



Turning On Your Idea: Starting a Specialty Food

Business Requires Careful Planning

“Thinking is the hardest work there is, which is the probable reason why so few engage in it.”

You have a great recipe or product idea that incorporates the good food you grow on your farm into a specialty food product. All of your friends and family rave about your idea. Making the transition from food producer to food processor seems like a logical step. And specialty food products have a proven track record in the marketplace.

But starting a specialty food processing business is not easy. Like any small business, specialty food processing requires careful planning, dedication, and skilled management to be successful.

Because your product can directly affect your customer’s health and safety, your business must comply with a number of complex and often confusing federal, state and local regulations.

Before you commit to producing hundreds of bottles of salsa, ask yourself the following questions about running a small food processing business:

Are you willing to invest the time and effort necessary to start this type of business?

Like any start-up business, a specialty food processing business takes careful planning. You will need to devote time to market research, phone calls, letters, office visits, and lots of decisionmaking before you turn out your first jar of jelly or can of organic vegetable soup. Months or even a year is not an unreasonable amount of time to expect to spend preparing to open your business.

Is this type of business a good fit for your family and your current farming operation?

Many business start-ups rely on family members to help with labor and possibly financial support, particularly in the early phase. If your family is already working in your farming operation, will they have time to work for this enterprise too? Who will handle your workload while you start this enterprise?

Who will purchase your product? It’s critical to know your “target audience” and more importantly, why people are willing to purchase certain types of products. Who is your typical customer? What is his/her age, sex, income,

buying habits? Where do your potential customers live? How much do they spend on related items? Where do they shop? What do they read? This is market research.

What is your product and how will you make it?

If you want to prepare a food product for retail sales, with very few exceptions, you will not be able to make it in your home. This means that you will either have to build your own facility and buy equipment, rent existing facilities and equipment, or contract with an existing food processor to “co-pack” your product for you. Co-packers manufacture and package foods for their clients.

In addition, it's one thing to make small batches of your product for family and friends, but larger production runs require developing large batch recipes. Where can you get professional advice on adjusting recipes and improving the shelf-life of your product? Where can you purchase the ingredients, packaging containers, and labels that make your product attractive and safe to the public? This is market research.

Are you aware of the local, state and federal regulations concerning food processing?

There may be local zoning ordinances or land use restrictions that affect the kinds of businesses you can operate on your property. You will need to be trained in basic food safety and sanitation procedures to ensure a safe food product. Your product also will need to comply with the Food Regulation Standards developed by the Food and Drug Administration (FDA). Your product may require a nutritional analysis or benefit from a specialty product label.

Can you make money with this enterprise?

Many small or on-farm specialty food processing activities are “income patching” enterprises. A processing activity may be one of several sources of income rather than the sole source of support.

How much time and financial resources can you commit to this new enterprise? How much will customers pay for your product? Consumers are generally willing to pay a slight premium for a specialty or gourmet products, but they must be high quality.

Knowing what your customers will pay will help you determine how many units you have to sell to break even. The other part of the profitability equation is your cost of production. You must calculate all your costs, both fixed and variable. Fixed costs are reoccurring expenses like a monthly rental payment. Variable costs are onetime payments such a licensing fee.

Remember, the goal is not to just break-even, but to make your target profit.

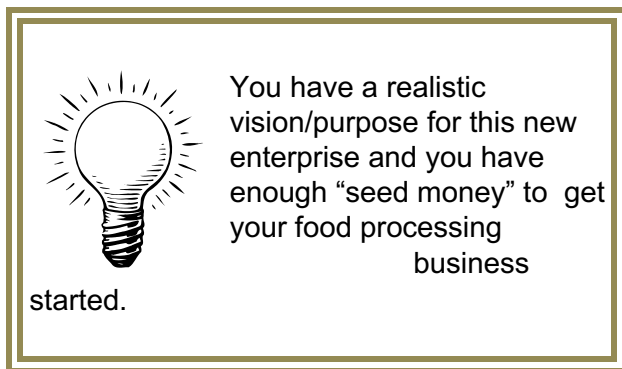
Do you consider yourself to be an “agripreneur”?

Risk is an intrinsic part of any business venture, and starting a new food processing can be risky. The hidden costs of the uncertainty from a new venture can be staggering in terms of stress on family relations, self-image and personal bank accounts.

To maximize your profit potential, you will need to sharpen your business management skills. You should write a business plan that includes a detailed marketing plan. Your business plan is the road map that outlines the goals for your business and how you plan to reach them. For help in writing your business plan, visit www.extension.umd.edu/mredc.

Do you have the necessary capital required to fund this new business?

Most successful businesses start small. Consider how you will develop your product and markets, work out production procedures, and learn the peculiarities of the industry before spending money on building permanent facilities, hiring labor, or quitting your day job.



As You Plan Your New Business, Answer the Who, What, Why Questions

According to the Appalachian Center for Economic Networks, about 15,000 new value-added products are introduced each year. However, only about one in ten of these products is successful and remains in production. Large companies rely on a product development team that includes food scientists, marketing and advertising experts and other specialists to develop and market their new products. The challenge for a small start-up food processor is to develop a network of resources and experts that can serve as a virtual development team. These experts may include county Extension Educators, university instructors and training classes, and local small business development centers.

Before you can assemble your team, you must determine what you plan to sell. Will it be fresh, refrigerated or frozen? Is it canned or bagged? What size containers will you offer, and what is the shelf-life of your product? Is it a stand-alone product or an ingredient?

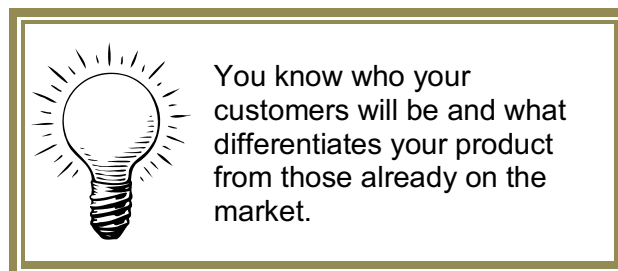
Most importantly, as you begin perfecting your delicious new salsa recipe or start looking for the latest cheese culture, answer these questions:

- Who will use my product?
- What is the competition?

- Where will I sell it?
- What price will I charge?
- Why will customers buy it?

Answers to these questions will help you better understand what your potential customers want. The answers will help you determine your market niche and develop your business plan.

Remember that the purpose of your business is to sell products at a profit, not to make products and hope they *might* sell.



Conducting Market Research is Part Science, Part Research and Part Intuition

Market research—gathering information about markets or customers—is a very important component of business strategy. Market research is a key factor in maintaining competitiveness.

Understanding your target audience(s) — those who will buy your product—is the foundation for building your business. You need to know important demographic information such as age, gender, buying habits, where potential customers live, how much they spend on products like yours and where they get information about the food products they buy.

While major food processors may contract with consultants to conduct extensive market research before developing a new food product, small businesses with limited capital need to keep the process simple and objective; in other words, you can't rely solely on family and

friends. You can learn about sources of market research information at major specialty food industry trade shows such as the Fancy Foods show held annually in New York City, meeting with local chefs to determine their menu needs, and talking with local food vendors and specialty food shops owners. Read the weekly food section of your local paper, cooking magazines, and watch food shows on television. These can be great sources of information on current food industry trends, consumer preferences and industry contact names.

Of course, there is no better market feedback than repeat sales. If possible, consider offering your product first at the county farmers' market where you can garner customer feedback with every sale. Use this information to determine how to proceed. If necessary, refine your product based on customer feedback about color, texture and appearance.

Focus on Identifying Your Marketing Niche

Once you have determined what product to make and who will buy it, you need to determine where to sell it. You must answer the question, "What market should I attempt to enter?" Direct markets, grocery stores, institutional food services, mail order or specialty shops are all separate and very different markets.

Direct marketing through local farm stands, farmers markets and festivals is one of the most cost-effective methods of introducing your product. The reception at these outlets is a good indicator of how your product will be received in larger venues. Direct marketing also allows you to receive customer feedback about product preferences, package sizes and pricing. This information can help you form new marketing ideas or revise an existing marketing plan.

Grocery stores are the hardest venues to enter. Shelf space in grocery stores commands a premium, and most grocery stores require a "slotting fee" to place products on their shelves. These fees are non-refundable and they do not guarantee that your product will remain in the store. In grocery stores, your product must compete against larger national manufacturers for shelf space and their advertising resources.

The **institutional foodservice market** is somewhat easier to enter than grocery stores. This market includes restaurants, schools, military facilities, penal institutions and hospitals. While most government institutions require bidding out their bulk food orders, specialty seasonal items can be added for menu variation. Specialty shops and local restaurants can help small specialty food processors introduce their product to the public while at the same time acquiring a unique item for their menu or ingredient in their recipes.

Specialty, gourmet or health food stores often have greater potential for sales of small food processor products than any other food market outlet. The uniqueness of your product and/or your packaging is very important. Shoppers in this market are looking for high-quality, tasty foods in unique or creative packaging.

Internet sales and mail order can work well for specialty food products that are targeted to specific audiences demographically, geographically or by special interests. These sales offer farmers new ways to form longdistance relationships with consumers. However, there are many hidden costs in mail order and Internet sales, including:

- Printed material costs or web design and maintenance;
- Product shipping costs, handling, credit sales, returns, and lost shipments;
- Customer complaints;
- Advertising; and

- Developing and maintaining address lists.

The venue best suited to your product determines the “niche” markets you should concentrate on developing. Niche marketing entails finding the best combination of product design, packaging, pricing, positioning, and promotion that will encourage customers to purchase your product.



Can You Make Money Selling Your Product?

Product price can mean the difference between success and failure. You must calculate the costs of making your product before you can set the price, and you must set the price before you can ask the ultimate question: How much are consumers willing to pay?

First, calculate all your costs, both fixed and variable. Fixed costs are the things that don't change whether you make one or 10,000 jars of salsa, including rent, basic utilities, insurance, salaries and taxes. Costs for such things as ingredients, packaging, labels, shipping, advertising, promotion, supplies, etc. are variable and depend on the number units produced.

The sum of your fixed and variable costs is the cost of production. To find your per-unit cost of production, divide the total costs by the number of units. Add the amount of per-unit profit to the per-unit cost. For example, 400 jars of your “Jammin Jelly” cost you \$1,000 to produce. You want to made 50 cents profit on each jar.

$\$1,000 \text{ total production costs} / 400 \text{ units} = \2.50 per unit
 $\$2.50 \text{ per unit production costs} + 50 \text{ cents profit} = \3.00

The resulting selling price, however, is only a starting place for pricing your product. (Product pricing will be discussed in more detail later in this publication.) The price you set may not be the final price the consumer pays. Everyone who handles your product before it reaches the consumer will mark it up to realize a profit too. Visit stores to check the price and availability of products similar to yours.

Consumers are generally willing to pay a premium for high-quality specialty food products, but you must determine what the market will bear. This is where your earlier market research information gives you a clearer picture of your potential customers' buying income and helps you to determine their price sensitivity.

Once you have an estimated selling price and production costs per unit, you need to determine how many units you must sell at that price to make a profit. You need to determine your break-even point--the point at which you have sold enough product to cover all of your expenses. However, you are not going into business to just break even, but to make a product you can sell at your target profit.

So you've decided that a specialty food business is a good match with your personal and financial resources. You have identified your potential customers and the product you will sell. And you have calculated a positive profit potential. Now it's time to begin making your product. You'll find information and resources at county and state offices that will help you get started.

There are Many Resources Available to Help You Start Your Specialty Food Business

State of Maryland Department of Health and Mental Hygiene (MDHMD)
Office of Food Protection and Consumer Health Services

6 St. Paul St., Suite 1301
Baltimore, Maryland, 21201
(410) 767-8444

MDHMD provides information on the rules and regulations concerning processing and selling food in Maryland. The Department determines the type of production facility you will need and the license(s) required to process your value-added food.

Maryland Department of Agriculture

Wayne A. Cawley, Jr., Building
50 Harry S. Truman Parkway
Annapolis, MD 21401-8960
(410) 841-5700, (301) 261-8106 (DC area)
Fax: (410) 841-5914; TDD: (410) 841-5982
Web: www.mda.state.md.us

MDA has many programs to ensure the safety and quality of animal and human food. The Food Quality Assurance Program combines regulatory and voluntary programs to promote the sale and consumption of high-quality, wholesome food products such as eggs, poultry, fruits, vegetables and grain.

The Maryland Rural Enterprise Development Center (MREDC)

University of Maryland - Western Maryland
Research & Education Center
18330 Keedysville Road
Keedysville, MD 21576 301-432-2767
www.extension.umd.edu/mredc

The MREDC provides information on selling and processing food in Maryland, including rules for specific foods and important regulatory information.

Local, State and Government Regulations Can Affect Start-ups

Food processing is a highly regulated industry. Zoning, permits, certification, and public health and safety rules may seem burdensome for a start-up business, but these regulations are important and not insurmountable.

Zoning Regulations Stipulate Designated Land Uses

The first step in determining where your agricultural enterprise will be based is to check local and state permitted land uses on your property or a property where you plan to do your processing.

Many counties have specific zoned use areas such as residential, commercial, and rural. If your business is located outside these three specified districts, you will need to determine early in the planning process if your business is in violation of any local zoning codes that may result in citations for non-conforming use. If so, you may be fined or ordered to cease all business operations on the site.

Counties that implement farmland preservation programs involving the purchase of development easements often have zoning regulations that detail permitted land uses on those parcels. Counties often differentiate between what is considered appropriate special exceptions on dedicated agricultural easements and purchased agricultural easements.

Most Permits and License Requirements are Mandated by the State

Permits and licenses allow governments to track the types of businesses operating in an area; ensure a verifiable standardization of services and/or products within certain types of businesses; guard public health; and generate state and local government revenues.

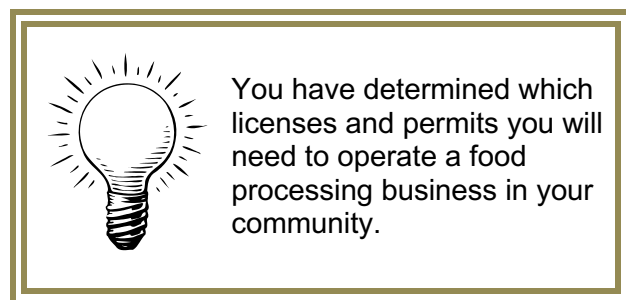
In Maryland, prospective business owners should contact the Maryland Department of Business and Economic Development at (410) 767-0545 to learn about state business

license and permit procedures. Maryland's Business License Information System (BLIS) is an Internet-based system that helps business owners determine the required state permits and licenses. The system also lists county permit and licensing agencies. BLIS may be accessed at www.blis.state.md.us

You will need to contact different county and state licensing and permit agencies depending on the goods you produce.

The county Department of Inspections and Permits issues permits for interior structural changes and/or improvements such as plumbing or electrical renovations. The county Department of Planning and Zoning handles changes to building exteriors, parking lots, setbacks, and landscaping.

Most jurisdictions require a vendor's license or business permit. In Howard County, local business licenses may be obtained through the Howard County Clerk of Courts Office. You'll need to visit several different offices and agencies to obtain all of the required permits and licenses. Don't get discouraged and don't try to short-circuit the process. Time invested in obtaining the necessary operating permits and licenses, both state and local, will save you problems later.



Familiarize Yourself with the Basic Requirements for Starting a Business in Maryland

Regulations and other legal requirements change constantly so you will need to check for the latest versions. An excellent resource for information on starting a new business in

Maryland is available at <http://business.marylandtaxes.com/newbusiness/new.asp>.

Select Your Business Structure

The first step in establishing a business in Maryland is to determine the most appropriate business structure for your operation. The four most common forms are sole proprietorship, partnership, corporation and a limited liability company.

Each structure has certain advantages and disadvantages. Choosing the appropriate organizational structure for your business is one of the most important decisions you will make and may require advice from an attorney, accountant or other professional advisor.

Sole Proprietorships or General Partnerships require no legal entry formalities except compliance with State and local licensing and taxation requirements.

Legal Entities (Corporations, Limited Liability Companies, Limited Partnerships, and Limited Liability Partnerships) must register with the state. Once you have chosen a structure for your business, the next step is to complete the necessary registration requirements. For more information on registration requirements for legal entities, contact:

State Department of Assessments and Taxation Corporate Charter Division

301 West Preston Street, Rm. 809
Baltimore, MD 21201 (410)
767-1340

www.dat.state.md.us

Select and Register Your Business Name

Naming your business is a critical step. You can select a business name yourself, or you can hire a professional to do a search on availability and file the necessary forms.

For information on trade name availability and forms, contact:

State Department of Assessments and Taxation Trade Name Search and Registration

301 West Preston Street
Baltimore, MD 21201 (410)
767-1340
www.dat.state.md.us

For information on corporate name availability and forms, contact:

State Department of Assessments and Taxation

Corporate Name Availability Search
301 West Preston Street
Baltimore, MD 21201 (410)
767-1340
www.dat.state.md.us

CHECKLIST FOR NEW BUSINESSES

- Select your business structure.
- Create or register your business.
- Select or register your business name and entity.
- Obtain personal property tax information.
- Obtain federal, state, county and local tax information.
- Check county and local zoning requirements.
- Obtain all necessary permits and licenses.

Obtain Property Tax Information

Personal Property and Local Taxation Requirements

In Maryland, businesses must pay annual taxes based on the value of their personal property (furniture, fixtures, tools, machinery, equipment, etc.). The Department of Assessments and Taxation administers the valuation process, while counties and towns collect taxes based on the location of the property.

The Department automatically registers corporations, limited liability companies, limited partnerships, and limited liability partnerships for property taxes when these legal entities are formed. All other businesses (sole proprietorships, general partnerships) that own or lease personal property or need a business license are required to: 1) obtain an identification number by registering with the Department of Assessments and Taxation, and 2) file an annual personal property return.

For information regarding personal property assessments, contact:

State Department of Assessments and Taxation Personal Property Division

301 West Preston Street

Baltimore, MD 21201

(410) 767-4991 Sole proprietors, general partnerships (410) 767-1170 Legal entities www.dat.state.md.us

Obtain Federal, State, County and Local Tax Information

All businesses must fulfill their federal and state tax obligations. To determine which state taxes apply to your business, complete Maryland's Combined Registration Application.

For additional information on obtaining and completing the Combined Registration Application, contact:

Taxpayer Registration Assistance Center

301 West Preston Street, Rm. 206

Baltimore, MD 21201 (410)

767-1318

[http://](http://www.comp.state.md.us)

www.comp.state.md.us

Other local taxes in Maryland require no additional registration. If you have any questions about county and local taxes, contact the Finance or Treasurer's Office for the county where the business will be located.

Federal Taxation Requirements Available from the Internal Revenue Service

New businesses should contact the Internal Revenue Service (IRS) to register for an employer identification number; income tax-business and employee withholding; social security; federal unemployment insurance; and other federal taxes.

The IRS will provide kits for three types of businesses: sole proprietorships, partnerships and corporations. For additional information, contact:

Internal Revenue Service

31 Hopkins Plaza

Baltimore, MD 21201

(410) 962-2590 Toll-

free: (800) 829-1040

<http://www.irs.gov>

Check County and Local Zoning Requirements

Be sure you choose a properly zoned location for your business activity. You will also want to determine if there are regulations on business signs and parking.

If you are planning to operate a business from home, check whether your community or county restricts home-based businesses. There may be local covenants that prohibit certain commercial operations in residential areas. To obtain more information on local zoning and building requirements, contact the planning and zoning department in the county where your business will be located.

Check State and Local License Requirements

Business Licenses

A State of Maryland Business License is required for most businesses, including retailers and wholesalers. A trader's license is required for buying and reselling. Business activities that require licenses include, but are not limited to:

Amusements, auctions, chain stores, construction, dry cleaners, farm machinery, garages, hawkers and peddlers, junk dealers, plumbing and gas fitters, restaurants, retail stores,

storage warehouses, traders, and vending machine owners.

To determine whether your particular business activity requires state licensing and any additional licenses and permits, contact the Clerk of the Circuit Court in the county in which your business will be located.

Jurisdictions with municipal corporations may require a license for businesses operating within their corporate limits. If your business is located in a municipal corporation, check with your municipal offices to see if a local business license is required.

You can get an application for a Maryland business license from the Clerk of the Circuit Court in the county in which your business will be located.

Regulatory Licenses

The Department of Labor, Licensing and Regulation is a major occupational and professional licensing agency in the State of Maryland. The Department is also responsible for enforcement of commerce, employment, and workplace and public safety laws.

For most occupations and professions, individuals must meet educational and work experience standards, as well as pass a qualifying examination to obtain a license.

The Division of Employment and Training ((410)767-2400) is responsible for administration of unemployment insurance laws. New businesses are required to pay unemployment insurance taxes and should contact the Division to establish an account.

The Division of Labor and Industry ((410)7672236) protects and promotes the health, safety and employment rights of Maryland

citizens. The Division administers laws governing these areas:

- Maryland Occupational Safety and Health
- Wage Payment
- Employment of Minors
- Prevailing Wage

- Amusement Ride Safety
- Boiler, Pressure Vessel, Elevator and Escalator Safety
- Employment Agencies
- Farm Labor Contractor Registration

The Division of Financial Regulation ((410) 3336808) regulates and, in many instances, licenses the operation of banks, credit unions, consumer loan, sales finance and mortgage companies and collection agencies.

**Maryland Department of Labor,
Licensing and
Regulation 500 N.
Calvert Street
Baltimore, Maryland 21202
(410) 230-6830**

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<http://www.dllr.state.md.us>

A Checklist for Turning on Your Idea

- 1.) Assess your personal skills and commitment to the business you are starting.
- 2.) Research your market, its potential, and your competition. Use local resources and business advisors.
- 3.) Develop your business idea.
- 4.) Check local zoning requirements or restrictions before acquiring or remodeling a property.
- 5.) Obtain a copy of local and state rules, regulations and agencies.