of the Entrepreneurial Business Planning process and its outputs” (p. 270). Hindle’s work resulted in production of the *Enhanced Entrepreneurial Business Planning Paradigm*, a complex construct embracing:

1. precise definition of application boundaries
2. twelve laws
3. six success rules

4. and specified instrumentation requirements

The laws and successes rules of the "Enhanced Entrepreneurial Business Planning Paradigm (Hindle 1997:122-123) are listed in Table 1.

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By measuring the extent to which Entrepreneurial Business Plans' content and format conform to Hindle's standards (ie. Laws and Rules in a paradigm) can potentially improve the input for the deal screening process.

Two relevant theoretical contexts converge on one practical necessity: developing an Entrepreneurial Business Assessment Regime to measure the quality of EBPs as a decision input.

Theoretical Research Guidance (design)

Semantic analysis (Palmquist, Carley, & Dale, 1997) (also call relational analysis), a subset of content analysis was the methodology used in this paper. Carley (1992) asserts that concepts are "ideational kernels;" these kernels can be thought of as symbols which acquire meaning through their connections to other symbols. Its fundamental purpose, at a general level was to discover an assessment regime for the content and format of Entrepreneurial Business Plans by looking for semantic, or meaningful relationships in business planning literature to discover "ideational kernels". At a specific level three objectives exist: (1) to identify the overall goals of an EBP; (2) to discover fundamental principles that an Entrepreneurial Business Plan should conform to; (3) to establish means to assess each principle.

Fourteen studies comprised the semantic analysis. The Enhanced Entrepreneurial Business Planning Paradigm (Hindle 1997) pioneered business-planning research and provides the groundwork for a system of benchmarking and quality control for writing and EBP documents; it was the primary study drawn from to establish the terms (or semantics) of the assessment principles. The terminology of each principles was then related between the other 13 studies. The principles formed the foundation of a tool to assess the quality of entrepreneurial business plans.

Findings

Communication, control and simulation should be goals of an EBP

A distillation of Hindle's Enhanced Entrepreneurial Business Planning Paradigm suggests that the Entrepreneurial Business plan should be a sharp two-pronged instrument; they have two primary goals: (1) to fundamental *communicate* the venture's vision, and (2) to articulate the *control* and *simulation* of the venture.

It is therefore logistical to design a regime to assess the quality of Entrepreneurial Business Plans using Communication and Control/simulation as dependant variables that form a graph when applied respectively to X and Y axis (see Figure 1).

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Y-axis communication. An EBP that is "proactive about an investor's due diligence requirements" is considered well communicated. From the communication perspective the EPB presents projections that include a rationale that is "testable and replicable by the reader" (p. 113). The aim of the communication mandate is to "anticipate the target investor's due diligence questions and provide answers to them before they are asked" (Hindle 1997: 113). An EPB must be a "unique, purpose-designed document – embodying high standards of literacy and numeracy – of the minimum length appropriate to the subject matter and target audience's information needs" (Hindle 1997: 125).

X-axis control and simulation. An EBP must effectively use the power of simulation to represent the new venture's most likely feasible future. Simulation "commences a dialogue with investors whose perspectives, responses and queries can then be used to forecast multiple alternative scenarios" (Hindle 1997: 115). From the control and simulation perspective an effective EPB has the capacity to enable the target investor to "gain flexible perspectives on the desirability and feasibility of the new venture" (Hindle 1997: 115).

Ten Fundamental Principles are Needed to Assess the Goals of Communication, Control and Simulation in an Entrepreneurial Business Plan

To evaluate the dependent variables of: (1) communication, and (2) control and simulation the individual principles (independent variables) need to be identified. A total of ten principles (five per dependent variable) were identified, largely, by adapting the twelve laws and the 6 success rules from Hindle's Enhanced Entrepreneurial Business Planning Paradigm. We found the goal of communication can be assessed by evaluating 5 independent variables: (1) expectations, (2) milestones, (3) opportunity, (4) content and (5) business model. Control and simulation we found are best assessed by evaluating the independent variables of: (1) team, (2) elaboration, (3) scenario integration, (4) financial link, (5) the deal. A summary matrix of the 10 principles and their link to Hindle's Enhanced Entrepreneurial Business Planning Paradigm is found in Table 2. The rationale for each assessment principle follows.

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Principle 1: expectations. Physically putting a business plan together requires the entrepreneur to translate the vision of the new venture and how it will perform into a format that is dictated, in large part, by the audience. All readers of Entrepreneurial Business Plans can be said to have one crucial thing in common: they use the information the plan contains to aid decision making about "provision of resources to the venture" (Hindle 1997: 11). Thus the prime audience for an EBP is always an investor. The type of investor and their stage of involvement should dictate the depth and breadth of the contents in the EBP. Law #3 of Hindle's Enhanced Business Planning Paradigm states the EBP must "nominate the intended audience" (p. 122). For example, at the screening stage, a Venture Capital firm is expecting from a business plan, an overview of the market opportunity, the distinctive competence, the management team, the business model and the deal structure. In later stages of the investor-entrepreneur relationship more detail will be expected in subsequent iterations the EBP.

In the deal screening stage a Venture Capital firm expects an EBP to communicate that: (1) key success factors and risks can be clearly identified and are understood; (2) the venture has projected market of at least $50 million with good potential market penetration; (3) a strategy for commercialization, profitability and market dominance is present; (4) a strong proprietary and competitive position can be established and protected.

Principle 2: milestones. The milestone approach satisfies the dual need for planning and flexibility and makes obvious the hazards of neglecting linkages between certain events. An effective EBP embodies the principle that "milestones planning takes entrepreneurs at the lowest possible cost to the next important stage, where they can make informed decisions rather than blunder along adhering to a fixed plan that out of ignorance they have based on faulty projections" (Block 1985: 196).

For milestones to be an effective signpost and tools for go/no-go strategies in an EBP they must be anchored by quantitative values rather than chronological dates. Hindle's fourth law states that the writer of an EBP must "identify all major plan objectives, primary as financial targets" (p. 123). Hindle's paradigm reinforces the critical importance of using milestones in EBPs that are anchored with financial and quantitative values.

Principle 3: Opportunity. No opportunity that lasts forever. Consumer trends and tastes, competitive landscape and technological innovation all evolve over time to inevitably change an initial opportunity. There are four aspects that must be described in an EBP to fully articulate the opportunity principle, (1) the new combination of the venture, (2) the magnitude of the opportunity (market size), (3) market growth trends, and (4) venture's value from the market (% of market share proposed market share value in dollars). Hindle's (1997) sixth law calls for the EBP to "Distinguish the venture's business concept, distinctive competencies and sustainable competitive advantages" (p.122). The distinctive competencies and sustainable competitive advantage of an entrepreneurial venture is a result of discovering a *new combination*. Finding new combinations involves a process of entrepreneurial discovery that will become the engine that drives a new venture. According to Schumpeter, "Everyone is an entrepreneur when he actually carries out new combinations, and loses that character as soon as he has built up his business, when he settles down to running it as other people run their businesses" (1934:78).

Principle 4: Context. A high quality Entrepreneurial Business Plan (EBP) should contain certain pieces of evidence related to context into which the new venture will be launched. According to Hindle's (1997) seventh law (message content) an EBP must "provide comprehensive statements of opportunity and risks" (p. 122). More specifically, Sahlman (1997) identifies four key aspects that a business plan should cover to adequately describe the context. First, the entrepreneurs should show a heightened awareness of the new venture's context and how it helps or hinders their specific proposal. Second, and more important, they should demonstrate that they know the venture's context will inevitably change and describe how those changes might affect the business. Further, the EBP should spell out what management can (and will) do in the event the context grows unfavorable. Finally, the business plan should explain the ways (if any) in which the entrepreneurial team can affect context in a positive way. For example, the team might be able to have an impact on regulations or on industry standards through lobbying efforts. From a communications perspective, heightened awareness of the context is demonstrated through the understanding underlying primary assumptions in the market. Quantifying these primary assumptions is the most effective demonstration of this principle. For example, "each month delay in market introduction beyond 15 months from now will cost us a 2% market share." In this example the heightened awareness of the context provides a measure of the incentive to provide increased resources to expedite the new venture.

Principle 5: business model. In an EBP a business model is quite simple: it is a brief statement of how an idea actually becomes a business that makes money. It tells who pays, how much, and how often. The same product or service may be brought to market with several business models. Any entrepreneurial task is made up of a combination of individual activities. When they are represented systematically in relation to one another, the result is a "business model". The business model describes the activities a company needs to perform to produce its product, deliver it to its customers and earn revenue. Sahlman (1997) states the EBP must describe an attractive, sustainable, business model; one that is possible to create a competitive edge and defend it.

A clear description of a business model shows potential investors that the entrepreneurial team has thought through the key drivers of the venture's success or failure. In manufacturing, such a driver might be the yield on a production process; in magazine publishing, the anticipated renewal rate; or in software, the impact of using various distribution channels. A business model that is clearly described and based on a reasonable revenue "driver" will prove to satisfy success rule #2: "empower the EBP reader" (p.123); and Law #6: "distinguish the venture's business *concept*, distinctive *competencies* and sustainable *competitive* advantages" (p. 122). These 'three

Cs' – business *concept*, distinctive *competency* and sustainable *competitive* advantage – form the trinity of message content that describe the business model and thus empower the reader (investor) (Hindle 1997: 265). Empowerment through the description of a business model "involves employing information that makes the potential investor feel competent-i.e. sufficiently potent – to make a decision" (p.123).

Principle 6: Team. An effective description of the entrepreneurial team in an EBP is critical: not because the people part of the new venture is the most important, but because without the right team, none of the other parts really matters (Sahlman 1997).

Many new ventures in reality have an excellent team but fail to adequately describe themselves and highlight their strengths to potential investors through an EBP (Sahlman 1997). The prospective investor is looking for the experience the entrepreneurs have in the market they are or intend to sell to; they are also looking to see if the entrepreneurial team has the skill necessary to carry out the plan. If the entrepreneurial team does not have all of the skills needed to carry out the plan, it should state what specific skills the team has, what specific additional skills are needed and identify how they will be acquired. If the team has identified candidates, those candidates should be revealed. If candidates have not been identified, then the EBP should discuss what skills the team intends to look for in prospective candidates. Hindle (1997) confirms the importance of an effective description of the entrepreneurial team. Hindle compared the skill attributes of the entrepreneurial team in four business plans and concluded that the "application of the enhanced EBP paradigm produced business plans which overcame many of the weaknesses of the less skilled entrepreneurs and augmented many of the strengths of the more skilled entrepreneur" (p.265).

Sahlman (1997) suggests that investors require a description of the entrepreneurial team in to answer three questions: (1) What do they know? (2) Whom do they know? and (3) How well are they known?

What and whom they know are matters of insight and experience. The description of the team should address the familiarity of the team members with industry players and dynamics. An EBP should candidly describe each team member's knowledge of the venture's product or service; its production processes; and the market itself, from competitors to customers.

Principle 7: elaboration. Building a new venture involves a great deal of detail work, which makes the EBP vitally important to not only keep an eye on the whole but to further breakdown individual tasks. Law #9 from Hindle's enhanced EBP paradigm calls to "elaborate the selected strategy as a set of sub-plans" (p.122). Elaboration of strategy is the "decomposition of the codified strategy into a three-part hierarchy: sub strategies; ad hoc programs and specific action plans" (p.25). The result is "a timed sequence of conditional moves in resource deployment" (Katz 1970; 356 cf. Hindle 1997: 25).

EBPs can be clarified by breaking down the overall strategy into a series of sub-plans where individual tasks are grouped. The EBP should elaborate plan by: (1) linking the milestones to sub-plans; (2) using a timeline to show how tasks, milestones and sub-plans interconnect.

Setting reasonable and achievable milestones in an EBP is critical to ensuring that the plan is credible to investors. There is always the danger that EBPs will be too optimistic or too pessimistic. Both errors can have serious consequences for the future of the new venture.

Principle 8: scenario integration. Building a new venture is like chess: to be successful, the entrepreneurial team must anticipate several moves in advance. An EBP that describes an "insuperable lead or a proprietary market position is by definition written by naive people" (Sahlman 1997). All opportunities have promise; all have vulnerabilities. An effective EBP doesn't whitewash the latter. Rather, it proves that the entrepreneurial team knows the good, the bad, and the ugly that the venture faces ahead (Sahlman 1997).

In terms of scenario integration, the discriminative of a good EBP from a bad one can be described using a photography analogy. Many entrepreneurs believe that a good EBP is a snapshot of an event in the future. Sahlman (1997) goes further to state that the best business plans go beyond a single snapshot; “they are like movies of the future. They show the people, the opportunity, and the context from multiple angles. They offer a plausible, coherent story of what lies ahead. They unfold possibilities of action and reaction.”(p. 104).

The most effective EBPs discuss the team (principle #6), opportunity (principle #3), and context (principle #4) as a moving target. All three principles (and the relationship among them) are likely to change over time as a company evolves from start-up to ongoing enterprise. The entrepreneurial team must consider themselves as writers in a screen play and focus on the dynamic aspects of the entrepreneurial process when writing the EBP. Hindle’s enhanced EBP paradigm places considerable focus on scenario integration to build the “provision of flexible credibility” (p.111).

Principle 9: financial link. In the presentation of financials in an EBP, the income and cash flow statements are preceded by operational statements setting forth the primary planning assumptions about market size, sales, productivity and basis for the revenue estimate. Too often entrepreneurs focus on the derivative assumptions such as forecast revenue and return on investment. The forecast profit or return on investment is meaningless by itself. Investors (especially venture capitalists) are well aware of that fact and spend most of their effort understanding the basis for the forecast and the source of the assumptions. They place the highest credibility in the assumptions by those entrepreneurs who have direct experience with the proposed market or technology (Sykes 1995). The key assumptions related to market size, penetration rates and timing issues of market context substantiated in the text of the EBP should be linked directly to the financial statements (Hindle 1997).

Principle 10: the deal. An EBP is written to secure financing. The goal of the EBP is to land a deal with the prospective investor. The entrepreneur must realize when crafting an EBP that “different categories of potential investor stand to gain different levels of benefit from different aspects of a potential investment situation” (Hindle 1997: 124).

Professional investors view a business plan from a holistic perspective. Rather than judge entrepreneurs or their business plans as winners or losers, it is most productive to look at the investment opportunity as an interconnected combination of four elements: people, context, business opportunity, and deal (Amis 2001). The right combination, which is often manageable, means a high-potential opportunity. A bad combination, or the lack of any single element, is a recipe for failure. Most important, within any investment opportunity, there is usually some potential for a win, if only the right investor would join it, or if the right changes would be made. If an entrepreneur implements this integrative philosophy of investing into designing of the deal, the EBP will have a higher chance of successfully securing funding. Hindle’s success rule #5 encapsulates this philosophy: “Create a value-adding deal structure” (p. 124).

A Survey Tool Assesses Each Principle: EBPAR

A survey tool called EBPAR used to assess the content quality of EBPs is derived from the ten assessment principles. EBPAR is design for simplicity; and simplicity is utility’s greatest friend. The tool is designed for the user to literally check boxes indicating the presence of item important to each principle. The user then simply circles a high-med-low rating based on the number of boxes checked for a respective principle. The survey tool is found in Tabl3 3.

DISCUSSION

Initial Utility of the Assessment Regime

Our search for an entrepreneurial business plan assessment regime began with three questions. At a general what are the overall goals of an EBP? What are the fundamental principles that an Entrepreneurial Business Plan should conform to? How can the principles be measured in a given Entrepreneurial Business Plan? The discovered regime provides some answers. The new question becomes how can the assessment regime be used?

Initially, its principal utility will be as a taxonomic device. Entrepreneurial Business Plans can now be practically classified and arranged in meaningful clusters. Two brief examples of hypothetical Entrepreneurial Business Plans will illustrate. EPB 1 describes a venture that proposes to manufacture a new type of sailboat. The vision for the sailboat, the market opportunity and the revenue model for the new venture are articulated with excellence through out the plan; but the plan fails to demonstrate flexibility by not discussing possible scenarios and contingency strategies. This Entrepreneurial Business Plan would rate high on *communication* and low on *control and situation*; it would be positioned as 'window dressing', it reads well but lacks credible flexibility (see Figure 2). EBP 2 describes a 10 minute oil change service. Present in the plan are a variety of capacity scenarios, detailed timelines, financials and management team responsibilities; but the vision for the service and its execution are poorly articulated. This Entrepreneurial Business Plan would rate high on *control and situation* and low on *communication*; it would be positioned as 'a diamond in the rough', the well thought-out credible flexibility of the venture is eclipsed by poor expression (see Figure 2).

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Assessment of both Entrepreneurial Business Plans would result in very different positioning 'profile' but the insight would be equally valuable; the principles important for the assessment of EBPs can be used as guidelines for their improvement. More generally, practicing entrepreneurs and academe may find the assessment regime useful during the writing process as a means of illustrating principles to improve the quality and consistency of an EBP. The Venture Capital community could benefit from the assessment regime if used to rate the quality of EBP as the primary input for the deal screening process.

Future Research Directions

This study has focused on the primary source of decision *input* in the deal screening process by Venture Capital firms: the Entrepreneurial Business Plan. What about *process*: Does the quality of an Entrepreneurial Business Plan affect the deal screening process? What about *actual venture outcome*: Is the quality of entrepreneurial business plans related to the actual performance of a new venture? It seems at least possible that the assessment regime described in this paper or another theoretically substantiated paradigm of the new venture articulation process, could be adapted to increase standardization of the business plans' content and format (decision inputs) in much the same way that the model represented by Generally Accepted Accounting Principles (GAAP) did for financial reporting. This could be a very fruitful area of investigation.

Conclusion

Our study has shown that the quality of Entrepreneurial Business Plans be can assessed based on theoretical principles. Improving the communication, control and simulation aspects of an EBP could have the potential to improve the likelihood that the plan passes the Venture Capital deal screening process. Determining a 'profile' of a particular EBP provides insight for entrepreneur and Venture Capital firm alike: the entrepreneur will be able to improve the articulation of the plan, the Venture Capital firm has another tool in their deal screening quiver. The focus of future research should progress towards greater standardization for the writing and rating of Entrepreneurial Business Plans. Standardization is not an end in itself. But it could become a means of achieving more consistency and greater transparency in the Venture Capital deal screening process.

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Tables

Table 1: Laws and Success Rules for the Enhanced Entrepreneurial Business Planning Paradigm (Hindle 1997)

Paradigm Laws:

Law #1: Codify the selected strategy as a multi-disciplinary continuum.
Law #2: Integrate the codified strategy as a 'base case' scenario.
Law #3: Nominate the intended audience
Law #4: Identify all major plan objectives, primary as financial targets.
Law #5: Define the investment offer(s) as an expected ROI.
Law #6: Distinguish the venture's business concept, distinctive competencies and sustainable competitive advantages.
Law #7: Provide comprehensive statements of opportunities and risks
Law #8: Seek and respond to feedback
Law #9: Elaborate the selected strategy as a set of sub-plans.
Law #10: Convert the selected strategy into a differentiated suite of financial budgets.
Law #11: Re-combine the differentiated budgets into an integrated suite of financial projections.
Law #12: Be able to answer the audience's 'what if' questions in financial terms.

Paradigm Success Rules:

Success Rule #1: Adapt plan length and depth of detail to the interest level and stage of involvement of the target audience.
Success Rule #2: Empower the EBP reader.
Success Rule #3: Create investor confidence by providing flexible credibility.
Success Rule #4: Anticipate and address the target audience's due diligence requirements.
Success Rule #5: Create a value-adding deal structure
Success Rule #6: Employ simulation techniques to obtain the most plausible 'base case' ~~scenario which~~scenario, which can withstand rigorous due diligence investigation

Table 2: Assessment Principles and their link to Hindle 1997

Dependent Variables	Independent Variables (Principle)	Source of Principle from Hindle (1997)
Communication	Expectations	Law #1: Codify the selected strategy as a multi-disciplinary continuum. Law #3: Nominate the intended audience Success Rule #1: Adapt plan length and depth of detail to the interest level and stage of involvement of the target audience. Success Rule #4: Anticipate and address the target audience's due diligence requirements.
	Milestones	Law #4: Identify all major plan objectives, primary as financial targets. Law #8: Seek and respond to feedback Success Rule #3: Create investor confidnce by providing flexible credibility.
	Opportunity	Law #6: Distinguish the venture's business concept, distinctive competencies and sustainable competitive advantages. Law #7: Provide comprehensive statements of opportunities and risks.
	Context	Law #7: Provide comprehensive statements of opportunities and risks.
	Business Model	Law #1: Codify the selected strategy as a multi-disciplinary continuum. Success Rule #2: Empower the EBP reader.
Control & Simulation	Team	Law #1: Codify the selected strategy as a multi-disciplinary continuum.
	Elaboration	Law #9: Elaborate the selected strategy as a set of sub-plans.
	Scenario Integration	Law #1: Codify the selected strategy as a multi-disciplinary continuum. Law #2: Integrate the codified strategy as a 'base case' scenario. Law #12: Be able to answer the audience's 'what if' questions in financial terms. Success Rule #4: Anticipate and address the target audience's due diligence requirements. Success Rule #6: Employ simulation techniques to obtain the most plausible 'base case' scenario which can withstand rigorous due diligence investigation.
	Financial Link	Law #10: Convert the selected strategy into a differentiated suite of financial budgets. Law #11: Re-combine the differentiated budgets into an integrated suite of financial projections.
	The Deal	Law #5: Define the investment offer(s) as an expected ROI. Success Rule #5: Create a value-adding deal structure. Success Rule #6: Employ simulation techniques to obtain the most plausible 'base case' scenario which can withstand rigorous due diligence investigation.

Table 3: Entrepreneurial Business Plan Assessment Regime (EBPAR)

Dependent Variables	Independent Variables (Principle)	Assessment Questions	Rating Criteria	
Communication	Expectations	Does this EBP meet my expectations for efficient provision of sufficient information upon which to make the screening decision? As a Venture Capitalist I am expecting to that: ❒ key success factors and risks can be clearly identified and are understood ❒ the venture has projected market of at least $50 million with good potential market penetration ❒ a strategy for commercialization, profitability and market dominance is present ❒ a strong proprietary and competitive position can be established and protected.	Low	Only 1 or 2 of the expectation items are present in the EBP
			Med	3 of the expectation items are present in the EBP
			High	All 4 of the expectation items are present in the EBP
	Milestones	Are milestones in the EBP are clearly communicated primarily as: ❒ quantitative values ❒ financial targets	Low	Either there are no milestones or they are without any quantitative values or financial targets.
			Med	Some of the milestones use quantitative values or financial targets.
			High	All milestones use quantitative values or financial targets.
	Opportunity	Does this EBP full describe the venture opportunity be describing the following: ❒ the new combination of the venture, ❒ the magnitude of the opportunity (market size), ❒ market growth trends ❒ venture's value from the market (% of market share proposed market share value in dollars).	Low	Only 1 or 2 of the opportunity items are described in the EBP
			Med	3 of the expectation items are described in the EBP
			High	All 4 of the opportunity items are described in the EBP
	Context	Does this EBP demonstrates awareness of the context by describing the: ❒ industry structure ❒ competition	Low	Only 1 or 2 of the content items are described in the EBP
			Med	3 of the context items are described in the EBP

		❒ the predicted changes to the industry over time ❒ factors that will inevitably change but cannot be controlled by the team.	High	All 4 of the context items are described in the EBP
	Business Model	Does this EBP outline the business model by explaining: ❒ who pays (paying customer) ❒ how much (average transaction value) ❒ how often (repetition)	Low	Only 1 of the business model items is explained in the EBP
			Med	2 of the business model items are explained in the EBP
			High	All 1 of the business model items are explained in the EBP
Control /Simulation	Team	Does this EBP describe entrepreneurial addressing: ❒ What do they know? ❒ Whom do they know? ❒ How well are they known?	Low	Only 1 of the aspects of the entrepreneurial team is addressed in the EBP
			Med	2 aspects of the entrepreneurial team are addressed in the EBP
			High	All 3 of the aspects of the entrepreneurial team are addressed in the EBP
	Elaboration	Does this EBP elaborates the overall strategy into sub-plans by: ❒ linking the milestones to sub-plans. ❒ using a timeline to show how tasks, milestones and sub-plans interconnect	Low	Either there are no sub-plans or they are without any linkage to milestones.
			Med	Some of the milestones linked to sub-plans.
			High	All milestones are linked to sub-plans and a timeline show their interconnectedness
	Scenario Integration	Does this EBP employs simulation techniques to obtain a variety of plausible future scenarios by establishing a: ❒ most likely case ❒ best case ❒ worst case	Low	Only a one scenario is presented
			Med	2 scenarios are presented
			High	3 scenarios are presented
	Financial Link	Does this EBP link the selected strategy discussed in the body of the plan to the financials by addressing: ❒ How much money does the company need over what period? ❒ The level of sales to break-even? ❒ When established, how much profit is the company likely to make? ❒ When does cash flow turn positive? ❒ What are the main assumptions that the forecasts are based on?	Low	1 or 2 of the aspects of the financial link are addressed in the EBP
			Med	3 of the aspects of the financial link are addressed in the EBP
			High	4 or 5 of the aspects of the financial link are addressed in the EBP

	The Deal	Does this EBP articulate a value-added deal structure by describing: ❒ funds required; the amount of cash investment required for growth and the use of the proceeds. ❒ the offer; for equity financing the offer in almost always stated as a % of the equity in the venture. ❒ the return; is commonly stated as an annual return on investment. ❒ exit strategy; the most likely mechanism in which in the investor can expect to receive the initial investment back plus the return. ❒ Exit horizon; the approximately length of time the investment will be illiquid.	Low	4 or 5 of the aspects of the deal are addressed in the EBP
			Med	4 or 5 of the aspects of the deal are addressed in the EBP
			High	4 or 5 of the aspects of the deal are addressed in the EBP

Figures

Figure 1: two overall goals of an entrepreneurial business plan

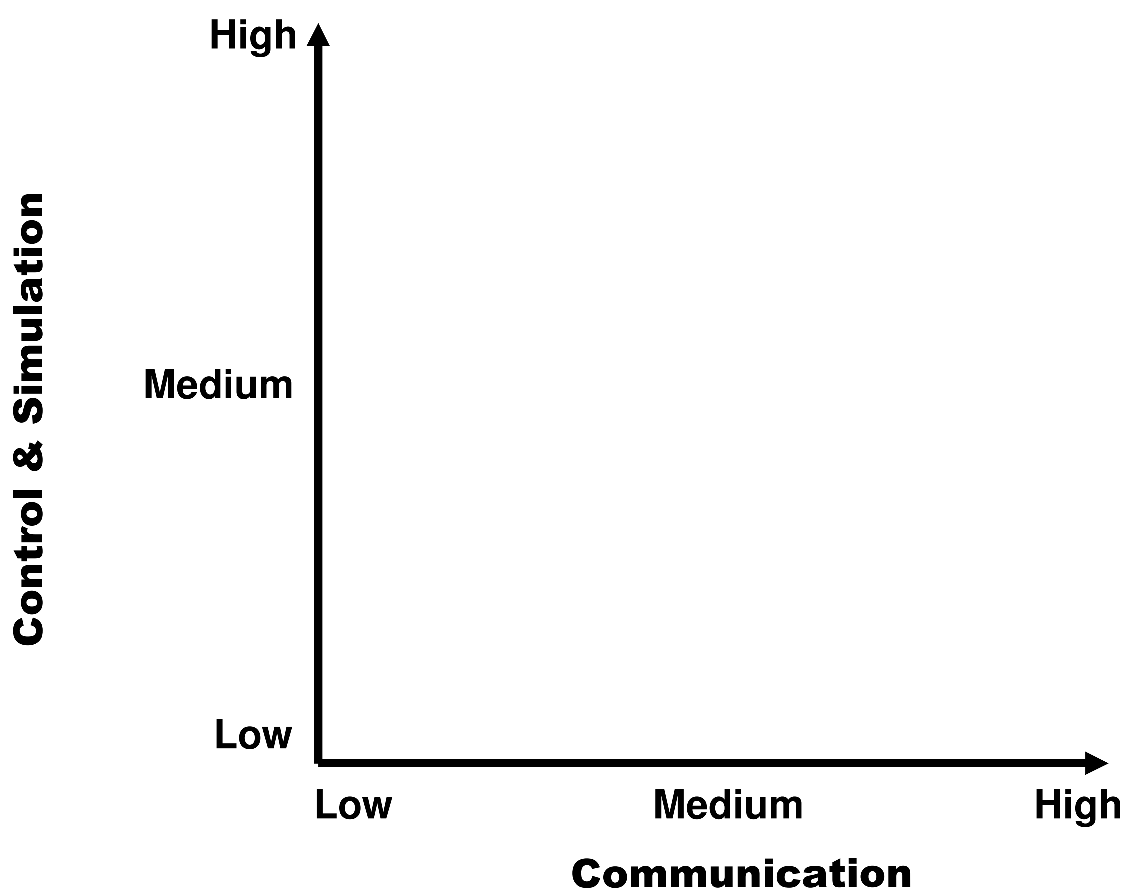
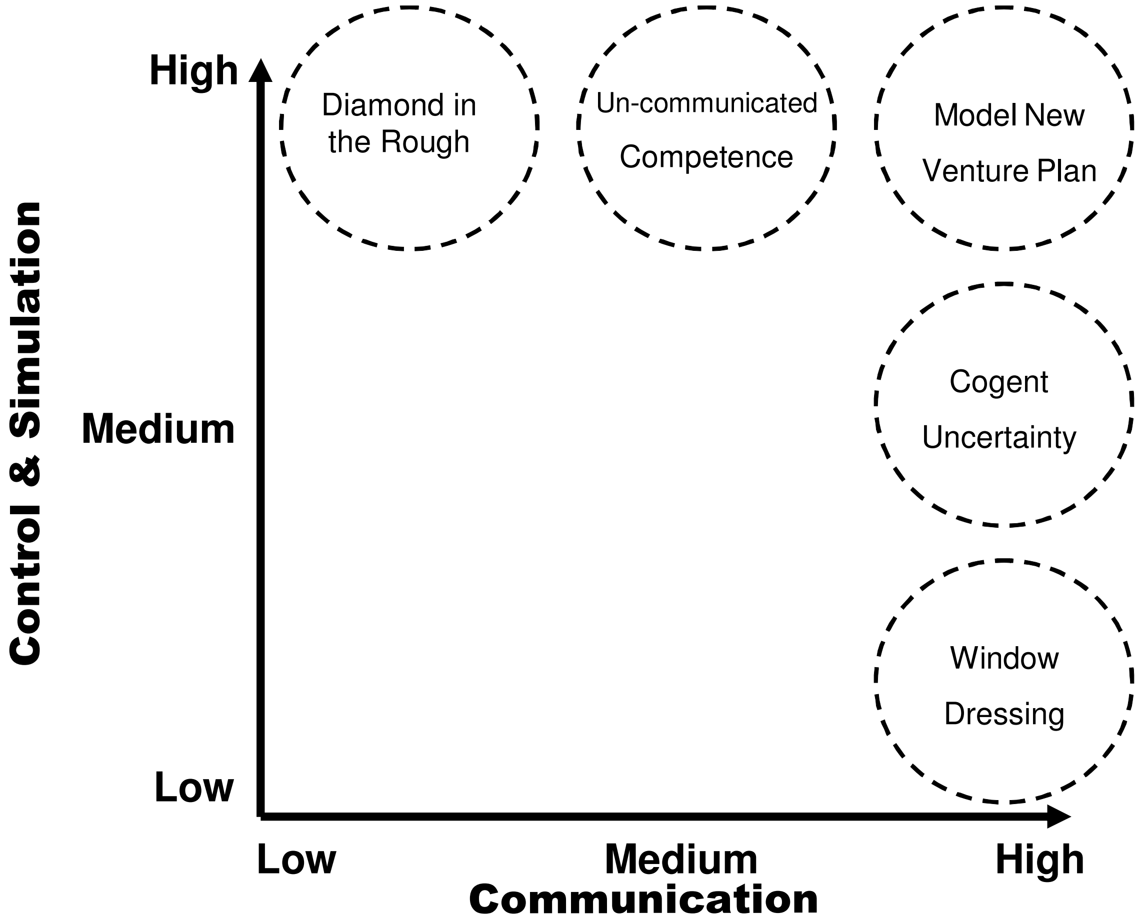


Figure 2: Positioning profiles of EBPs using the Entrepreneurial Business Plan Assessment Regime (EBPAR)



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Appendix A: Detailed rational for each of the ten assessment principles

3.2.1 Principle 1: Expectations

Rationale:

Physically putting a business plan together requires the entrepreneur to translate the vision of the new venture and how it will perform into a format that is dictated, in large part, by the audience. All readers/users of Entrepreneurial Business Plans (EBP) can be said to have one crucial thing in common: they use the information the plan contains to aid decision making about "provision of resources to the venture" (Hindle 1997: 11). Thus the prime audience for an EBP is always an investor. The type of investor and their stage of involvement should dictate the depth and breadth of the contents in the EBP. Law #3 of Hindle's Enhanced Business Planning Paradigm states the EBP must "nominate the intended audience" (p. 122). For example, at the screening stage, an equity investor is expecting from a business plan, an overview of the market opportunity, the distinctive competence, the management team, the business model and the deal structure. In later stages of the investor-entrepreneur relationship more detail will be expected in subsequent iterations the EBP.

Receivers of an EBP communication are "investors" – defined, broadly, as "potential providers of the funds or resources not currently controlled but needed to achieve identified plan objectives" (Hindle 1997: 121). A tailored version of the plan should be targeted to each sub-audience distinct enough to warrant a separate investment offer. The EBP document should "embody appropriate length as a function of the venture's degree of complexity and the target audience's qualified stage of interest. Even one page is too long if the plan is presented in the wrong way to an uninterested or unqualified (in the sense of not being bone fide potential investor) reader. Five hundred pages may be too shallow a level of documentation for deeply interested investor who is immersed in a detailed process of due diligence" (Hindle 1997: 103)

In terms of expectations, arguably the greatest challenge is balancing the detailed communicated about the technology (or new combination) and the market opportunity. For example, an EBP that dwells on the detailed discussion of technology instead of balancing the product/service description with the market opportunity is sure to undercut the confidence of a potential investor. This approach tells the potential investor that the entrepreneurial team considers the technology more important to the business than the market opportunity; this is an approach investors know very rarely works. The investors reading an EBP are expecting the document to show that management understands the technology (or new combination) and how to best structure a business model that will most effectively facilitate sales.

The EBP should treat the potential investor as the prospect. The entrepreneurial team should view the EBP as a vehicle to sell the potential investor a part of the company (or a promise to repay a loan in the case of debt financing). As with any prospect, the first thing that has to be done is to qualify the investor to the EBP. The entrepreneur must make sure they are talking to and writing for the right prospect.

Practically all types of investors limit the investments they make by one or more of (1) the stage of the investment; (2) the amount of the investment; (3) the industry of the investment; (4) the projected return on investment and (5), sometimes, the geographic location of either the company or the market.

From the expectations perspective, all writers of EBPs must begin by asking who's going to read their work. This is especially true for people writing EBPs, because they have the added task of persuading readers to part with their money. The EBP must target the investor's specific concerns. The general categories of target investors and their expectations for the EBP are found below.

Target Audience	Expectation considerations for the EBP
Banks and other lending institutions	Bankers are generally the most conservative of investors. They're looking for a more or less foolproof plan that clearly outlines the collateral (equipment, buildings, vehicles, other person assets, etc.) the entrepreneurial team is willing to put on the line. In addition, lenders will expect to see through the EBP that the entrepreneurial team is trustworthy. They're going to want to see a detailed credit history, plus as much evidence of past entrepreneurial success as possible. If bad credit history is present, the lender will expect to have a sound explanation included in the plan.
Individual Angel investors	Individual Angel Investors typically have a successful history in business development themselves and want to now spend their money helping other entrepreneurs grow. Angel investors prefer to back business ventures they are knowledgeable about. It is rare that they will explore investing in entrepreneurial ventures that lie outside of their industry expertise. Angel investors typically invest in new ventures seeking between $100,000 and $1 million. They are, however, usually more patient than venture capitalists about seeing their return. An EBP targeting Angel Investors should be crafted to accommodate the expectation that the individual investor will offer hands-on expertise, experience and contacts in addition to the money they invest. Even so, they normally don't insist on the control that venture capitalists do. Geography does play a role in their decision making as angels investors want to have the ability to easily arrange for a meeting with entrepreneurs, and not have to spend money on travel and accommodation costs.
Venture capitalists	Venture capital corporations typically expect to receive EBPs that call for in excess of $1 million in investment. Competition for venture capital money is fierce and as a result an EBP must make a case that the venture is not just going to be profitable, but will grow rapidly over a period of five to seven years. A personal introduction or referral will help enormously, since venture capital firms get many more proposals than they can read. A venture capitalists audience expects that the EBP is short and the investment offer is clearly defined (Hindle 1997:79). In general the EBP should communicate to a venture capital audience that: • key success factors and risks can be clearly identified and are understood. • the venture has projected market of at least $50 million with good potential market penetration • a strategy for commercialization, profitability and market dominance is present • a strong proprietary and competitive position can be established and protected
Family and Friends	Family and friends of the entrepreneurial team are a great source of financing at the very early stages of a new venture. Trust from the personal

	relationships with family and friends easily transfer to an investment capacity. Unlike other investors, family and friends are generally less sophisticated. As a result they invest more because of their connection with the entrepreneur(s) than the merits of the business idea/opportunity. It is unusual for a single investor in the family and friends category to invest more than $100,000. The entrepreneurial team targeting this type of investor should keep the EBP simple and free of business and technology jargon but it is still important to keep the plan as professional as possible. Many relationships with family and friends change significantly (for the worst) as a result of expectations that were poorly communicated prior to the investment. The entrepreneurial team should (generally) not expect family and friends to sign on out of a sense of duty. The EBP must demonstrate to them that the venture can be genuinely profitable, and make sure any agreement that is reached is committed to writing.

Assessment Question

To what degree does the depth and breadth in the plan match the interest level and stage of involvement of the target audience?

Assessment Criteria:

Low (1,2,3)	The EBP is not written for the investor's stage of involvement and there is no match between the EBP's content and the investor's expectations.
Medium (4,5,6)	The EBP is written generally for the reader's stage of involvement and partially matches the investor's expectations.
High (7,8,9)	The EBP is written specially for the investor's stage of involvement and matches the investor's expectations.

3.2.2 Principle 2: Milestones

Rationale:

An effective EBP is like a good road map. A road map clearly indicates all possible routes to a variety of destinations. However, more importantly, road maps indicates what the driver should be looking for to determine the progress of the trip at any point in time; signposts that appear on the map are compared to those along the route to indicate a driver's progress towards his/her destination. In an EBP, the entrepreneur uses milestones described in the business plan to monitor the progress of a new venture. However, where EBPs and road maps differ is in the fact that a road map is based on the documentation of previous exploration where as an EBP is a rough chart for previously un-chartered territory.

Conventional planning, in which much is known, is analogous to an established road map. McGrath (1995) defines conventional planning as 'platform-based planning' that "operates on the premise that managers can extrapolate future results from a well-understood and predictable platform of past experience' (p.44). The platform-based approach may make sense for ongoing businesses, but it is sheer folly when applied to new ventures. By definition, new ventures call for entrepreneurs to create an EBP to envision what is unknown, uncertain, and not yet obvious to the competition. New ventures are undertaken with a high ratio of assumptions to knowledge. In ongoing businesses, the ratio is considered to be inverse - high ratio of knowledge to assumptions. However, where no map exists, McGrath (1995) coins the term 'discovery-driven planning' that "forces entrepreneurs to articulate what they don't know, and forces a discipline for learning how to best achieve their desired destination" (p.54). Discovery-driven planning is defined as "the real potential of the new venture is discovery as it develops" (p. 45).

Milestone planning is a familiar technique for monitoring the progress of new ventures. The basic idea, as described by Block (1993) is to postpone major commitments of resources until the evidence from the previous milestone event signals that the risk of taking the next step is justified. Milestones serve as corner stones in EBPs. The milestone approach to measuring new venture performance examines what has been learned and how effectively the entrepreneurs have modified plans to respond to new information rather than use projections versus performance as a measure. Entrepreneurs should create and use EBPs to make financing decisions as events are completed, using what they have learned to make go, no-go or redirection decisions. For most ventures, however significant events-not dates-should determine milestones (Block 1985: 184). The only hard dates in the plan should be externally imposed, for example factors like contract agreements or competitive pressures.

Block (1985) states "to give an event milestone maximum learning value, the business plan must define the event's completion so that managers can test any assumptions they make" (p.185). For example, a plan would not just read: "Milestone – completion of product development". A better, more specific statement would be: "Milestone – completion of product development. Completion of a prototype machine that costs no more than $150,000; that can be manufactured for a direct cost of $12,000; that can produce 40 widgets per minute at 30 cents per widget; that the FCC will approve; and that high school graduates can operate with three days of training".

The milestone approach satisfies the dual need for planning and flexibility and makes obvious the hazards of neglecting linkages between certain events. An effective EBP embodies the principle that "milestones planning takes entrepreneurs at the lowest possible cost to the next important stage, where they can make informed decisions rather than blunder along adhering to a fixed plan that out of ignorance they have based on faculty projections" (p.196).

For milestones to be an effective signpost and tool for go/no-go strategies in an EBP they must be anchored by quantitative values rather than chronological dates. Hindle's fourth law of his enhanced EBP paradigm states that the writer of an EBP must "identify all major plan objectives, primary as financial targets" (p. 123). Hindle's paradigm reinforces the critical importance of using milestones in EBPs that are anchored with financial and quantitative values.

Assessment Question:
Are the major milestones of the plan clearly communicated primarily as quantitative values and financial targets?

Assessment Criteria:

Low (1,2,3)	The EBP either does not identify major milestones of the new venture or does without any quantitative values or financial targets.
Medium (4,5,6)	The EBP describes some (but not all) of the major milestones of the new venture with quantitative values and financial targets.
High (7,8,9)	The EBP describes the major milestones of the new venture with quantitative values and financial targets.

3.2.3 Principle 3: Opportunity

Rationale:
There is no opportunity that lasts forever. Consumer trends and tastes, competitive landscape and technological innovation all evolve over time to inevitably change an initial opportunity. There are four aspects that must be described in an EBP to fully articulate the opportunity principle, (a) the new combination of the venture, (b) the magnitude of the opportunity (market size), (c) market trends and growth, and (d) venture's value form the market (% of market share proposed market share value in dollars).

(a) New combination

Hindle's (1997) sixth law calls for the EBP to "Distinguish the venture's business concept, distinctive competencies and sustainable competitive advantages" (p.122). The distinctive competencies and sustainable competitive advantage of an entrepreneurial venture is a result of discovering a new combination. Finding new combinations involves a process of entrepreneurial discovery that will become the engine that drives a new venture. According to Schumpeter, "Everyone is an entrepreneur when he actually carries out new combinations, and loses that character as soon as he has built up his business, when he settles down to running it as other people run their businesses" (1934:78).

Schumpeter (1934: 66) identified 5 categories of a new combination:

1. introduction of new good: one with which consumers are not yet familiar - or a new quality of an existing good.
2. introduction of a new method of production: one not yet tested by experience in the branch of manufacture concerned, which need by no means be founded upon a discovery scientifically new, and can exist in a new way of commodity commercially.
3. opening of a new market: into which the particular branch of manufacture of the country in question has not previously entered, whether or not this market has existed before
4. conquest of a new source of supply: including raw materials or half-manufactured goods, again irrespective of whether the source of supply already exists or whether it has first to be created.
5. carrying out of the new organisation of any industry: like the creation of a monopoly position ... or the breaking-up of a monopoly position.

An entrepreneurial business plan must clearly communicate the source of the venture's new combination.

(b) Magnitude

The optimal magnitude of a market opportunity is not the same for all new ventures. Muzyka (2000) identifies four factors entrepreneurs should consider before deciding on and articulating the magnitude of a market opportunity in an EBP. First, the size of the opportunity that entrepreneur chooses is dependent on the magnitude of value that they wish to create and that will attract and retain investor interest. Risk capital investors usually have a minimum market value threshold that must be met before they invest. Second, the magnitude of the opportunity will affect the initial and future competitive position of the new venture in the marketplace. Third, the entrepreneur must consider the economic factor of "minimum efficient scale". The new venture should try as best as possible to 'fit' the opportunity and resources to use required assets in the most efficient way (Timmons 1994). Fourth, the entrepreneurs must consider the magnitude of the business necessary to hold their own interests and attract the key members required to successfully grow the new venture.

(c) market trends and growth

An EBP must clearly describe how the market will grow and change over time. For any market opportunity the entrepreneur is rewarded with profits resulting from a temporary monopoly situation, in some cases leading to "creative destruction" and the redistribution of wealth (Schumpeter 1967). Creative destruction inherently causes a temporary advance for a new venture. Understanding market trends and clearly describing them in the EBP, signals to the investor that the entrepreneur comprehends the forces that will shape the evolution of the market. Specifically the EBP should discuss how big the market would grow in the next three to five years. The growth estimates should be supported with industry trends, technological developments, changing customer needs and other related factors. The sources and assumptions should be clearly stated and realistic.

(d) Venture's value from the market

If the EBP overstates the venture's market share, investors will question the credibility of the entire business plan. The EBP should breakdown the overall size of the market to the venture's share of the market. The EBP can state this value as a percentage of the overall market or as a dollar value.

Assessment Question:

Does the plan distinguish the forces creating the opportunity and its magnitude? (trends, market size and growth)

Assessment Criteria:

Low (1,2,3)	The EBP does not adequately distinguish the forces creating the opportunity and its magnitude. The plan addresses one (or none) of the following: (a) the new combination, (b) market trends, (c) market size, and (d) the venture's market penetration rate (or proposed market share value in dollars).
Medium (4,5,6)	The EBP somewhat distinguishes the forces creating the opportunity and its magnitude by addressing some (at least 2 of 4) of the following: (a) the new combination, (b) market trends, (c) market size, and (d) the venture's market penetration rate (or proposed market share value in dollars).
High (7,8,9)	The EBP clearly distinguishes the forces creating the opportunity and its magnitude by addressing all (or at least 3 of 4) of the following: (a) the new combination, (b) market trends, (c) market size, and (d) the venture's market penetration rate (or proposed market share value in dollars).

3.2.4 Principle 4: Context

Rationale:

A high quality Entrepreneurial Business Plan (EBP) should contain certain pieces of evidence related to context into which the new venture will be launched. According to Hindle's (1997) seventh law (message content) states that an EBP must "provide comprehensive statements of opportunity and risks" (p. 122). More specifically, Sahlman (1997) identifies four key aspects that a business plan should cover to adequately describe the context. First, the entrepreneurs should show a heightened awareness of the new venture's context and how it helps or hinders their specific proposal. Second, and more important, they should demonstrate that they know the venture's context will inevitably change and describe how those changes might affect the business. Further, the EBP should spell out what management can (and will) do in the event the context grows unfavorable. Finally, the business plan should explain the ways (if any) in which management can affect context in a positive way. For example, management might be able to have an impact on regulations or on industry standards through lobbying efforts. From a communications perspective, heightened awareness of the context is demonstrated through the understanding underlying primary assumptions in the market. Quantifying these primary assumptions is the most effective demonstration of this principle. For example, "each month delay in market introduction beyond 15 months from now will cost us a 2% market share." In this example the heightened awareness of the context provides a measure of the incentive to provide increased resources to expedite the new venture.

Assessment Question:

Does the plan communicate a heightened awareness of the proposed operating environment?

Assessment Criteria:

Low (1,2,3)	The EBP demonstrates low to no awareness of the context by failing to address (one or fewer) the following: (a) industry structure, (b) competition, (c) predicting changes over time, and (d) identifying factors that inevitably change but cannot be controlled by the team.
Medium (4,5,6)	The EBP indicates a moderate awareness of the context by addressing some (at least 2 of 4) of the following: (a) industry structure, (b) competition, (c) predicting changes over time, and (d) identifying
High (7,8,9)	The EBP describes a heightened awareness of the context by addressing all (at least 3 of 4) of the following: (a) industry structure, (b) competition, (c) predicting changes over time, and (d) identifying factors that inevitably change but cannot be controlled by the team.

3.2.5 Principle 5: Business Model

Rationale:
In an EBP a business model is quite simple: it is a brief statement of how an idea actually becomes a business that makes money. It tells who pays, how much, and how often. The same product or service may be brought to market with several business models.

Any entrepreneurial task is made up of a combination of individual activities. When they are represented systematically in relation to one another, the result is a "business model". The business model describes the activities a company needs to perform to produce its product, deliver it to its customers and earn revenue. Sahlman (1997)states the EBP must describe an attractive, sustainable, business model; one that is possible to create a competitive edge and defend it.

A high quality EBP must include a clear description of a business model that shows the entrepreneurial team has thought through the key drivers of the venture's success or failure. In manufacturing, such a driver might be the yield on a production process; in magazine publishing, the anticipated renewal rate; or in software, the impact of using various distribution channels. A business model that is clearly described and based on a reasonable revenue "driver" will prove to satisfy success rule #2 in Hindle's Enhanced Entrepreneurial Business Planning Paradigm, "empower the EBP reader" (p.123). Law #6 of the Enhanced Entrepreneurial Business Planning Paradigm calls for the EBP to "distinguish the venture's business concept, distinctive competencies and sustainable competitive advantages" (p. 122). These 'three Cs' – business *concept*, distinctive *competency* and sustainable *competitive* advantage – form the trinity of message content that describe the business model and thus empower the reader (investor) (Hindle 1997: 265). Empowerment through the description of a business model "involves employing information that makes the potential investor feel competent-i.e. sufficiently potent – to make a decision" (p.123)

Assessment Question:
Does the plan sufficiently outline the overall business model and explain the key assumptions that underpin the model?

Assessment Criteria:

Low (1,2,3)	The EBP leaves the potential investor feeling incompetent to make a decision by failing to (a) provide a clear description of the business model and (b) explain the key assumptions that underpin the model.

Medium (4,5,6)	The EBP leaves the potential investor feeling moderately competent to make a decision by failing to adequately address one of the following: (a) a clear description of the business model or (b) an explanation of the key assumptions that underpin the model.
High (7,8,9)	The EBP leaves the potential investor feeling completely competent- i.e. sufficiently potent – to make a decision by (a) providing a clear description of the business model and (b) explaining the key assumptions that underpin the model.

3.2.6 Principle 6: Team

Rationale:

An effective description of the entrepreneurial team in an EBP is critical: not because the people part of the new venture is the most important, but because without the right team, none of the other parts really matters.

A typical venture capital firm receives hundreds of business plans per year. Most sophisticated investors realized that the venture idea is secondary to the team in terms of importance. The execution of the idea is more important than the idea; this requires the right team. As Arthur Rock, a venture capital legend associated with the formation of such companies as Apple, Intel, and Teledyne, states, "I invest in people, not ideas." Rock also has said, "If you can find good people, if they're wrong about the product, they'll make a switch, so what good is it to understand the product that they're talking about in the first place?" (Sahlman 1997).

Many new ventures in reality have an excellent team but fail to adequately describe themselves and highlight their strengths to potential investors through an EBP (Sahlman 1997). The prospective investor is looking for the experience the entrepreneurs have in the market they are or intend to sell to; they are also looking to see if the entrepreneurial team has the skill necessary to carry out the plan. If the entrepreneurial team does not have all of the skills needed to carry out the plan, the plan should state what specific skills the team has, what specific additional skills are needed and identify how the additional specific skills needed will be acquired. If management has identified candidates, those candidates should be revealed. If candidates have not been identified, then the EBP should discuss what skills management intends to look for in prospective candidates. Hindle (1997) confirmed the importance of an effective description of the entrepreneurial team. Hindle compared the skill attributes of the entrepreneurial team in four business plans and concluded that the “application of the enhanced EBP paradigm produced business plans which overcame many of the weaknesses of the less skilled entrepreneurs and augmented many of the strengths of the more skilled entrepreneur” (p.265).

Sahlman (1997) suggests that investors require that the description of the entrepreneurial in the EBP answer three questions about the venture's team members: (1) What do they know? (2) Whom do they know? and (3) How well are they known?

What and whom they know are matters of insight and experience. The description of the team should address the familiarity of the team members with industry players and dynamics. An EBP should candidly describe each team member's knowledge of the new venture's type of product or service; its production processes; and the market itself, from competitors to customers.

Assessment Question:

Does the plan clearly describe the entrepreneurial team?

Assessment Criteria:

Low (1,2,3)	The EBP does not adequately describe the entrepreneurial team. Only one (or none) of the following aspects were adequately addressed: (a) What do they know?, (b) Whom do they know?, (c) How well are they known?
Medium (4,5,6)	The EBP describes some aspects of the entrepreneurial team. Two (of 3) of the following aspects were adequately addressed: (a) What do they know?, (b) Whom do they know?, (c) How well are they known?
High (7,8,9)	The EBP clearly describes all aspects of the entrepreneurial team by addressing all (all 3 of 3) of the following: (a) What do they know?, (b) Whom do they know?, (c) How well are they known?

3.2.7 Principle 7: Elaboration

Rationale:

Building a new venture involves a great deal of detail work, which makes the EBP vitally important to not only keep an eye on the whole but to further breakdown individual tasks. Law #9 from Hindle's enhanced EBP paradigm calls to "elaborate the selected strategy as a set of sub-plans" (p.122). Elaboration of strategy is the "decomposition of the codified strategy into a three-part hierarchy: sub strategies; ad hoc programs and specific action plans" (p.25). The result is "a timed sequence of conditional moves in resource deployment" (Katz 1970; 356 cf. Hindle 1997: 25).

EBPs can be clarified by breaking down the overall strategy into a series of sub-plans where individual tasks are grouped. The EBP should, however, not contain more than approximately a half dozen (6) of these sub-plans. Each sub-plan should contain a "milestone"—a specific measurable, time-based target. The milestone has been reached when the relevant target is achieved.

Setting reasonable and achievable milestones in an EBP is critical to ensuring that the plan is credible to investors. There is always the danger that EBPs will be too optimistic or too pessimistic. Both errors can have serious consequences for the future of the new venture.

Over-optimistic planning in an EBP creates double jeopardy. First, the entrepreneurial team will rapidly lose credibility with all their partners. Second, over-optimistic planning can easily result in the failure of a new venture shortly after its launch. It can happen like this:

- Resources—material and human—are built up rapidly, according to plan, and costs rise accordingly. The jargon term for this a high "burn rate"—the money is burnt up rapidly.

- Some delay occurs, perhaps in product development, market entry, or in reaching sales targets. Income is delayed, while at the same time the costs of under-utilized resources are rising. The new venture is not just posting book losses, it is losing cash.

- Inevitably, the money runs out before the planned success is achieved. New funds are needed in an emergency situation.

- If no investors can be found, the venture fails. If there are investors who still believe in its success (which is doubly unlikely after the loss of credibility due to faulty planning), they will provide further funds. However, for the entrepreneur this often means a painful reduction in his/her share of the company, and perhaps even the total loss of equity.

At first glance, pessimistic or conservative planning seems the lesser evil. The entrepreneurial team and the investors will be pleasantly surprised by the progress, and everything goes better, and happens more quickly, than expected. However, the fact remains that pessimistic planning can have just as serious consequences, as shown in the following two scenarios:

- The business takes off, but the necessary resources are lacking. One option is to try to meet the demand with the available resources, but this is bound to produce quality problems that will put the long-term success of the new venture at risk. An alternative is to grow according to the plan, in the knowledge that potential sales are being lost, and with the risk that a competitor will enter the business. At any event significant value-added is lost, for both the entrepreneur and the venture.

- The business grows more quickly than expected. However, growth requires liquid assets (cash) and usually investments in production. The company quickly runs out of money, although it is posting book profits. The consequence for the entrepreneur is the need to find additional funds earlier than planned, under time pressure and on unattractive terms. This road leads to insolvency: the entrepreneurial team can literally "grow the venture bankrupt".

Both wild optimistic and over conservative planning can not only adversely affect credibility with investors but put the future of the new venture at risk. The effective EBP takes into account of all uncertainties by creating sub-plans and setting milestones than are reasonable and credible.

<u>*Assessment Question:*</u>
Does the plan sufficiently elaborate the overall strategy as a set of achievable sub-plans?

<u>*Assessment Criteria:*</u>

Low (1,2,3)	The EBP does not adequately elaborate the overall strategy into sub-plans. There are no measurable milestones that link to the sub-plans.
Medium (4,5,6)	The EBP somewhat elaborates the overall strategy into sub-plans. There are some measurable milestones that link to the sub-plans.
High (7,8,9)	The EBP clearly and credibly elaborates the overall strategy into sub-plans. There are measurable milestones that link to all the sub-plans.

3.2.8 Principle 8: Scenario Integration

<u>*Rationale:*</u>
Building a new venture is like chess: to be successful, the entrepreneurial team must anticipate several moves in advance. An EBP that describes an "insuperable lead or a proprietary market position is by definition written by naive people" (Sahlman 1997). All opportunities have promise; all have vulnerabilities. An effective EBP doesn't whitewash the latter. Rather, it proves that the entrepreneurial team knows the good, the bad, and the ugly that the venture faces ahead (Sahlman 1997).

In terms of scenario integration, the discriminative of a good EBP from a bad one can be described using a photography analogy. Many entrepreneurs believe that a good EBP is a snapshot of an event in the future. Sahlman (1997) goes further to state that the best business plans go beyond a single snapshot; "they are like movies of the future. They show the people, the opportunity, and the context from multiple angles. They offer a plausible, coherent story of what lies ahead. They unfold possibilities of action and reaction."(p. 104).

The most effective EBPs discuss the team (principle #6), opportunity (principle #3), and context (principle #4) as a moving target. All three principles (and the relationship among them) are likely to change over time as a company evolves from start-up to ongoing enterprise. The entrepreneurial team must consider themselves as writers in a screen play and focus on the dynamic aspects of the entrepreneurial process when writing the EBP.

Hindle's enhanced EBP paradigm places considerable focus on scenario integration to build the "provision of flexible credibility" (p.111). Hindle states two paradigm laws and two success rules that pertain to the principle of scenario integration:

> Law #2: Integrate the codified strategy as a 'base case' scenario.
>
> Law #12: Be able to answer the audience's 'what if' questions in financial terms.
>
> Success Rule #4: Anticipate and address the target audience's due diligence requirements.
>
> Success Rule #6: Employ simulation techniques to obtain the most plausible 'base case' scenario, which can withstand rigorous due diligence investigation.

In practical essence scenario integration in EBPs "means being able to adapt the plan very quickly to the particular inquiries, emphases and assumptions of a particular investor" (Hindle 1997:123).

Originally conceived by the US Air Force as a war gaming technique for defense strategy (Deweerd 1967) and used by futurist Herman Kahn in the 1960s, scenario analysis was first applied in a significant commercial setting by Shell Oil in the early 1970s (Bers 1997). As Schwartz (1991) recounts, brilliant analysis led Shell's Group Planning organization to the prediction that previously stable oil prices were about to become radically destabilized. But they failed in their efforts to persuade senior management. Fortunately, out of their failure emerged a new view of the role of planning: "We no longer saw our task as producing a documented view of the future business environment five or ten years ahead. Our real target was the….mental model of our decision-makers". Scenario analysis allowed operating managers to think through how they would manage in the future under different possible scenarios. By the time OPEC oil shocks arrived in 1973, these mangers had already been used to working through the implications of much higher prices and much greater volatility by employing scenario analysis.

Bers et al (1997) found that executives understanding of assumption critical to the success of a venture increased significantly after applying scenario analysis to their respective business. While the entrepreneurial team does not and cannot know with certainty the exact future scenario that will come to pass, they can define a variety of scenarios in the EBP distinctly enough that investors can feel reasonably confident that the actual future will turn out somewhere among them.

Assessment Question:

Does the EBP employ simulation techniques to obtain a variety of the most plausible future scenarios?

Assessment Criteria:

Low (1,2,3)	The EBP does not adequately employ simulation techniques. The EBP is written around a single scenario.
Medium (4,5,6)	The EBP somewhat employs simulation techniques to obtain plausible future scenarios. At least two scenarios are identified but not adequately described.
High (7,8,9)	The EBP employs simulation techniques to obtain a variety of plausible future scenarios. At least two scenarios are identified and described in detailed.

3.2.9 Principle 9: Financial Link

Principle:

In the presentation of financials in an EBP, the income and cash flow statements are preceded by operational statements setting forth the primary planning assumptions about market size, sales, productivity and basis for the revenue estimate. Too often entrepreneurs focus on the derivative assumptions such as forecast revenue and return on investment. The forecast profit or return on investment is meaningless by itself. Investors (especially venture capitalists) are well aware of that fact and spend most of their effort understanding the basis for the forecast and the source of the assumptions. They place the highest credibility in the assumptions by those entrepreneurs who have direct experience with the proposed market or technology (Sykes 1995).

The key assumptions related to market size, penetration rates and timing issues of market context substantiated in the text of the EBP should be linked directly to the financial statements. Hindle states two laws pertaining to financial link:

> Law #10: Convert the selected strategy into a differentiated suite of financial budgets.
>
> Law #11: Re-combine the differentiated budgets into an integrated suite of financial projections.

What professional investors are impressed by is a small number of well thought out key figures not several pages of statements demonstrating the ability to use electronic spreadsheet software. The financials is the EBP plan must answer the following questions:

- How much money does the company need over what period?
- When established, how much profit is the company likely to make?
- What are the main assumptions that the forecasts are based on?

This information will give investors an idea to what extent the figures are reasonable and plausible. The reasonability of the figures is dependent upon how closely they are linked to the assumptions substantiated through the EBP. Simulating the future performance of the new venture is a critical function of the financials in an EBP. "For any EBP, the fundamental co-ordination, control and simulation instrument must be a comprehensive financial projection model capable of enumerating the financial implications of alternative scenarios (Hindle 1997: p.343). Hindle designed and built a generic financial modeling system called FIPRAL. This 'financial projection and analysis model' (FIPRAL) aids in the creation of financial projections in an EBP.

Exacting detailed financial calculations to the dollar is not necessary, as forecasts are by their nature approximate, and even more so for a new company. The financial numbers in an EBP should appear mainly in the form of a business model that shows the entrepreneurial team has thought through the key drivers of the venture's success or failure. In manufacturing, such a driver might be the yield on a production process; in magazine publishing, the anticipated renewal rate; or in software, the impact of using various distribution channels. The model should also address the break-even issue: At what level of sales does the business begin to make a profit? And even more important, when does cash flow turn positive? Without a doubt, these questions deserve a few pages that comprise the financials of an EBP (Sahlman 1997).

Assessment Question:

Does the EBP convert and link the selected strategy using critical assumptions substantiated to create an integrated suite of financial projections?

Assessment Criteria:

Low (1,2,3)	The EBP does not adequately link the selected strategy discussed in the body of the plan to the financials. There is a significant disconnect between the strategy and assumptions stated in the plan and the financial projections.
Medium (4,5,6)	The EBP somewhat links the selected strategy discussed in the body of the plan to the financials. There is some connection between the strategy and assumptions stated in the plan and the financial projections.
High (7,8,9)	The EBP effectively links the selected strategy discussed in the body of the plan to the financials. There is a virtually seamless connection between the strategy and assumptions stated in the plan and the financial projections.

3.2.10 Principle 10: The Deal

<u>Rationale:</u>

An EBP is written to secure financing. The goal of the EBP is to land a deal with the respective investor. The entrepreneur must realize when crafting an EBP that "different categories of potential investor stand to gain different levels of benefit from different aspects of a potential investment situation" (Hindle 1997: 124).

Professional investors view a business plan from a holistic perspective. Rather than judge entrepreneurs or their business plans as winners or losers, it is most productive to look at the investment opportunity as an interconnected combination of four elements: people, context, business opportunity, and deal (Amis 2001). The right combination, which is often manageable, means a high-potential opportunity. A bad combination, or the lack of any single element, is a recipe for failure. Most important, within any investment opportunity, there is usually some potential for a win, if only the right investor would join it, or if the right changes would be made. If an entrepreneur implements this integrative philosophy of investing into designing of the deal, the EBP will have a higher chance of successfully securing funding. Hindle's success rule #5 encapsulates this philosophy: "Create a value-adding deal structure" (p. 124).

More specifically, the four elements of the Harvard Framework for equity investment provide further insight into deal structure. The framework was developed by William Sahlman and Howard Stevenson at Harvard Business School and is explained in Amis and Stevenson (2001). The integrative nature of the four elements show in figure 1 followed by a description outlining each element below:

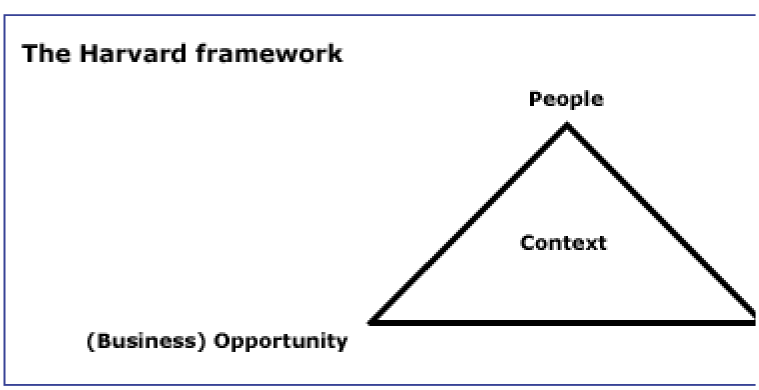

Figure 1

People: The people in the deal, include the entrepreneur, team members, investors, advisors, and any significant stakeholders. The details of this element are discussed in the rationale of principle #6: Team found above.

Business opportunity: The potential business opportunity, which includes the business model, the size (which implies the potential returns), the customers, and the window within which it can be seized. (See Principle # 3: Opportunity found above)

Context: The context includes the macro-situation, which includes external factors, such as: technology development, customer desires, the state of the economy, industry trends, etc. (See Principle # 4: Context found above).

Deal: The elements of the deal include structure of the deal, its terms and pricing. Not only is each element critical by itself, but also the way they interact is also crucial.

The deal described in an EBP should include 5 key elements:

1. funds required: the amount of cash investment required for growth and the use of the proceeds.
2. the offer: for equity financing the offer in almost always stated as a % of the equity in the venture.
3. the return: is commonly stated as an annual return on investment. Hindle's Law #5 pertaining to the deal states to "Define the investment offer(s) as an expected ROI" (p.122).
4. exit strategy: refers to the most likely mechanism in which in the investor can expect to receive the initial investment back plus the return. Examples of common exit strategies include Initial Public Offering, acquisition by another company, fixed payment buyout, and hold and collect dividends.
5. Exit horizon: the approximately length of time the investment will be illiquid.

<u>*Assessment Question:*</u>
Does the plan articulate a value added deal structure?

<u>*Assessment Criteria:*</u>

Low (1,2,3)	The EBP does not adequately articulate a value added deal structure. Only one (or none) of the following aspects are adequately addressed: (a) funds required, (b) the offer, (c) the return, (d) exit strategy, (e) exit horizon.
Medium (4,5,6)	The EBP describes some aspects of a value added deal structure. Two to three (of 5) of the following aspects are adequately addressed: (a) funds required, (b) the offer, (c) the return, (d) exit strategy, (e) exit horizon.
High (7,8,9)	The EBP clearly articulates a value added deal structure by addressing 4 or more (of 5) of the following: (a) funds required, (b) the offer, (c) the return, (d) exit strategy, (e) exit horizon.

================ Appendix 1====================

Paradigm Laws:
Law #1: Codify the selected strategy as a multi-disciplinary continuum.
Law #2: Integrate the codified strategy as a 'base case' scenario.
Law #3: Nominate the intended audience

Law #4: Identify all major plan objectives, primary as financial targets.
Law #5: Define the investment offer(s) as an expected ROI.
Law #6: Distinguish the venture's business concept, distinctive competencies and sustainable competitive advantages.
Law #7: Provide comprehensive statements of opportunities and risks
Law #8: Seek and respond to feedback
Law #9: Elaborate the selected strategy as a set of sub-plans.
Law #10: Convert the selected strategy into a differentiated suite of financial budgets.
Law #11: Re-combine the differentiated budgets into an integrated suite of financial projections.
Law #12: Be able to answer the audience's 'what if' questions in financial terms.

Paradigm Success Rules:
Success Rule #1: Adapt plan length and depth of detail to the interest level and stage of involvement of the target audience.
Success Rule #2: Empower the EBP reader.
Success Rule #3: Create investor confidence by providing flexible credibility.
Success Rule #4: Anticipate and address the target audience's due diligence requirements.
Success Rule #5: Create a value-adding deal structure
Success Rule #6: Employ simulation techniques to obtain the most plausible 'base case' scenario, which can withstand rigorous due diligence investigation.

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