Editors' Note
Paul Goodman, CPA, PFCI, and Derrick Myers, CPA, CFP, love a good financial management challenge, however big or small. Send your questions to fmeditor@safnow.org, and we’ll challenge the experts to tackle them in an upcoming article.
Q: How do I know if my business is healthy enough financially to renovate? How do I set a budget for the project?

> In essence, you are asking whether or not you can afford to renovate, and that answer ultimately depends on your access to cash or financing. But let’s start with a basic question: Is your shop profitable? If you are not making a profit, you most likely should not set out on a renovation. Unless you have a rich and generous uncle, you most likely won’t be able to pay for it.

Ask yourself a second question: Are you paying yourself a reasonable salary? That may sound like an odd question that has little to do with renovation. However, it’s all about money. If you have to borrow to do the renovation, the bank is going to want assurances that you can repay the loan. You need to be personally and financially healthy enough that you won’t need to get extra cash (compensation) from the business while it’s trying to pay back a renovation loan.

So, if you are paying yourself a livable wage and the business is profitable, most likely you can consider a renovation project. The next step will determine whether you can afford it. To do that, you need a budget. Begin by setting out the parameters of the project: Are you redesigning your display area or considering a major shop layout/overhaul with new coolers and equipment?

Your budget might be very modest for a display area renovation — something in the range of $3,000 to $5,000. That amount would be easy for any profitable business to swallow. In fact, many would just pay cash and be done with it. However, if you are making major changes and the budget is $100,000 or higher, you will need to take a closer look to see if you can afford it. (Regardless of the scope of the project, get estimates from your suppliers or contractors.)

Take your budgeted amount and subtract any amount of cash you can give to the project. What’s left is what you will need to borrow. Next, you need to figure out what your payment will be and how long it will take you to pay off the loan. You can go to your friendly banker and ask what he or she would do in terms of interest rates and the length of the loan.

Or you can go online and Google a “loan calculator.” With the loan calculator you can vary the interest rate and also vary the length (term) of the loan to see how those variables affect the payment.

Once you have a payment amount, you can determine if it’s affordable. Do you have enough profit from your business to make the payment required? If not, you need to start over and reduce the size of the project. If you can make the payment from your profit, then you’re good to go.

Q: Where can I get financing for my renovation project?

> Of course, the ideal would be to have saved the cash to do the renovation in advance. However, if you are not in that position, you will need to find a lender. The options are your bank, a credit union, a relative or a friend. I highly recommend staying away from relatives and friends — not because they wouldn’t help you, but because borrowing money from them can end up ruining the relationship if you don’t perform as promised. If you do borrow from a relative or friend, be professional about it. Set up and sign a formal loan agreement, and then make the payments on time or early without fail.

If you go to a bank or credit union, they will want to know the answer to one question: How are you going to pay this back? You will need to present them with your income statements for the past few years as well as your current balance sheet. They will be able to quickly assess your ability to repay. They might want you to apply for a government-guaranteed small business loan. If you are approved by the government for the small business loan, the bank will readily loan you the money because it has no risk of nonpayment.

Q: Do some renovation projects have a better return on investment than others?

> Some projects pay for themselves due to energy savings. New coolers, lighting, windows and insulation projects come to mind. You need some upfront cash to get started, and then you begin saving money every month. However, with most renovation projects it’s harder to establish a return. For example, you might be able to bring your design area out into the display area and save money by being more efficient and cutting payroll enough to pay for the project over time. In the end, many projects are just “updating” the shop — making it look better for the customers. Those kinds of projects don’t lend themselves to a return on investment analysis. They are like replacing air conditioners — just a part of running an ongoing business.

Q: If you can fund the project yourself by going “piecemeal,” is that a good idea?

> It certainly is the conservative route and could make sense. However, depending on how big the project ultimately is and what’s involved — demolition, construction, electrical, plumbing, etc. — it mostly likely would be better for you, your employees and your customers to get the project completed as quickly as possible. In fact, if you could wave a magic wand and have the project completed instantly and avoid all the hassles of construction, that would be the best way to go. So, unless you are handy and love DIY projects, you probably don’t want to do it piecemeal. Paul Goodman, CPA, PFCI, is founder of Floral Finance Business Services, based in Tulsa, Okla.; editor of Floral Finance; and author of The Profit-Minded Florist. pgoodman@aol.com