

## **KEATING INC.\***

Carol Keating was sure of the goals and problems her family's business would attempt to address as 2006 began: "Ask anyone in this company and you'll find... [they will list] three major challenges... One, how do each of us, as owners, get more time to relax from the stresses of the business? Two, how can we get over the short-term cash flow problems the business is having? Three, how do we insure that we don't expand too quickly?"

In one way all the members of the Keating family agreed with Carol: the family business, Keating Inc. (KI) faced three main challenges. However, exactly what these challenges were differed for almost each family member. Rob Keating, Carol's father and founder of Keating Inc., indicated that the main needs of the business were (1) to secure financing for expansion of the family owned businesses; (2) to use the borrowed funds to develop the present enterprises and (3) acquire real estate adjacent to some of the present property in order to allow for future expansion. Nora, Rob's wife wanted to reduce debt, have a less stressful working environment and fund insurance for all family members. The sons were in total agreement with each other. They both agreed that there was a need for better equipment, more personal spending money and shorter working hours. All the family members agreed that they needed to find some way to work together toward common goals.

### **THE HISTORY OF KEATING INC.**

Hard work toward a common goal and a need for money were nothing new to the Keatings. As Carol will tell you:

"Back in 1990 my parents declared bankruptcy. My parents, brothers and I packed up all we owned and headed out from Denver in an old station wagon. For a while we stayed in Miami where my Dad managed a skid row hotel. We had to leave because drug dealers almost blew his head off. He managed a furniture manufacturing plant in Milwaukee, but left because the owners wanted him to do some shady things with the cash flows. We ended up on welfare... My Dad then took \$500 my Mom scraped together for 'emergencies' and bought a run down shoe repair shop... twenty miles from where we lived! And he'd never fixed a shoe in his life!"

Thus in 1992 the Shoe Shop was born. This business was the beginning of a highly eclectic collection of businesses the Keatings would call Keating Inc. or K.I.

#### **The Shoe Shop Inc.**

Rob was quickly able to learn the craft of shoe repair through a combination of good instruction from the shop's previous owner, his natural ability with the craft and a desire to stay off welfare (not to mention Nora's threats as to what might happen should this venture fail). The whole family pitched in to help in the business: Nora learned as fast as Rob could find the time to teach her; the two eldest children, Carol and Ben were operating the machinery before they were teenagers; Jay, the youngest, waited on customers before he was ten. The firm, through ups and downs, supported the Keatings well since they bought it.

By 1996 they had four Shoe Shops in and around Abbotsford B.C. Canada. Nora ran one, Ben (then 16 years old) another, Carol (at the time 19 years old) the third, and Rob ran the fourth. An emergency might send Rob to one of the other stores. This would leave 12 year old Jay in charge of the store in his absence. In less than five years, the Keating family's tale had all the earmarks of becoming a rags to riches story. This allowed Rob and the family to set their sights to

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\* The names, amounts, places and dates in this case have been disguised.

bigger and better possible business ventures. These included a: a larger chain of stores and/or different business lines.

However, in 1997, disaster struck. Rob came down with double pneumonia. The illness was prolonged due to Rob's worn down condition from work related stress associated with attempting to control the activities of four different shops. Family members urged Rob to consolidate the businesses into one location. As Rob convalesced, he gave his approval to sell off excess equipment and move the best machines to one shop in Chilliwack B.C. (about a 90 minute drive from Vancouver). Rob decided that instead of geographic expansion the business would pursue diversification of services at the one remaining location.

### **The Creation of K.I.**

The first chance to diversify lines of business activity came when the Keatings had the opportunity to acquire a post office contract. The post office had determined that the area had grown sufficiently so that additional service was needed. The Keatings were able to take advantage of the opportunity to bid on and receive the contract from the post office. Stationary sales and eventually a typing service ("Secretary-in-a-Hurry") were developed in association with the postal service. Nora was put in charge of the postal services and Carol ran the typing service. All these services brought in more customers and so helped the shoe repair to expand. The postal, stationary, and secretarial service also increased profits by a third.

As a reflection of the more diversified lines of business pursued by the organization, Rob created K.I. in 1998. The idea was that K.I. would act as a holding company for all Keating family businesses. The post office substation, Shoe Shop Inc. and Secretary- in-a-Hurry, were made wholly owned subsidiaries of K.I.

Further expansion occurred in 1999 when the Keatings became lottery ticket agents. This involved instant, daily and lottery ticket sales. A percentage commission was taken out by the company and the remaining funds were deposited in a bank trust account. Every Friday the previous calendar week's deposits were taken out of the trust account by the province via electronic funds transfer. When the lotto jackpot would get large, the amount of trust funds could get up to \$35,000. The Keatings became adept at handling large sums of cash under this type of trust arrangement. Trust funds of this type would also prove to be an irresistible source of funds when times were tight.

In 2000 the Keatings contracted with several local utilities to collect payments from customers. So, instead of mailing a phone or electric bill payment from the Keatings' post office, one could simply pay the bill to the Keatings as agents for the utility. The Keatings would then deposit the funds into the utility's trust account (net of an agreed to commission) and the utility customer's payment would be recorded as paid when the Keatings mailed the list of payments to the utility at the end of the day. Thus, several trust accounts came under the Keatings' control. It was therefore necessary to make several trips daily to their financial institution so the cash on hand did not grow too large. Rob indicated that if they waited until the end of an average day to make the deposits they would be carrying more than \$5,000 in trust deposits alone. This was an unacceptable security risk for the Keatings.

The large amount of cash running through accounts that the Keatings controlled allowed them a certain amount of clout with their financial institution. The credit union the Keatings did business with was just across the street from the Shoe Shop. Branches of at least five other banks were located within five minutes drive of the shop. Since the Keatings did all their banking at this one Credit Union, they were one of the bank's biggest customers. This allowed Rob to use the threat of going to one of the other nearby financial institutions to obtain financing.

## **On the Home Front**

Even with all this activity on the job the Keatings were busy at home. In 2001 Rob and Nora Keating sold their home in Langley and moved to Sardis B.C., about a 15 minute drive from their Chilliwack store. With the proceeds from the sale they bought a trailer and made a down payment on two 10-acre lots of heavily wooded land. The contract with the previous owner (to whom the Keatings paid their mortgage) stipulated that some of the land could be cleared for a building site to construct a house. In violation of the agreement, the Keatings cleared the entire 20 acres. Good timber from the clear cut was sold to local sawmills and the lesser quality logs were sold as firewood. The Keatings then had to pay off the mortgage since their clear cut violated the terms of the mortgage and the mortgagor was threatening foreclosure. The family then built their home by themselves on one of two ten-acre parcels. They then sold the trailer and purchased an adjacent three-acre parcel as an investment.

## **The Making of the Country Store Inc.**

From 2000 to 2002 the businesses ran smoothly. The Keatings lived in an attractive three-bedroom home on 23 acres. Rob became bored with the business however, and began looking for additional business ventures. The opportunity arose to buy the property adjacent to the family's 23 acres. This property consisted of a five-acre corner lot with an old farmhouse and an additional six-acre lot.

Rob's idea was to convert the bottom of the farmhouse into a convenience store and the upper floor into office space and sleeping quarters for the two boys. This plan solved several problems. First, it gave the family an additional location from which to bring in business. Second, in the event the Shoe Shop lost its lease in 2007, the family would have ownership of a commercial property. (Moving the Shoe Shop would probably mean loss of the postal and lottery contracts, however.) Third, Rob viewed the two businesses as seasonally balancing each other out. Ben confirmed this final observation:

“This sounds crazy, but it's true. In bad weather people are more likely to get their shoes repaired. Folks don't realize they have holes or other problems with their shoes until they step in a puddle and their feet get wet. Summer in this part of the world is the dry season, for the shoe repair business, for weather and for people. On a hot, dry day when the shoe repair business is slow, the convenience store business should be booming with hot and thirsty people!”

A final rationale behind the purchase of the store property was it got Rob's two sons out of the house. Rob, Ben and Jay all agreed that such a move would be for the best since Rob and the two boys had almost come to blows on several occasions. “We work more than 60 hours a week and all we get for pay is room, board and spending money; that's all. It's a lot of work without much reward”, Ben complained. Ben estimated that he and Jay received about \$200 per month each and that Carol received about \$1500 per month (the larger sum went to Carol since she was not living at home). Jay added:

“It's good to be out of the house since we'd rather not have to listen to Dad's B.S. all the time. He's always telling us that we don't appreciate the fact that: *'the business moves we make and the work we put in are for the good of the family'* and *'being entrepreneurial requires sacrifice and dedication,'* but *'in the end you've really got something!'* The problems I see are that *'the end'* is never any time in the near future and whatever *'something'* we're supposed to get out of all this work we don't have yet. I don't know if we ever will.”

In early 2003 the farmhouse and five acres and the adjacent six-acre lot were purchased. Under Rob's direction, Ben and Jay started to rewire and re-plumb the building. A parking lot was put in and walls were knocked out. Ben and Jay put in fifty to sixty hours at the Shoe Shop and then worked on the future convenience store and their living quarters during their 'off hours.' They were driven to finish the rebuilding since upon completion they would also have a decent (or at least a less dusty) place to live. After eating dinner and taking care of the day's accounting, Carol and sometimes Nora would pitch in to help on renovations.

Ben worked alone on enlarging several passageways through supporting walls of the building that became the convenience store. "I worked alone because I needed to be able to concentrate. I risked a couple of tons of 50 year old house falling on me if I made a wrong move." The old walls are shown as dotted lines on a layout plan supplied by the Keatings. Ben also commented that mistakes on the remodeling job he did could have been fatal in a couple of ways: "If I collapsed the house the falling timbers may have killed me, if they didn't then my Dad would have killed me for destroying the place." The tone of his voice indicated he did not say this in jest.

When the remodeling was completed the building became a small 2000 square foot convenience store – groceries, milk, snack food, pop, video rentals, some hot food, etc. Thus, the Country Store, Inc. was added to the list of K.I. enterprises. Rob Keating planned to later expand operations at the Country Store location to include gas pumps, a restaurant, a hardware area, and a feed and grain department. Rob planned to eventually develop this five acres into a small strip mall of K.I. enterprises and stores rented by others. The idea was to take advantage of the rural nature of their area and to create what Carol called a "New Fashioned General Store" and what Ben referred to as "The Country Mall."

A similar 'Country Mall' scheme had been attempted by another entrepreneur about five kilometers away but it had closed years ago. Rob insisted that his plan would work because this other mall was on a busy main highway where people were less likely to stop and the Country Store was part of the community with long-term loyal customers.

Though family members thought the chances of gaining a loyal customer base for the Country Store, and a Country Mall were likely, there was no firm evidence to support this idea. The store was out of the way and, except for the family members who would work for low wages, the enterprise had no real competitive advantage (see below, "K.I. and Functional Support"). In spite of this, family members were positive about the Country Store. Carol Keating's comments were typical:

"The only competition we have is an old, dirty grocery and gas store a mile down the road. Since that place opened 12 years ago the population has more than doubled in this area. The community will easily support both of us – except we plan to out do the guy down the road. First we plan to offer more services, a cleaner, friendlier place and we'll be open 8 A.M. to 10 P.M. every day, he's only open 9 to 9."

## **PRESENT BUSINESSES**

Thus, at the close of 2000, the Keating businesses included three legal entities: Shoe Shop Inc., (which included Secretary-in-a-Hurry), K.I. and the Country Store Inc. The Chilliwack location was the headquarters for Shoe Shop Inc. and Secretary-in-a-Hurry and the other two entities were headquartered in Sardis, BC. K.I. was the sole owner of all the businesses.

### **Shoe Shop Inc. & Secretary-in-a-Hurry**

The Shoe Shop was located in the corner of a small strip mall, and the store itself was not visible from the road. The storefront was about 8 metres wide and had a large sign proclaiming "Shoe

Shop.” Taped on the inside of two large display windows were the store’s hours (8:00 A.M. to 6:00 P.M.), various notices as to the services to be found inside: Lottery, Post Office, money wires (which was added in 2000). Additionally, posters for recently arrived videos were taped on these large display windows. Since the Keatings had a ready supply of videos from the Country Store, Rob had decided that these could also be rented-out from the Shoe Shop.

Inside the Shoe Shop, about 10 metres from the door, stretched from the right to left wall was the well-worn wood paneled service counter. To the left were racks of videos and to the right were two shelving units. The shelving units contained stationary and mailing supplies (e.g. wrapping paper for parcels, regular and padded envelopes in a variety of sizes, writing paper, pens, etc.) and shoe related items (e.g. polish, laces, shoe horns, brushes, etc.). At the counter, no formal divisions existed but generally one end of the counter handled the typing service and postal customers, the shoe repair business, utility contract payments and video rentals were handled at the center of the counter and the money wires and lottery patrons were served at the other end of the counter. In back of the counter was an assortment of machinery: a scale for the post office, a shoe patcher (an old Singer sewing machine), etc. Also, in back of the counter were repaired shoes waiting for pickup, and, of course, the cash tills. A diagram of the store layout is included at the end of this case.

There was a door behind the counter that went into the office. This office held some of the company records and the equipment for Secretary-in-a-Hurry. The door to this office was usually kept open so that people in the office could see if the counter became crowded. If more than four people were waiting at the counter someone would come from the office to the counter to help. Rob believed that keeping the door open allowed family members to get more done and still give quality service. Another door led from the office to the back room where all the shoe repair equipment and supplies were kept. The door to the back room was usually shut to reduce noise and odors. Most of the equipment in the back room was 15 to 20 years old but still in fairly good working order. In the back room another door led outside. This outside back door was usually kept open to provide ventilation.

### **The Country Store Inc.**

As Rob explained it, the bend in road as one drove up to the Country Store was critical to the success of the business. He reasoned that since people had to slow down at the curve in any case, they would be more likely to stop at the store. However, getting to the store from the main road was somewhat problematic. Due to zoning requirements the parking lot entrance was not on the main road, Oak Street, but on a side road, Barley Avenue. At the corner of Oak and Barley a small brightly lit new sign stood atop a five-metre metal pole “The Country Store.”

The Country Store building was a small, neat barn red wood building with white trim. The inside of the store was brightly lit and clean. Just inside the store was the main service counter. On top of the counter were the cash register, a microwave and some impulse purchase items. Behind the counter were cigarettes, pop machines, hot snack food facilities and, usually, Rob Keating. Across from the counter was a window designed to spot customers at the gas pumps that were planned for the location. Under this window was a candy rack. Rob indicated that this placement was important. If he put the rack anywhere else his theft losses would be astronomical.

In spite of carefully placing small items where they could easily be seen from the counter and the careful placement of mirrors for security purposes, theft losses were twice as high as the liberal allowances Rob had originally made for such losses. The theft losses averaged approximately 4.5% of the cost of goods sold. The only comparable data Rob had was on supermarkets. Supermarkets had a 1.5% theft loss rate. Rob suspected some employees were

guilty of the thefts. He felt that his minimum wage employees thought they were worth more than the wage they were paid and decided to enhance their incomes through pilferage. In the store's first four months in business two of six non-family staff had been fired based on theft accusations. Rob also made sure that at least one family member was working during store hours to keep an eye on other employees. All these actions did little to cut the theft rate. There was some indication from Carol the high theft rate could probably be traced to midnight raiding from Ben and Jay. As she stated: "Ben and Jay live upstairs. If you got the midnight munchies and there was a whole convenience store right downstairs what would you do? I think my dad must know, but he probably figures he can right the expense off as part of Cost of Goods Sold."

Toward the back of the store was a full bathroom and laundry room. The laundry room contained not only the hot water heater and washer dryer but also a kitchen sink and stove. Jay and Ben shared these facilities with the employees since there was no other bath or kitchen facilities in the building. Also in the back of the store was a room that served as a workshop while the Keatings were reconstructing the building. If the Keatings lost the lease on their other location then this room would, in the future, be used as a shoe repair shop. Upstairs were Jay and Ben's small bedrooms, as well as a large center hall area (large enough to be a room) and a large office for the records and plans of K.I. and the Country Store.

### **K.I. & Keating Family Finances**

K.I. is a holding company. Its only real purpose, according to company Treasurer Carol Keating, is to coordinate the activities and finances of the Shoe Shop, Secretary-in-a-Hurry and the Country Store. Thus the statements of these companies were combined into K.I.'s financial statements (included at the end of this case). The balance sheet also showed both personal and business assets and liabilities. The reason for this unusual mingling was explained by Carol Keating:

"Our bank always makes my parents sign personally for credit. The bank also demands statements of their personal and business assets and liabilities. In order to avoid complications we just put everything on the one Balance Sheet. My Dad says that if you're an entrepreneur, you have to put it all on the line. I think his view is that since we started with almost nothing, we have nothing to lose. So we try to maximize our leverage by using all available credit and sometimes even floating three or four days worth of checks."

This 'float' could account for some part of the Keatings' negative cash balance, but not all of it. This is because the Keatings used the overall cash flow from all activities to cover any short-falls from any one activity. If the Shoe Shop account was short, funds from a trust account were used for a few days. These funds would then need to be replaced from operating funds or inflows from a different trust account. As long as the right amount of funds were in the right account when the funds were withdrawn all was well. If an account came up short, the Keatings could always chalk it up to an accounting error. Repeated mistakes could bring suspicion upon the Keatings since this activity, called kiting by accountants, is strictly illegal; in fact it is a felony.

Other unusual items on the financial statements were the fact that the real estate properties were shown at appraised market value. The reason for this according to Rob Keating was that the bank would evaluate how much credit to extend to the Keatings based on the appraised market value of the properties rather than their historical cost. Additional notes on the financial statements were made by Carol to help the bank analyze the documents. However, she also stated that a couple points on the statements needed additional explanation:

"The minority interest in the equity section shows stock holdings for Ben and me. Mostly, we're stockholders because there are certain income tax benefits that accrue to the family and to K.I. as a corporation. Ben and I don't really get cash dividends, but

we get our bills paid by the business. Between the two of us we've racked-up about \$35,000 in cash advances and other bills. Of course the bills aren't exactly ours. Basically, we lent my parents the use of our credit cards when the businesses weren't doing well a few years ago. Now they credit card bills are slowly being paid down. I have a bachelor's degree in management and they never taught this in my finance classes. Anyway, these credit card debts have allowed my Dad to accomplish what I think are his two most important goals: maximizing business leverage and making sure Ben and I don't leave the business like we often threaten to do."

### **K.I. & Functional Support**

Below is a brief synopsis of the support functions performed by K.I. in its role as coordinator for Keating business activities:

**Marketing** at K.I. was minimal. Promotion was done through the Yellow Pages<sup>TM</sup>, roadway signs at both locations and word of mouth. Market research involved in the decision to open the Country Store was based on a detailed demographic report of the region surrounding the store obtained from a secretarial service client. This report had been used in 2002 as the basis to open a large supermarket about 7 miles from the Country Store. Product lines the Shoe Shop carried were determined on a trial and error basis (Ben: "We buy a bit of it something, if it sells we buy more, if it doesn't, we don't any buy more.") Product lines carried by the Country Store were suggested by vendors and basically followed the same trial and error pattern.

The pricing policy at the Country Store was substantially in the hands of suppliers who suggested the appropriate mark-ups for products. Pricing at the Shoe Shop and Secretary-in-a-Hurry was determined through price comparison – i.e. what price were others charging for same services the Keatings were offering. This was done through occasional inquiries at other repair shops or typing services around Chilliwack and Abbotsford. Prices were set to be competitive (Carol: "We're not the highest priced or the lowest priced – I think people pick us because the location is convenient, not because of the price.") One way Carol maximized this convenience for Secretary-in-a-Hurry was to offer the service at both Keating business locations (each location contributed to about half of the secretarial service's revenue). Plans to offer shoe repair services at both locations were discussed.

**Logistics** functions for K.I. were mostly performed by outside vendors. All products were delivered to the Country Store by vendors. Newspapers and magazines were brought daily, and the store was credited for unsold past date publications (i.e. yesterday's newspapers, last week's weekly journals, etc.). Various beverage companies came twice weekly to check and restock their products in the appropriate sections. Dairy, snack food and bakery products were checked and restocked daily by the relevant suppliers (the store again being credited for unsold past date product). The remaining products (groceries, paper products, sundry, candy, frozen pizza, etc.) were all supplied by one large wholesaler, Marcan, who delivered once a week. Marcan was not greatly different from other wholesalers in terms of price or service, but Marcan did extend credit to the Country Store and this was the deciding factor.

The Shoe Shop suppliers came around about twice a month and supplies of polish, laces, heels, etc. were ordered when Ben saw that they were getting low. The amount of stamps, money orders and other post office supplies that were supposed to be on hand were stipulated in the Keatings' contract with the Postal Service. Since inventory reports were required to be filed weekly with the Postal Service, the supplies to be ordered by Nora were simply the difference between the inventory-on-hand and the inventory amounts stipulated in the contract. Ordering supplies for the lottery and money wires, operated in the same manner as for the postal supplies. Paper and printer ink purchases for Secretary-in-a-Hurry were made by Carol on an 'as needed' basis.

**Accounting & Finance.** In the last two weeks of the month Rob would budget for the next month using a computer spreadsheet (e.g. June's expected revenue, expenses and capital spending are budgeted in the last two weeks of May). Typically, one month's budget was pretty similar to the next month. Expenses which did not occur every month were, on occasion, forgotten until the bill arrived (e.g. semi-annual auto insurance payments). While such problems would throw the budget out of whack, Rob still preferred to only budget one month in advance since he felt it gave the firm greater flexibility. During the course of the month daily cash receipts and disbursements were recorded separately for each subsidiary. Monthly statements of cash receipts and disbursements were produced for each subsidiary at the end of the month and occasionally compared to the budget.

**Management, Operations / Human Resources.** Rob manages the Country Store and controls the Shoe Shop by phone. Rob occasionally visited the Shoe Shop to keep employees on their toes. In Rob's absence, Nora was in charge of the postal and money wires, Jay was in charge of the lottery and video, Ben managed the shoe repair and Carol the typing services. When people need to be shifted to different posts because of a customer backlog in one area it was Carol who made the assignments. Wages were as close to minimum wage as possible and there was no benefits package for employees, or family members.

**Integration & Coordination** for the companies had been done at the Keatings' dinner table. Family members gathered together most days at dinner to coordinate business efforts. Since opening the Country Store (due to Country Store staffing requirements), these meetings were impossible and now occurred only two or three times a week after the Country Store closed at ten P.M. These meetings usually lasted about two hours and Rob chaired them. Meetings kept main K.I. employees in touch with one another and made them aware of events occurring within the firm. These meetings also served as a sounding board for operational problems and as a brainstorming session for possible solutions. However, the final decisions were made by Rob. Implementation was sometimes a problem if other family members did not support the final decision.

**Strategic / Long Range Planning** functions were managed by Carol Keating with substantial input from Rob Keating. There were two reasons this task had fallen to Carol: (1) her bachelor's degree in business administration and (2) her typing ability. Both skills allowed her to develop quality business plans which she could present to the bank for financing. Final approval of the plan was made by Rob.

## **SOME NOTES ON THE COMPETITION**

Due to their busy work schedule the Keatings were only able to gather limited information on their competition. What they did know was the geographical placement of their competitors' businesses and some of the competitors' prices. Competitors for the Country Store's business included other convenience stores and supermarkets. Keating family members also noted that other competitors included video rental stores and gas stations that were increasingly moving into the business of selling snack foods. Locations are indicated on the map of the Chilliwack area included at the end of the case. Occasional purchases from these competitors allowed the Keatings to track competitors' prices. Rob Keating, however, felt that vendor suggested prices were sufficiently close to the competitors and so these vendor-suggested prices were the ones always used.

Secretarial service Competitors included five people in Chilliwack who performed typing and copying in their home. Carol Keating stated that if people wished to travel down the road to Abbotsford they could find "a dozen professional offices that did typing and maybe twice that many 'at home' services." It was these Abbotsford and Chilliwack services Carol called to check to see if her prices were competitive.



In Chilliwack there were one other smaller shoe repair shop. To use Ben's wording: "We have the shoe repair business... sown-up." There were five to ten shops between in Abbotsford and Hope that repaired shoes and these were the ones he or Jay called to check the Shoe Shop's pricing.

## **THE FUTURE**

In discussing the plans for the future of the Keating companies, Carol Keating, in her role as strategic planner, told of the businesses' plans for one, two, three, five and ten years into the future. Carol began with the two priority items for the next year:

"First, we're going to try to acquire the property across the street for about \$5,000 down and a purchase price of about \$200,000. The people who own it are getting divorced and want to get rid of the property quickly. The house needs some work, but we can use most of the 10 acres it sits on for future development. In the meantime we can rent the place out for a bit less than the payments until we get a chance to work on the place. It may be helpful to own both corners at this intersection for the purpose of future expansion five to ten years down the line.

"The second thing we need to do is get the gas pumps. My dad thinks our business will really pick up when those come in. However, they cost \$250,000. On the other hand, those pumps may be vital for bringing customers to support the Country Store's expansion over the next two years."

Over the longer term Carol set out some specific goals for K.I. and the rest of the Keating enterprises:

"The other important thing we'll try to do in the next three years is to arrange financing for the strip mall we're planning. We've applied to two different banks for a half million in loans. All is going according to plan: we've been turned down twice. "

Carol went on to explain that to be entitled to certain types of grants or other government aid, they felt that K.I. needed to get turned down several times by regular lending institutions. After these refusals they felt that the funds from granting agencies would become available. The Keating's were certain that this is the kind of project for which they could get funding from such agencies:

"Over the long run several projects will be finished. Three to five years out we'll be constructing the strip mall, expanding our present lines to fill some of the mall space and finding tenants for the rest of the space. Six or seven years down the line we'll fix-up the house across the street. We'll also begin development of the rest of that property. Over the eight to ten year time frame we may acquire a couple other rural locations for the Country Store and from there probably develop a chain of stores."

While Carol expressed these optimistic plans she also expressed some misgivings on their likelihood of occurring and her role in their implementation:

"Right now I doubt things will look anything like what we're planning. We have cash flow problems now and added projects aren't going to help. In addition, the workload for all of us is increasing at a time when I want to spend less time at work. I've just gotten married and I want to spend more time with my husband. Ben just got engaged and he is already trying to work less hours. In the short run we may need to hire more employees but this will put further strain on our cash."

**KEATING INC. REVENUE BREAKDOWN, DECEMBER 31, 2005**

<u>Store Breakdown</u>			<u>Product Line Breakdown</u>									
<u>Shoe Shop</u>	<u>Country Store</u>	<u>Month</u>	<u>Food</u>	<u>Shoe Repair</u>	<u>Retail</u>	<u>Video</u>	<u>Sec./ Copy.</u>	<u>Lotto</u>	<u>Con-tract</u>	<u>S.S. Misc.</u>	<u>C.S. Other</u>	<u>Total</u>
\$30,562	\$17,320	Jan.	\$13,740	\$14,000	\$2,800	\$3,600	\$3,560	\$2,300	\$5,042	\$2,160	\$680	\$47,882
30,638	19,484	Feb.	15,800	14,060	2,790	3,510	3,860	2,200	5,042	2,160	700	50,122
28,782	21,430	Mar.	17,680	12,500	2,480	3,500	4,000	2,240	5,042	1,920	850	50,212
25,832	33,970	Apr.	29,350	9,370	1,860	4,320	4,920	1,800	5,042	1,440	1,700	59,802
23,002	41,760	May	36,200	6,250	1,240	5,200	5,920	1,400	5,042	,960	2,550	64,762
22,220	44,440	June	39,020	6,000	800	5,000	5,840	1,600	5,040	,960	2,400	66,660
20,632	39,390	July	35,350	6,250	1,240	3,780	4,300	1,400	5,042	,960	1,700	60,022
23,328	35,674	Aug.	31,350	7,810	1,550	4,050	4,600	1,800	5,042	1,200	1,600	59,002
35,978	32,934	Sep.	27,450	15,620	3,100	5,130	5,840	2,800	5,042	2,400	1,530	68,912
49,636	30,136	Oct.	23,500	24,200	4,800	6,210	7,060	4,000	5,042	3,600	1,360	79,772
47,776	25,676	Nov.	196,102	23,400	4,650	5,670	6,460	4,000	5,042	3,600	1,020	73,452
36,064	21,036	Dec.	16,450	16,740	3,690	4,030	5,140	2,460	5,040	2,640	910	57,100
<u>\$374,450</u>	<u>\$363,250</u>	<u>Total</u>	<u>\$481,992</u>	<u>\$156,200</u>	<u>\$31,000</u>	<u>\$54,000</u>	<u>\$61,500</u>	<u>\$28,000</u>	<u>\$60,500</u>	<u>\$24,000</u>	<u>\$17,000</u>	<u>\$737,700</u>

<u>% of Revenue</u>	<u>Food</u>	<u>Shoe Repair</u>	<u>Retail</u>	<u>Video</u>	<u>Sec./ Copy.</u>	<u>Lotto</u>	<u>Con-tract</u>	<u>S.S. Misc.</u>	<u>C.S. Other</u>	<u>Total</u>
<u>Applicable to:</u>										
Shoe Shop	-	21.2%	4.2%	3.7%	4.2%	3.8%	8.2%	3.2%	-	48.5%
Country Store	48.5%	-	-	3.7%	4.2%	-	-	-	2.2%	51.5%

<u>% of Labour</u>	<u>Food</u>	<u>Shoe Repair</u>	<u>Retail</u>	<u>Video</u>	<u>Sec./ Copy.</u>	<u>Lotto</u>	<u>Con-tract</u>	<u>S.S. Misc.</u>	<u>C.S. Other</u>	<u>Total</u>
<u>Applicable to:</u>										
Shoe Shop	-	25.0%	1.0%	3.0%	5.0%	8.0%	15.0%	1.0%	-	58.0%
Country Store	33.0%	-	-	3.0%	5.0%	-	-	-	1.0%	42.0%

**ROB & NORA KEATING INCOME STATEMENT, DECEMBER 31, 2005**

		<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
<b>Income:</b>	Dividends from K.I. . . . .	\$ 123,274	\$ 103,460	\$ 55,320	\$ 61,170
	Salaries from K.I. . . . .	70,000	60,000	60,000	48,000
	Total Income	<u>\$ 193,274</u>	<u>\$ 163,460</u>	<u>\$ 115,320</u>	<u>\$ 109,170</u>
<b>Expenses:</b>	Interest Paid . . . . .	\$ 51,920	\$ 48,800	\$ 25,440	\$ 19,800
	Loan Principle Paid . . . . .	27,000	14,000	12,000	10,000
	Taxes . . . . .	27,198	20,000	7,200	7,200
	Living Expenses . . . . .	87,156	80,660	70,680	72,170
	Total Expenses	<u>\$ 193,274</u>	<u>\$ 163,460</u>	<u>\$ 115,320</u>	<u>\$ 109,170</u>
<b>Net Income</b>		<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>

**ROB & NORA KEATING & K.I. INC. BALANCE SHEET, DECEMBER 31, 2005**

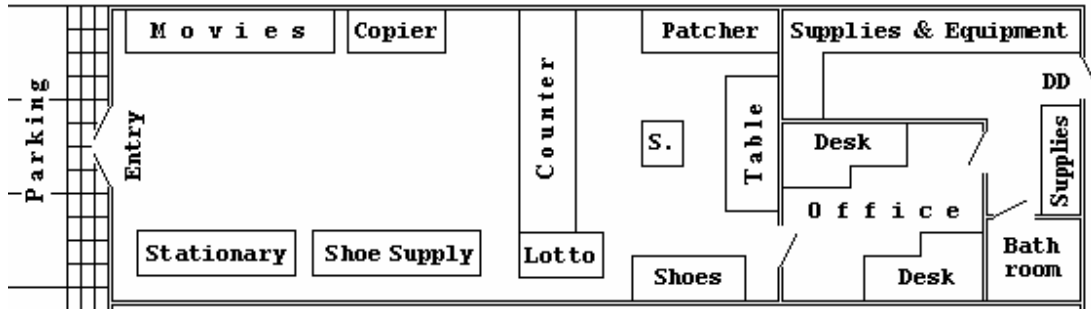
<u>ASSETS</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>LIABILITIES</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
<b>Current Assets</b>				<b>Current Liabilities</b>			
Personal Cash	\$ 3,500	\$ 3,000	\$ 4,000	C.S. Payables	\$ 24,000	\$ 16,000	\$ 2,000
C.S. INC. Cash	1,000	1,000	1,000	S.S. Payables	5,000	2,000	2,000
S.S. INC. Cash	-15,000	-4,000	-4,000	Postal Service	20,000	20,000	20,000
Trust Account	24,000	20,000	15,000	Payroll Taxes	4,000	4,000	3,000
Stamps	20,000	20,000	20,000	Sales Tax	4,000	4,000	3,000
C.S. Inventory	25,200	14,000	0	Trust Deposits	24,000	20,000	15,000
S.S. Inventory	5,300	5,400	5,400	C.S. Credit Line	22,000	15,000	10,000
				Cur. Part LT Debt	<u>38,400</u>	<u>33,600</u>	<u>20,000</u>
Total Current	<u>\$ 64,000</u>	<u>\$ 59,400</u>	<u>\$ 41,400</u>	Total Current	<u>\$ 141,400</u>	<u>\$ 114,600</u>	<u>\$ 75,000</u>
<b>Other Assets</b>				<b>Long Term Debt</b>			
Improvements	\$ 70,000	\$ 60,000	\$ 15,000	Improvements	\$ 51,000	\$ 30,000	\$ 10,000
Depreciation	-35,866	-18,000	-13,200	C.S. Fixtures	8,000	8,000	
C.S. Fixtures	10,000	7,000	0	S.S. Equipment	12,000	8,000	4,000
S.S. Equipment	14,000	14,000	14,000	Videos	20,000	8,000	8,000
Autos	10,000	10,000	10,000	LT Capital Lease	20,000	16,000	
Videos	20,000	10,000	5,000	Store & 5 Acres	130,000	140,000	150,000
C.S. Misc.	1,000	1,000		Home & 10 Acres	240,000	250,000	170,000
Personal	20,000	20,000	20,000	10 Acre Parcel	50,000	55,000	60,000
Capital Lease	30,000	22,000		6 Acre Parcel	28,000	30,000	
				Cur. Part LT Debt	<u>-38,400</u>	<u>-33,600</u>	<u>-20,000</u>
Store	240,000	220,000	200,000	Total LT Debt	<u>\$ 520,600</u>	<u>\$ 511,400</u>	<u>\$ 382,000</u>
Depreciation	-12,000	-2,000					
				Total Liabilities	<u>\$ 662,000</u>	<u>\$ 626,000</u>	<u>\$ 457,000</u>
Store 5 Acres	60,000	56,000	50,000	<b>EQUITY</b>			
Home, 10 Ac.	280,000	260,000	240,000	Family Equity	\$ 196,134	\$ 224,400	\$ 302,200
10 Ac. Parcel	120,000	110,000	100,000	Property Equity	130,000	66,000	
3 Ac. Parcel	24,000	22,000	20,000	Common Stock	2,000	2,000	2,000
6 Ac. Parcel	76,000	68,000	60,000	Minority Contrib.	1,000	1,000	1,000
Other Assets	<u>\$ 927,134</u>	<u>\$ 860,000</u>	<u>\$ 720,800</u>	Total Equity	<u>\$ 329,134</u>	<u>\$ 293,400</u>	<u>\$ 305,200</u>
Total Assets	<u>\$ 991,134</u>	<u>\$ 919,400</u>	<u>\$ 762,200</u>	Liab. & Equity	<u>\$ 991,134</u>	<u>\$ 919,400</u>	<u>\$ 762,200</u>

- Equipment at the Shoe Shop fully depreciated on 12-31-04; 3-5 more years use expected from it.
- All 2004 & 2005 cap. lease payments, depreciation., bus. int. (less \$3,400) is Country Store (C.S.).
- Utilities for the Shoe Shop (S.S.) are \$1,600 per year for 2004 and 2005.
- The \$12,000 rent expense applies to the S.S.; All Improvements apply to the C.S.
- With the exception above expenses, all expenses are equally shared by S.S. and C.S.
- Videos, Payroll Payable, Sales Tax Payable are half C.S. and half S.S.; auto is personal.
- Advances from S.S. to C.S. total \$210,406 at the end of 2005.
- For 2003, 2004 and 2005, current portion of S.S. Long Term (LT) debt was \$2400, \$5,000, \$6,000, respectively; personal portion of LT debt was \$10,000, \$14,000, \$12,000, respectively.
- Personal tax: \$8,000 of 2004 taxes and \$24,000 of 2005 taxes relate to back income tax owed but not paid in 2003. Tax payments were current as of 12-31-2005. C.S. losses result in a \$3,300 tax benefit.

## K.I. INCOME STATEMENT, DECEMBER 31, 2005

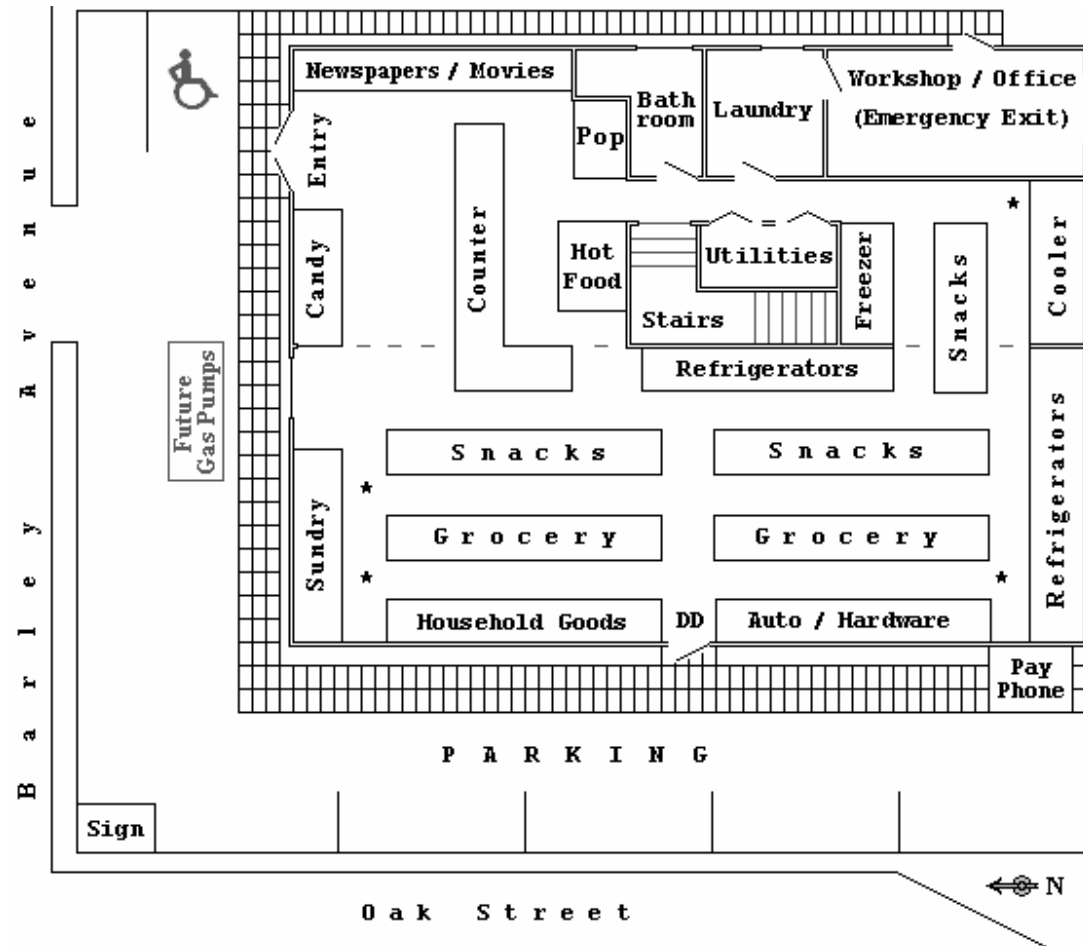
		<b>2005 Breakdown</b>					
		<b>Shoe Shop</b>	<b>Country Store</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Sales:	Dairy Foods	\$ 0	\$ 54,000	\$ 54,000	\$ 24,000	\$ 0	\$ 0
	Baked Goods		64,000	64,000	33,000		
	Beverages		86,000	86,000	42,000		
	Snack Foods		101,500	101,500	54,000		
	Country Store Other		17,000	17,000	11,000		
	Shoe Repair	156,200		156,200	124,000	145,000	134,000
	Shoe Related	31,000		31,000	23,000	28,000	26,000
	Secretarial & Copies	30,750	30,750	61,500	52,000	56,000	50,000
	Contract Payments	60,500		60,500	50,000	51,000	45,000
	Video Rental	27,000	27,000	54,000	45,000	6,000	
	Lotto Commission	28,000		28,000	23,000	29,000	26,000
	Shoe Shop Misc.	24,000		24,000	19,000	11,000	10,000
	<b>Total Sales</b>	<b>\$357,450</b>	<b>\$380,250</b>	<b>\$737,700</b>	<b>\$500,000</b>	<b>\$326,000</b>	<b>\$291,000</b>
Cost of:	Dairy Foods	\$ 0	\$ 42,000	42,000	20,000	\$ 0	\$ 0
Goods Sold	Baked Goods		50,000	50,000	26,000		
	Beverages		64,500	64,500	32,000		
	Snack Foods		74,000	74,000	40,000		
	Country Store Other		12,426	12,426	8,140		
	Shoe Repair	31,000		31,000	24,000	32,000	28,000
	Shoe Related	19,500		19,500	14,000	18,280	15,730
	Secretarial & Copies	10,500	10,500	21,000	16,000	20,000	15,000
	Total C.O.G.S.	61,000	253,426	314,426	180,140	70,280	58,730
Gross Profit		<b>\$296,450</b>	<b>\$126,824</b>	<b>\$423,274</b>	<b>\$319,860</b>	<b>\$255,720</b>	<b>\$232,270</b>
Operating Expenses:	Salaries & Wages	\$ 59,160	\$ 42,840	\$102,000	\$ 97,500	\$ 21,000	\$ 22,500
	R.& N. Keating Salaries	40,600	29,400	70,000	60,000	60,000	48,000
	Rent	24,000		24,000	24,000	24,000	24,000
	Equipment Lease		20,400	20,400	20,400		
	Depreciation		17,866	17,866	4,800	4,800	4,800
	Utilities	5,200	5,200	10,400	9,000	3,200	3,000
	Insurance	2,400	2,400	4,800	4,000	1,500	1,000
	Supplies & Repairs	1,250	1,250	2,500	2,000	500	500
	Bank Charges	1,000	1,000	2,000	1,500	500	500
	Legal & Accounting	500	500	1,000	1,000	1,000	1,000
	Advertising	250	250	500	500	500	500
	Shoe Shop Misc.		2,000	2,000	1,500	500	500
	Taxes	36,700	-3,300	33,400	33,000	11,000	8,000
	Interest	3,400	34,000	37,400	36,000	28,500	4,000
Total Operating Expenses		<b>\$174,460</b>	<b>\$153,806</b>	<b>\$328,266</b>	<b>\$295,200</b>	<b>\$157,000</b>	<b>\$118,300</b>
Net Income		<b>\$121,990</b>	<b>-\$ 26,982</b>	<b>\$ 95,008</b>	<b>\$ 24,660</b>	<b>\$ 98,720</b>	<b>\$113,970</b>
Dividends		<b>\$ 61,637</b>	<b>\$ 61,637</b>	<b>\$123,274</b>	<b>\$103,460</b>	<b>\$ 55,320</b>	<b>\$ 61,170</b>
Change in Equity		<b>\$ 60,353</b>	<b>-\$ 88,619</b>	<b>-\$ 28,266</b>	<b>-\$ 78,800</b>	<b>\$ 43,400</b>	<b>\$ 52,800</b>

### SHOE SHOP FLOOR PLAN



DD Delivery Door: used only for deliveries and locked at all other times.  
 S Scale for Postal.

### COUNTRY STORE FLOOR PLAN



\* Wide angle ceiling mirror mounted about here for security.

# CHILLIWACK AREA MAP

