

DRUG STORES  
BUSINESS AND INDUSTRY PROFILE

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DRUG STORES

NOTE: Every effort has been made to ensure that the information contained in this booklet is comprehensive and accurate. However, this guide should only be considered as a reference. Proper legal council and other professional guidance should be obtained prior to starting a business.

DRUG STORES  
(SIC 3912)

GENERAL INDUSTRY INFORMATION

BUSINESS TYPE, INDUSTRY CHARACTERISTICS AND PROSPECTS

## Nature of the Industry

Drug stores have been assigned the Standard Industrial Classification (SIC) Industry Number 5912. These are establishments engaged in the retail sale of prescription drugs, proprietary drugs, and nonprescription medicines. Also, this SIC includes drug stores which can also operate a soda fountain or lunch counter, and may carry a variety of related lines such as cosmetics, toiletries, tobacco, novelty merchandise, and lottery machines in those states with lotteries.

Corporations dominate in the retail pharmaceutical industry, with 76 percent of total firms being incorporated. Single proprietorships account for 20 percent while partnerships represent 4 percent. From 1976 to 1986, independent stores witnessed sales growth of 75 percent over the ten year period 1976-1986 (about a 6.4 percent annual rate). The large chains grew much faster in this period than the independents, increasing their share of the market from 45 percent to 60 percent, with sales growth of over 200 percent or nearly three times the rate of sales growth shown by independents.

## Nature of Business

Obviously, the prescription department is the profit core and center of business of the drug store. The prescription department ranks as one of the most profitable sections in the pharmacy and has a significant influence on other department sales. The pharmacist should, therefore, concentrate on making this department the central focus of the drug store. Other merchandise may be carried based upon clients' needs and what the drug store's competition is offering.

A broad line of merchandise may be carried to appeal to a wide range of shoppers. Some of the items generally carried by a drug store include: cosmetics/fragrances, cigarettes and cigars, small art and crafts items, hair care/skin care products, magazines/books, film/film developing, vitamins, greeting cards, batteries, disposable diapers, blank videotapes, oral hygiene products, contact lens solutions, diet aids, pet food, and candy. Some drug stores have added a cooler with beverages and snack foods.

The following products generate more than 5 percent of average total sales per store:

DEPARTMENT	PERCENT	GROSS
Prescriptions	27.2%	35-40%
Drugs/proprietarys	14.5	30-35

Toiletries	10.8	25-30
Tobacco	7.5	15-20
Housewares	6.7	35-45
Cosmetics	5.3	35-40
Other (stationery, candy, toys, general merchandise, grocery, liquor, miscellaneous)		15-45%

In 1987, according to the business census, 33,456 drug stores with 52,200 outlets operated in this industry. Thirty percent were very small, with annual sales of up to \$500,000 and a workforce of from one to four employees. Approximately 65 percent of the drug stores operated as single units. In 1987, several drug store chains had several hundred different outlets. The mean sales per store was slightly above \$1 million; the average number of workers per unit was about 11, and salaries were about 12 percent of sales. In 1987, the number of drug store employees totaled 555,520 people, receiving an average salary of \$9,335. Salaries of people working in a drug store, however, may vary widely, ranging from the salary paid to a licensed pharmacist to just above minimum wage paid to a general clerk or cashier. Salaries ranged from 15 to 16 percent of sales at the smaller stores and as low as 9 to 10 percent at the large chains.

#### Growth Potential

Prospects for growth in the future decade are mixed. There is likely to be a growing demand for certain products while other product lines may shrink due to changing demographics. The population in the U.S. is aging; thus, sales of prescriptions and proprietary drugs are likely to increase. However, the older population spends fewer dollars on cosmetics and beauty aids, so there may be some sales shrinkage in this area. Diversification of product lines and general merchandise geared toward customer needs and volume business may hold the brightest future for the independent drug store.

#### Level of Competition

Beginning with the early 1980's, the retail drug market became more competitive. That is, large supermarkets began to stock a wider range of household items, beauty aids, and proprietary drugs. Some supermarkets even installed their own pharmacy. The combination store (roughly one and one-half times the size of a supermarket) began to appear, offering the combined products usually carried by a supermarket, a drug store, and a dry goods store. Moreover, K-Mart, Wal Mart, and other expansion-minded discount or department stores began to promote these product lines more vigorously.

Health maintenance organizations sometimes install their own

pharmacies at hospitals and clinics. Thus, the squeeze has been felt by the independent drug stores, many of which liquidated in recent years. The liquidation rate in this industry is about 4.5 percent yearly, somewhat higher than the rate of formations, indicating a growing degree of competition.

Total sales of products generally carried by drug stores should continue to rise by 1 to 2 percent annually above the level of price inflation, but profit margins are likely to be squeezed as more generic drugs flood the market and as more price discounters expand their sales. Large chain that are open virtually around the clock are likely to continue to expand their sales, while sales for many of the independents will stagnate.

#### MARKET OPPORTUNITIES IN VARIOUS SIZED COMMUNITIES

##### Marketing Plan

Before starting a drug store, the owner(s) should develop a marketing plan. A marketing plan is basically a blueprint for the business and should include important information about the venture. Topics that should be addressed include: whether or not the area can support the proposed venture; the existence of an unidentified market niche that may be exploited; the level of competition in the area; the current customer base population, income, and growth trends; competitive pricing strategies; and a variety of other facets of the business that owners and managers need to know to develop a viable and profitable business.

Assistance in developing a marketing plan can be obtained from many sources -- some at cost, others for free. A few sources for assistance and information are local chambers of commerce, banks, accounting firms, local and state governments, the Illinois Department of Commerce and Community Affairs (DCCA), the U.S. Small Business Administration (SBA), colleges and universities (through business management programs or Small Business Development Centers), private consultants, and public libraries. Existing drug stores may be contacted to determine what services they offer and what they charge. Also, check with drug wholesalers who may provide assistance in appraising potential locations and sites.

##### Market Data

To determine the market potential and to acquire demographic data (e.g., average household income, number of households, and number of businesses), contact the local chamber of commerce, public library or city and county governments. Prospects for the success of a drug store are good in communities with a growing population, either in the very young category (0 to 5 years) or by the group nearing or at retirement age.

During the 1980's, competition in the drug and beauty aid business from supermarkets stifled the growth of drug stores in many small communities. In 1987, a population of approximately 4,800 supported an individual drug store. Two small cities of 2,000 to 3,000 should jointly support one drug store or its equivalent in a supermarket.

Sales will be greater for a drug store operating in a mall or near a hospital or group of physicians' offices, as it will receive a large number of walk-in patrons or shoppers for prescription drugs. Services can increase sales if other drug stores do not offer the same convenience. Free delivery service should be offered at a minimum to shut-in or handicapped patients. A five to ten mile radius for deliveries is common.

## FRANCHISING

### Franchising Opportunities

Franchise opportunities exist for drug stores and offer an alternative to starting a business from the ground up. Franchising gives the entrepreneur an opportunity to use the mass buying power, training programs, specific territory, experience, and name recognition of the franchisor to build a viable and profitable business. The Source Book of Franchise Opportunities, by Robert E. Bond, is one of several reference books that lists information on franchise opportunities, fees and investment requirements.

Several of the large drug store chains boast annual sales in excess of \$1.5 billion. This is possible because of the large number of stores they operate. The five largest chains in 1986 were as follows:

FRANCHISE/HEADQUARTERS	(millions)	STORES
Walgreen's (Deerfield, IL)	\$3,390	1,183
American Stores (Salt Lake City)	\$2,900	529
Revco (Twinsburg, OH)	\$2,650	2,003
Jack Eckerd (Clearwater, FL)	\$2,540	1,588
Rite Aid (Shiremanstown, PA)	\$1,560	1,392

Most of the franchising firms provide training at their home offices for key officers of franchisee businesses. Video cassettes may be provided that illustrate correct techniques for performing certain types of assignments. Ongoing training also should be provided, especially as new equipment or improved service products are acquired.

### Franchising Costs

Some franchisors may require that an annual fee or percentage of sales be paid by the franchisee. A representative list of franchises in the drug store industry, including the franchise fee, capital requirements, and training provided in the late 1980's are as follows:

NAME OF FIRM	FRANSHISE FEE/CAPITAL	TRAINING
Drug Castle	\$25,000/\$200,000	4 weeks
Drug Emporium	25,000/ 700,000	6 weeks
Health Mart	5,000/ N/A	1 week
Medicap Pharmacy	15,000/ 30,000	3 days
Medicine Shoppe	18,000/ 29,000	1 week

#### COSTS/FINANCIAL CONSIDERATIONS

##### COSTS AND TYPES OF ASSETS NEEDED TO START A BUSINESS

###### Initial Investment Considerations

Initial investment factors to consider include: How much capital is required to operate the business until the break-even point is reached? How much will be needed for wages, six months of working capital, unforeseen expenses, and supplies and equipment inventory? What types of insurance coverage are necessary and what will they cost? How much will building, remodeling or improvements cost?

Starting a drug store can be expensive. As a rough guide, a capital investment of at least \$2 for every \$5 in estimated annual sales should be anticipated. While the drug store is not a capital intensive business, nor a labor intensive one, substantial amounts of money must be invested into store shelving, equipment, and inventory items.

Many of the smaller stores are operated out of leased facilities, but monies might be needed for leasehold improvements of older structures and for adding needed shelving and other equipment.

The owner/manager of a drug store is, almost without exception, a licensed pharmacist. Some stores are open from 8:30 a.m. to 5:30 p.m. and are staffed by the owner/pharmacist and at least one or two other clerks. A trained, licensed pharmacist should earn about \$30,000 to \$40,000 annually. One trade digest suggests that the employment of a full-time pharmacist must be supported by a sales activity of 80 prescriptions per day. The general clerks in the store may: earn from \$8,000 to \$12,000 annually, depending upon their experience and job assignments.

In a larger store, and one that remains open for more hours, an additional pharmacist will usually be employed, as well as one or two additional clerks and an office worker to handle correspondence, charges (Visa, Mastercard, insurance billings), accounting, inventory control, and supply orders.

#### Average Expenses

The Almanac of Business and Industrial Financial Ratios provides operating expense breakdowns for corporations using IRS published data. The following expenses for drug stores, broken down as a percentage of revenues, were provided in 1987 for firms with under \$100,000 in assets and for those with assets ranging from \$100,000 to \$250,000.

EXPENSE ITEM	COMPANIES	
	WITH ASSETS OF UNDER \$100,000	WITH ASSETS OF \$100,000 - \$250,000
Cost of Operations	66.8%	67.8%
Compensation of officers	9.7	5.8
Repairs	0.2	0.3
Bad debts	0.1	0.2
Rent on business property	2.1	2.8
Taxes (except federal taxes)	1.8	1.9
Interest	0.4	0.7
Depreciation/amortization	1.1	1.3
Advertising	0.6	0.8
Pension/benefit plans	1.2	0.6
Other expenses	13.1	15.6
Net profit before taxes	2.9%	2.2%

#### Average Balance Sheet

For the independent drug store, nearly one-half of the gross profits go toward paying officers' compensation or employees' salaries, including fringe benefits. Items that require about 5 to 6 percent of sales include advertising and rent.

The breakdown of assets, liabilities, and net worth for a drug store, according to Dun and Bradstreet, was as follows:

ASSETS		DEBTS AND NET WORTH	
Cash and near cash	10.4%	Accounts Payable	16.2%
Accounts receivable	13.1	Bank loans	4.7
Notes receivable	0.4	Other notes payable	0.0
Inventories	51.3	Other current debts	10.1
Other current assets	2.7	Total current debts	31.0
Total current assets	77.9	Other long-term debts	16.0

Fixed assets	10.5	Deferred credits	0.0
Other noncurrent assets	11.6	Net worth	53.0
Total assets	100.0%	Total debts/net worth	100.0%

"Near cash" refers to checking or savings accounts that may be liquidated easily to cash. "Other noncurrent assets" generally refers to intangible assets such as leaseholds or leasehold improvements. "Fixed assets" are a mixture of land and buildings, equipment, and delivery vehicles. "Accounts payable" are amounts owed to suppliers of inventories and equipment. "Bank loans" are amounts owed to suppliers of open market notes or equipment installment notes. "Other long-term debts" include both equipment and mortgage notes.

#### TYPICAL BUSINESS RATIOS FOR OTHER FIRMS IN THE INDUSTRY

The comparison of actual operations with typical, industry-wide ratios is frequently helpful in making decisions concerning service charges, budgeting, and realistic profit expectations. These ratios are also helpful in preparing projected financial statements (cash flow projections, income statements, and balance sheets) for loan purposes.

According to Dun and Bradstreet, the median key financial ratios for drug stores, during 1986, were as follows:

#### Solvency Ratios

Quick ratio (cash plus accounts receivable/current liabilities)	0.8 to 1
Current ratio (current assets/current liabilities)	2.9 to 1
Total debts to net worth	63.8%

The quick ratio expresses the degree to which a company's current obligation (expenses) are covered by the most liquid current assets (cash and customer payments due the company). Generally, larger ratios are preferable and any value of less than one to one implies a dependency on inventory or other physical assets to liquidate short-term expenses. The current ratio is a rough indication of "cushion" between current obligations and a firm's ability to pay them from current assets. Total debts to net worth compares total liabilities in the form of debt with owners equity, which for small firms usually does not exceed 100 percent. Thus, owners have more at stake than creditors.

#### Efficiency Ratios

Collection period (accounts receivable/sales x 365)	14.6 days
Sales to inventory (net sales/inventory)	6.3 times

Assets to sales (total assets/annual net sales) 31.4%

The quality of the receivables (degree to which customers pay their bills on time) of a company can be determined through the collection periods. When comparing the collection period of one concern with that of another or comparing against industry norm, allowances should be made for possible variations in selling terms. The sales to inventory relationship is a guide to the rapidity at which merchandise is being moved, which has a direct effect on the flow of funds into the business. The assets to sales ratio ties in sales and the total investment that is used to generate those sales. By comparing a company's assets to sales ratio with industry norms, it can be determined whether a firm is overtrading (handling an excessive volume of sales in relation to investment) or undertrading (not generating sufficient sales to warrant the assets invested).

#### Profitability Ratios

Return on sales (profit after tax/annual net sales) 4.2%  
Return on net worth (profit after taxes/net worth) 16.9%

Return on sales reveals the profits earned per dollar of sales and, therefore, measures the efficiency of the operation, and is an indicator of the firm's ability to withstand adverse conditions such as falling prices, rising costs and declining sales. Return on net worth (return on equity) is used to analyze the ability of the firm's management to realize an adequate return on the capital invested by the owners of the firm. Generally, a relationship of at least 10 percent is regarded as a desirable objective for providing dividends plus funds for future growth.

### MANAGEMENT CONSIDERATIONS

#### DEVELOPMENT AND SITE LOCATION

##### Zoning

When selecting a location and a specific site for the business, consideration must be given to local zoning requirements. Many communities forbid, through zoning ordinances, the establishment of home-based businesses. It is essential to check these local restrictions prior to contracting to rent, lease or buy a property for the business.

##### Other Considerations

Other considerations in locating the business are health and

safety requirements (Occupational Safety and Health Administration); the physical size of the operation; adequate storage space with proper ventilation and fire extinguishing systems in place; fire, electrical and safety codes; expected traffic patterns; and sign restrictions. Adequate parking for service vehicles and workers' and clients' cars is essential.

### Design and Layout

The smallest of the drug store groups is the traditional independent, which, in the latter 1980's, customarily had about 4,000 square feet of space and generated about \$600,000 in annual sales. As much shelf information as possible should be displayed. This helps sell items to browsing patrons or to customers that are waiting for prescriptions to be filled. Two examples are: the daily requirements for vitamins and minerals, and a comprehensive display of correct dietary needs (e.g., protein, carbohydrates, and calories). The promotional chain drug store is generally twice as large in terms of square feet (about 8,000) and has annual sales of about \$2 million. A supermarket usually devotes substantial space to the items carried by drug stores (such as drugs, beauty aids, and housewares) and normally has a store size of about 20,000 square feet. The combination stores commonly called "combos," are about 30,000 square feet in size and boast a combination of a complete supermarket, a complete pharmacy, and a dry goods store. Shoppers are able to complete more of their shopping with one stop. Many of the combos remain open 24 hours a day in order to appeal to late night shoppers. For those stores with limited hours, a telephone number is frequently posted for customers who require emergency service after the store closes. Ample, nearby, well-lit parking is imperative.

### Location

The two most important considerations for location are heavy customer traffic and minimum competition. As with most other retail establishments, convenience has become the key word. That is, the more a store is a one-stop shopping center for its customers and provides services that save time, the better its chances for survival. Some drug stores have increased their sales by locating in a strip mall near convenience stores, hardware stores, restaurants, liquor-stores, dry cleaning and laundromat facilities. It has become increasingly difficult for a drug store to remain profitable in a stand-alone site unless it is near a great deal of health care related business, such as a hospital, a nursing home, or a health care complex.

### EXPERIENCE AND TRAINING NEEDS

### Management/Owner Training

Generally, a pharmacist has to complete a five-year pharmacy course and a lengthy internship program to be licensed. However, most pharmacists lack sufficient business training in regard to store operations.

Training for management should cover the "how to" of the business, including general management, marketing, inventory control, financial, record keeping and accounting areas. Attention should be given to the philosophy of the business (e.g., growth possibilities, avoiding legal and business risks), as well as to front office administration. Training in these areas can be obtained through regional small business development centers which offer self-employment training programs. The pharmacists usually attend seminars provided by large, national pharmaceutical companies introducing them to new drugs on the market. Some attend conventions one or two times per year and subscribe to trade journals and periodicals in order to remain current in their field.

#### Employee Training

Essential to the success of the business are well-trained and courteous employees. A training program might include retail selling techniques, store etiquette, inventory and stock control, display arrangement and new product knowledge. Clerks may be experienced in performing some duties expected of them when hired, while others may be teamed with experienced employees to receive on-the-job training. Updates on taxes, insurance coverage, and health care are also important training opportunities for the drug store owner and staff. An important consideration in hiring is thorough checking of employee references since drug stores maintain stocks of narcotics and drugs. All employees should be provided with a written job description detailing specific duties and responsibilities, and the owner, manager and employees should understand the contents. The employees should also be advised of promotion opportunities, overtime practices and other compensation available.

#### KEYS TO SUCCESSFUL MANAGEMENT

##### Business Methods

In order to be successful, the management of a drug store must know its competition, have a vision as to the markets that it can cultivate, promote a helpful atmosphere for both clients and employees, and strive for profitable accounts and customers.

Management of a drug store should be able to gauge the approximate saturation point in a given market area. Markets should be developed where growth potential exists and where the firm has a

price or some other advantage. Effective labor, supplies, and operating cost controls should be followed by the owners and employees. By combining reliable professional service and responsive product offerings to meet customer health care needs, independent drug stores can expect to maintain a position of profitability. Those drug stores that can be flexible to meet changing customer attitudes will continue to fill a vital need within their community.

Potential customers must be attracted to the store and then enticed to buy the offered merchandise. Promotion in the drug store business is very important. The store front should be neat and appealing, while the inside should be clean, white, and "hospital-like" in appearance. Signs may indicate specials for the week. Generally, the prescription department should be elevated and in the rear of side of the store so customers pass other merchandise to get to the counter.

The firm's operating objective should be to develop a good reputation in the industry for quality pharmaceuticals and goods at a fair price.

#### Advertising and Promotions

Annual expenditures for advertising should be about 4 percent of sales. New businesses should expect this to be 6 percent to build up a clientele.

Spot radio ads, newspaper ads, telephone directory yellow pages listings, and direct contact (telephone or mailings) are some methods of advertising drug stores. Delivery vans often bear company logos and a brief listing of services offered on their sides, along with a business telephone number. Billboards are used by some firms in the industry. Check with drug suppliers and product manufacturers for free enclosures, ready-made ads, mailing pieces and other assistance to complete an ad campaign and save money.

### GENERAL START-UP ISSUES

#### FINANCING METHODS

The ability to raise initial capital is critical for business start-ups. According to a survey conducted by Western Illinois University, one-half of entrepreneurs reported difficulties in obtaining financing, including both initial and working capital. The survey also found that entrepreneurs relied heavily on personal funds, in addition to investments from family and friends. In fact, the survey indicated that approximately one-half of initial funds came from these sources. On the average, bank

loans accounted for nearly one-third of initial capital. Other private lenders, government agencies, venture capital and stock placements only rarely provided initial capital for businesses.

About one-half of both goods and service-producing firms surveyed had applied to lending institutions for credit. Only 5 percent of goods-producing firms had been denied credit more than once, while approximately 18 percent of service-producing firms reported credit denials. The most frequent reasons for credit denial included lack of adequate collateral and a policy of not lending to the typed of business applying for credit. Since obtaining credit is difficult, many entrepreneurs find it necessary to finance a business through a combination of sources of funds. Following are descriptions of several common types of financing.

### Equity Sources

Equity sources of funds are the entrepreneur's personal funds or assets or the funds or assets of other investors in the business. Banks often require a minimum equity investment of 20 to 25 percent.

Personal Savings or Insurance -- Individuals with bank passbooks, certificates of deposit, U.S. savings bonds, permanent life insurance (with a cash surrender value), or other savings should view these as a source of financing. Conversion of these savings (or borrowing funds using these savings as collateral) should be explored carefully to determine the effect on the family if funds are not repaid.

Personal or Family Investors -- Next to personal assets, this is the most commonly used source of equity financing and perhaps the one source most abused. A business owner who secures equity funds from family members or friends should enter the relationship on a strictly professional business basis. Potential family conflicts which might result from the business might be avoided by preparing a simple contract to designate the details of the business arrangement.

Personal Assets -- An individual may have accumulated some equity in personal assets such as a vacation home, a second vehicle, or recreation equipment such as a boat, camper, etc. People starting a new business and trying to finance the business could sell these assets to generate funds to capitalize the business. This offers the advantage of not having loan debt to repay during the early years of a business and also shows potential investors and lenders the commitment of the owner.

### Debt Financing

Entrepreneurs should be aware of typical lending practices, sources of funds and different types of credit (and their respective costs) before approaching lending sources.

Institutional Investors -- Banks, savings and loans, and commercial credit companies expect the small business owner to make a significant personal investment (equity) in the business prior to any lending activity. The lack of personal investment is viewed as a sign of greater risk and less commitment on the part of the owner. Smaller loans can sometimes be obtained through a bank's consumer loan division. Security in the form of a second mortgage on the borrower's house or a lien on property such as auto is usually required.

Leasing Agents -- Leasing companies allow small start-up firms to obtain needed equipment with a small cash down payment and regular monthly payments. Leasing has advantages and disadvantages both for the leasing agent and the small business that rents equipment. Leasing companies may be able to use favorable federal tax advantages (such as depreciation allowances), and thus lease terms are often only slightly higher than if the asset were financed with a bank note. However, if the lease is an operating contract (not a lease to purchase), the leasing company retains ownership.

Trade Credit -- Although it is often overlooked, trade credit is a frequently used means of debt financing. Trade credit is extended from suppliers who accept deferred, rather than immediate, cash payment. Trade credit conceivably could be generous enough to allow use or resale of the product, so that the customer's cash can be used to pay the supplier.

#### Public Sources

Public sources of funds include federal, state or local governments which may loan money to small or emerging businesses at relatively low rates of interest as a method to improve the economy. Public sources also generally take a second position on the collateral so that the bank has first claim to the assets if the loan defaults. Although public funds have their limitations, entrepreneurs should explore such funds. Most public sources of funds require 20 to 25 percent owner equity, additional private bank financing, and some guarantee that job creation will occur.

Federal Sources -- An example of a public source of funds is the U.S. Small Business Administration (SBA), which offers a variety of loan programs to eligible existing and start-up small businesses which cannot borrow on reasonable terms from conventional lenders without government assistance.

Local Revolving Funds -- Many communities in Illinois use

available economic development funds to establish revolving loan pools to promote business and industrial growth.

State Loans -- The Illinois Department of Commerce and Community Affairs offers several important financing programs to help start-up businesses. Each of these should be considered, along with their associated requirements. For more information on financing programs, contact the Illinois Small Business Hotline at 1-800-252-2923.

#### FORM OF ORGANIZATION

There are three basic forms of business organization, each of which offers distinct advantages and disadvantages for a prospective business owner. The main considerations in selecting a form of organization include:

- Cost and complexity of formation;
- Tax and securities law implications;
- Need for attracting additional capital;
- Investor's liability for debt and taxes; and
- The goals and purpose of the enterprise.

Each of these should be thoroughly discussed with an attorney and an accountant prior to selecting one of the following forms of business.

Sole Proprietorship -- A sole proprietorship is owned and operated by an individual. Advantages of this form of organization include ease of formation and relative freedom from government controls and restrictions. Disadvantages include less access to capital and financial resources. Also, this form of business organization provides less protection with regard to personal liability. For instance, the owner may be required to sell personal property, including home, car, etc., to repay debts resulting from the business.

Partnership -- Generally, a partnership is defined as two or more individuals carrying on an association as co-owners of a business for profit. Typical partnership agreements are in writing and are prepared by an attorney. The agreement defines how much owner equity each partner must contribute, the extent to which each partner will work in the company and the share of the profits or losses to be received by each of them. It is desirable to have the agreement prepared by an attorney. As with sole proprietorship, a general partnership exposes the owners to personal liability. If the business is not successful and the partnership cannot pay all it owes, the general partners may be required to do so using their personal assets. Limited partners are exposed only to the extent of their investment in the

partnership.

Corporation -- A corporation is a distinct legal entity and is the most complex form of organization. A corporation may sell shares of stock, which are certificates indicating ownership, to as many people as is desirable. The shareholders then elect a board of directors, which selects a president and other officers who run the company on a day-to-day basis. Among the advantages of corporate formation are limited liability of the shareholder and ease of transferring ownership. Electing S Corporation status is another option when starting a business. In general, an S Corporation does not pay a tax on its income. Instead, the income and expenses of the corporation are divided among its shareholders, who then report this data on their own income tax returns. To qualify for S Corporation status, a corporation must meet several requirements, one of which limits the number of shareholders to 35. All shareholders must also consent to the S Corporation status.

For further information regarding S Corporations, contact the Internal Revenue Service (IRS) at 1-800-424-1040 or request a copy of Publication 589, Tax Information on S Corporations, by calling 1-800-424-3676.

#### LICENSING/REGISTRATION

Illinois Licensing Requirements -- To operate a drug store in Illinois, a beginning pharmacist must take an examination and orientation session with a required fee of \$35 (\$200 for pharmacists educated outside of or relocating to Illinois) to obtain a Pharmacist License. This license must be renewed every two years with a \$70 renewal fee. The business must also be registered and licensed. This consists of a \$100 one-time registration fee for a Pharmacy License, which then must be renewed every two years for \$200. A renewable \$5 controlled substance registration is also required. For more information, contact the Illinois Department of Professional Regulation at 320 W. Washington, Springfield, IL 62786, or call 217-782-8556.

Assumed Names Act -- Once a decision has been made regarding the form of organization for the business, it must be registered to legally conduct business in Illinois. Under the Illinois Assumed Name Act, sole proprietorships and partnerships must register with the county clerk if the name of the business will operate under a name other than the owner's full legal name (e.g., "John Doe" would not need to file; "John Doe's Cleaners" would). Limited partnerships and corporations are required to register with the Illinois Secretary of State's Office. More detailed information on business registration is contained in the "Starting a Small Business in Illinois" handbook, which can be obtained by

contacting the Department of Commerce and Community Affairs' Small Business Hotline at 1-800-252-2923.

Certificate of Registration -- Most businesses must register with the appropriate state agency to submit tax or informational returns or to collect and remit sales taxes. In Illinois, business owners must contact the Department of Revenue to determine if an Illinois Business Taxpayer Certificate of Registration (Business Tax Number) is required for the business. Contact the Department of Revenue at either of the addresses listed under Information Sources.

Unemployment Insurance Liability -- Businesses that hire employees may be required to make unemployment insurance contributions to the state. Liability is determined by the Illinois Department of Employment Security (DES). The form, "Report to Determine Liability," and instructions for completion are available through the Small Business Hotline or by contacting either of the DES offices listed under Information Sources.

Local Regulations -- Most local jurisdictions require that business operation licenses be applied for and renewed annually. Where crowds of people are in attendance, fire codes concerning rest rooms and fire exits are in effect. Fire and safety inspections may be made periodically by the local fire and safety inspector. Contact the city or county clerk for information on licensing, inspections, sign restrictions, and other local regulations.

Federal Employer Identification Number (FEIN) -- Every partnership, corporation and S Corporation must have a FEIN to use as its taxpayer identification number. A sole proprietorship must also have a FEIN, if it pays wages to one or more employees or files any excise tax returns, including those for alcohol, tobacco or firearms. (Otherwise, a sole proprietor can use his or her social security number as a business taxpayer identification number.) To apply for a FEIN, use form SS-4, Application for Federal Employer Identification Number. To receive a FEIN application, contact the Internal Revenue Service (IRS) Hotline at 1-800-424-3646. The application is also included in the "One Stop Business Start-Up Kit" and can be obtained by calling the Illinois Small Business Hotline at 1-800-252-2923.

## TAXES

Taxation for small businesses can be quite simple or very complex, depending on the size and type of operation. The following list outlines the major taxes which may impact a business. Of course, the tax liability of each business will be different, based on sales volume, form of organization, etc.

## Business Taxation

Income Tax -- Every individual, corporation, trust, and estate residing in Illinois or earning or receiving income in Illinois must pay an income tax based on net income. A sole proprietor must pay individual income taxes on earnings from the business. In a partnership, each partner must pay taxes on the distributive share of partnership income. Corporations must pay a corporate income tax.

Franchise Fees -- In addition, corporations are assessed a franchise tax each year. Corporate franchise taxes are administered and collected by the Secretary of State's Office.

Replacement Tax -- Illinois does not have a personal property tax, but does have a personal property replacement income tax. The replacement tax is also applied to the net income of partnerships, corporations, and trusts. S Corporations are subject only to replacement tax.

## Sales Taxes

Four categories of taxes comprise the state and local sales taxes. These are the Retailers' Occupation Tax, the Use Tax, the Service Occupation Tax and the Service Use Tax. State, county and municipal governments, and certain mass transit districts may levy Retailers' Occupation, Use and Service Occupation taxes, subject to criteria and rate limits established by Illinois law. Additional information regarding the various types of sales taxes may be obtained by contacting the Illinois Department of Revenue at 217-782-2972 or 1-800-732-8866.

A list of items which are exempt from Illinois Sales Tax is contained in "Starting a Small Business in Illinois," which can be obtained through the Illinois Small Business Hotline at 1-800-252-2923. For further information on Sales Tax regulations or the "Illinois Retailers' Tax Booklet" (NUC-19), contact the Department of Revenue at 217-782-2972 or 1-800-732-8866.

## Real Estate Taxes

All for-profit real estate owners are required to pay property taxes. The property tax rate is determined by local taxing districts and taxes are paid to the township or county tax collector in the year following assessment.

## Withholding Taxes

Certain taxes, including state and federal income taxes and FICA

(Social Security), must be withheld from employee wages and remitted to the government. You may be required to register with both the federal government and the State of Illinois for tax withholding purposes.

Federal Withholding -- To register with the federal government, contact the Internal Revenue Service at 1-800-424-3676 and request: "Your Business Tax Kit" (YBTK) for either a sole proprietorship, partnership or corporation; "Tax Guide for Small Business" (Publication 334); and "Employer's Tax Guide" (Publication 15).

State Withholding -- To register with the State of Illinois, contact the Illinois Department of Revenue Hotline at 1-800-732-8866, or write to the department at:

100 W. Randolph, Concourse 300  
Chicago, Illinois 60601  
312-814-5258

101 West Jefferson Street  
Springfield, Illinois 62794  
217-785-3707

## BUSINESS SERVICES

### Legal Counsel

Attorneys can provide services fundamental to the success of the business. A competent attorney can advise on such issues as choosing the most appropriate type of business organization; complying with local, state and federal regulations; obtaining licenses and permits; preparing contracts; and resolving tax questions.

Attorneys also can provide professional help when dealing with other parties such as financial institutions, owners of possible business locations, union officials, governmental bodies, franchising companies, suppliers and customers. In addition, problems may arise requiring the services of an attorney, including collection problems with customers, disputes with creditors or employees, or expansion opportunities.

There are several methods for selecting an attorney. An initial course of action might be to seek recommendations from other business owners. Another method of finding an attorney is to contact the Illinois State Bar Association Lawyer Referral Service at 1-800-252-8916. The Martindale-Hubbel Law Directory may also be helpful. It contains a listing and rating of attorneys in your city; a copy may be found at the local library. The public library is also a source for reference books on legal topics. One such book is Small Business Legal Advisor by William A. Hancock, published by McGraw-Hill.

## Bookkeeping

Access to proper information is provided by a sound bookkeeping system. Functions of a good system include:

Receipts and Expenses -- Creating and maintaining an accounting system for the accurate and timely recording of the company's cash receipts, disbursements, sales and operating expenses.

Financial Statements -- Preparing periodic financial statements (balance sheet and profit and loss statement) and establishing systems that track accounts receivable and payments due.

These responsibilities may be undertaken from within or outside of the business, depending on the size and nature of the business and the owner's experience and available time. An accountant, attorney or banker can help determine firm's need for a bookkeeper or bookkeeping service.

## Accounting

In addition to bookkeeping requirements, a need may arise for the services of a certified public accountant (CPA), an accountant who has passed a written examination prepared by the American Institute of Certified Public Accountants and who has received a state license for the public practice of accountancy. Most CPAs provide the following services:

Auditing -- Although a bookkeeper employed by the firm may maintain accounting records and prepare financial statements, banks and other lenders frequently require an independent audit prior to granting a loan and during the loan repayment period.

Tax Preparation -- The tax services provided by CPAs include planning transactions for the lowest present and future tax liabilities, preparation of tax returns, conferences with taxing authorities who are examining prior years' tax returns and estate planning.

Consulting -- Some CPAs provide assistance in reducing costs, improving reports, installing or upgrading accounting systems, budgeting and forecasting, conducting financial analyses, controlling production, controlling quality, compensating personnel, and managing records.

The Independent Accountants Association of Illinois (IAAI), established in 1949, can refer a competent accountant to the potential Illinois small business person. Many of the IAAI accountants are "Enrolled Agents," licensed to represent a client before the IRS should the client's tax return be audited. For more information, write the Independent Accountants Association of

Illinois, P.O. Box 1506, Galesburg, Illinois 61402, or call 309-342-5400.

### Insurance Coverage

A well-planned insurance program is essential for protecting a business from unforeseen losses and significant financial burdens. In organizing an insurance program, there are three basic considerations: recognize the perils facing the business and the potential loss from each; investigate the methods by which the cost of coverage can be reduced, which includes "shopping" for appropriate insurance plans; and prepare an insurance plan that is compatible with the operation and goals of the business. A qualified insurance agency or broker can explain options, recommend the best coverage and help save money.

Four types of insurance coverage are essential: fire, liability, vehicle and workers' compensation. Other desirable types of insurance coverage include business interruption, crime, and key employee.

### INFORMATION SOURCES

There are a variety of resources available to assist with starting a business. Local libraries, chambers of commerce, community colleges, and universities are excellent sources of information.

Several sources of information are useful for improving the level of profitability of a drug store or for learning more about this type of operation. These include trade associations, reference books and directories, periodicals, ratio studies, investment services, and government assistance. A list of these for this industry is given below.

#### SMALL BUSINESS HOTLINE

In Illinois, many of the forms needed to start a business may be obtained from the Illinois Small Business Hotline, a program of the Illinois Department of Commerce and Community Affairs' Small Business Assistance Bureau. State business forms, permit and license information, and general business information, such as the "Starting a Small Business In Illinois Handbook," are available from the Small Business Hotline at 1-800-252-2923.

#### BUSINESS DEVELOPMENT CENTER NETWORK

The Illinois Business Development Center Network and Service Corps of Retired Executives (SCORE) offices can provide technical

assistance, business plan development, finance, marketing, management, international trade, government procurement, energy management, and commercialization of technology-related products. Additional information on these services is available through the Small Business Hotline.

#### SMALL BUSINESS RESOURCE CENTER

The Small Business Resource Center is a Chicago-based center that provides information on area Small Business Development Centers and other state and local service providers. Contact the Small Business Hotline for more information.

The U.S. Small Business Administration offers many publications for a minimum fee. A list of these management aids is available from the Small Business Hotline.

Several sources of information are useful for improving the level of profitability of a drug store firm or for learning more about this type of operation. These include trade associations, directories and reference books, periodicals, financial ratios, and government publications/assistance. A list of these for the drug store industry is given below.

#### TRADE ASSOCIATIONS

Associated Chain Drug Stores. 212 Fifth Avenue, New York, NY 10010. 212-689-4690.

Illinois Pharmaceutical Association. 223 West Jackson, Suite 1000, Chicago, IL 60606. 312-939-7300.

National Association of Chain Drug Stores. 413 North Lee Street, Alexandria, VA 22314. 703-549-3000.

National Association of Retail Druggists. 1750 K Street, N.W., Suite 1200, Washington, DC 20006. 202-347-7495.

National Wholesale Druggist's Association. P.O. Box 238, 105 Oronoco Street, Alexandria, VA 22313. 703-684-6400.

#### DIRECTORIES AND REFERENCE

American Druggist Blue Book. Hearst Corporation, 224 West 57th Street, New York, NY 10019. 212-262-5700.

Chain Drug Stores. Chain Store Guide, Two Park Avenue, New York, NY 10016. 212-371-9400.

Drug and Cosmetic Catalog. Harcourt Brace Jovanovich, Inc., 757 Third Avenue, New York, NY 10017. 212-888-2130.

Drug Topics Red Book. Medical Economics Company, Inc., 680 Kinderkamack Road, Oradell, NJ 07649. 201-262-3030.

Maintaining Profits in a Highly Competitive Market, Merchandising Alert Annual NARD Employee Training Manual. National Association of Retail Druggists, 1750 K. Street, N.W., Washington, DC 20006. 202-347-7495.

Modern Drug Store Merchandising: How to Increase Our Sales and Profits, Coleman, Thomas E., 1975, Lebhar-Freidman Publications, Inc., 425 Park Avenue, New York, NY 10022. 212-371-9400.

#### PERIODICALS

American Druggist. Hearst Corporation, 224 West 57th Street, New York, NY 10019. 212-262-5700.

American Pharmacy. American Pharmaceutical Association, 2215 Constitution Avenue, N.W., Washington, DC 20037. 202-628-4410.

Beauty Fashion. Beauty Fashion, Inc., 48 East 43rd Street, New York, NY 10017. 212-687-6190.

Chain Drug Review. Racher Press, Inc., One Park Avenue, New York, NY 10016. 212-889-8741.

Cosmetic World. Cosmetic World, Inc., 48 East 43rd Street, New York, NY 10017. 312-687-6190.

Drug and Cosmetic Industry Drug Markets. Harcourt Brace Jovanovich, Inc., 757 Third Avenue, New York, NY 10017. 212-888-2130.

Drug Store News. Lebhar-Friedman, Inc., 425 Park Avenue, New York, NY 10022. 212-371-9400.

Drug Topics. Medical Economics Company, Inc., 680 Kinderkamack Road, Oradell, NJ 07649. 201-262-3030.

Lilly Digest. Eli Lilly and Company, Indianapolis, IN 46206.

NARD Journal. National Association of Retail Druggists, 11750 K Street, N.W., Washington, DC 20006. 202-347-7495.

Pharmacy Times. Pharmacy Times, Inc., 80 Shore Drive, Box 911, Port Washington, NY 11050. 516-883-6350.

Product Marketing--Cosmetic and Fragrances Retailing. Charleston Publications, 124 East 40th Street, New York, NY 10016. 212-953-0940.

Profitunities and Better Buys. Jobson Publishing Corporation, 352 Park Avenue, New York, NY 10010. 212-685-4848.

#### FINANCIAL RATIOS

Almanac of Business and Industrial Financial Ratios. Prentice-Hall Inc., 1818 Ridge Rd., Englewood Cliffs, NJ 07632. 800-922-0579 or 201-592-2000.

Annual Statement Studies. Robert Morris Assoc., 1 Liberty Place, 1650 Market St., Philadelphia, PA 19103. 215-851-9100.

Industry Norms and Key Business Ratios. Dun and Bradstreet Credit Services, 1 Diamond Hill Rd., Murray Hill, NJ 07974. 800-223-0141 or 908-665-5224.

#### GOVERNMENT PUBLICATIONS

CENDATA. U.S. Department of Commerce, Bureau of the Census, Washington Executive Plaza, Room 315, Upper Marlboro, MD 20772. 301-763-2074.

County Business Patterns - Illinois. U.S. Dept. of Commerce, Bureau of the Census. Order from: Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402. 202-783-3238. In Chicago: Government Printing Office Bookstore, 219 S. Dearborn, Chicago, IL 60604. 312-353-5133.

Small Business Information Bibliography. Illinois Department of Commerce and Community Affairs, 620 E. Adams St., Springfield, IL 62701. 217-785-6193.

Statistics of Income Bulletin. Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402. 202-783-3238. In Chicago: Government Printing Office Bookstore, 219 S. Dearborn, Chicago, IL 60604. 312-353-5133.