Terminating a Business With Honor and Dignity ©

Arthur Lipper

I gave a talk to the members of the American Assembly Collegiate Schools of Business in 1985 entitled "Why Entrepreneurship Education". I urged that those with entrepreneurial leanings be given tools that will be useful to them. In this talk * I included the following text:

"The entrepreneur frequently has difficulty in understanding opposing views and should be helped by being forced to change perspectives. I believe that there should be mandatory courses offered in "When and how to terminate a business with honor and dignity". Business discontinuances do not have to result in lasting personal tragedies. The course should be mandated as no entrepreneur will believe the course will have any relevance for him."

Since then I have tried and failed to persuade business school deans and academics to create courses helping entrepreneurs to better understand when the odds favor discontinuing the exercise and how to do so with the least harm to all concerned. It is no fun to be in the position of fearing the contents of unopened envelopes or conversations to result from the answering of phones.

The then leading entrepreneurship educator at Harvard leveled with me by saying "I get paid for the number of seats I fill in my classes. How many will sign up for a course on how to fail at business or want an A in the course?" He further suggested that those coming to such a course would do so wearing ski masks to hide their identity.

Of course, one of the problems is that many entrepreneurship education academics are "textsperts" in that they are self-proclaimed experts in that which they have studied, but not personally experienced. This is even more the case in terms of those having successfully terminated a business.

It is generally believed that businesses have to be terminated due to insufficient funding being available. I believe, the absence of necessary funding is more likely the symptom of the failure to correctly predict cash flow and/or commencing the business without

having acquired or be assured of obtaining, at least the minimum predicted necessary amounts before reaching cash flow breakeven from predicted levels of revenues. Due to the normal overly optimistic expectation of timing and amount of revenues and underestimation of time required and costs more than the minimum cash requirement should be assured.

This essay is particularly focused on startup companies, as there is an untempered institutional and social encouragement for the creation of new businesses. The termination of established businesses is in many ways easier as there are more options and yet more difficult for the business owners due to longer term personal and family involvements.

Therefore, I am suggesting that if the business and specifically cash flow planning, something entrepreneurs hate to do, had been more accurate or followed there could be many fewer business startups and terminations.

The area of greatest difficulty is the planning of a business is estimating timing and magnitude of revenues. Profitability can be influenced, if not controlled by cost adjustments but there has to be revenues at levels sufficient to justify the risk and effort. It is amateurish to believe that if or when the product or service is ready for sale there will be buyers. The need and budget for marketing must be included in the cash flow analysis. Also, it must be recognized that the skills necessary in the creation of a product or business are not necessarily the same skills needed to create sales. There are lots of businesses having had good products or services to offer which have had to be sold or terminated as the anticipated revenues never were achieved.

Using royalties, instead of the sale of debt and equities, as a means of financing early stage companies can be better for both the business owners and the investors. The royalty owner gets a percentage of defined revenues and is interested in the company's survival, not its declared profitability or valuation. Of course, the royalty issuing company must have a profit margin sufficient to be able to afford payments coming off the top. It is assumed that in the case of early stage companies there is predicted a substantial profit margin, as why else would the business be attractive to most of those involved. Reviewing the writings at www.Royalties.Website is recommended.

The development of a "Termination Plan" could be constructive if points of possible vulnerability and resulting termination were considered. This will require addressing a number of "what if" questions. These what ifs could include; inability to create proof of concept model within given period, loss of key personnel, competitive product introduction, supplier failure, financing disappointment, regulatory problem, customer commitment disappointment and fire, flood and natural disaster problems.

Once a decision is reached to terminate a business the following groups must be told of the decision and timing. The groups include; employees, those to whom money is owed, investors, suppliers of goods and services, those having bought or indicated an interest in the product, landlord, insurers, etc.

The announcement should be brief, factual and constructive in terms of the quality of the staff and effort. If the business makes sense to be continued if additional funds were available this cold be mentioned.

The reality of business closures is that in retrospect most business owning entrepreneurs would agree that had the decision been reached earlier the loss would have been less and the problems lessened.

Therefore, an analysis as to the reality and cost of the actions, which can be taken re the points of most vulnerability, should be undertaken. Recognizing and planning for the "What Can Go Wrong?" possibilities is a primary job of the early stage company business owner. Many of the problems can be cured with the investment of additional funds and/or delaying planned product offering. All business owners, especially those for early stage companies, must understand that time is the enemy as overheads continue and may even be increased. The replacement of key personnel, including the founding entrepreneur, should also be considered.

My attempt here is not to create the curriculum for a course on "Terminating a Business With Honor and Dignity", though I would be pleased to collaborate in doing so, but to emphasize the need for such a course.

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*** Copies of the 16-page talk text are available.**