




Accounting For Your Small Business

Overview:

Overview of accounting topics for small business, including accounting principles, budgets and payroll.

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Basic Accounting For Small Businesses

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Basic Accounting Principles-overview



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Introduction

- Creativity and determination will get a business off the ground
- Accounting records will tell you if you are making money or not
- Accounting analysis will help you to make informed decisions about the future of your business

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Why Keep Accounting Records?


- To report business activity to the government
- To obtain cooperation with creditors
- To monitor your business' health and success
- To communicate your business status to advisors



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What Are the Major Components of an Accounting System?


- Paper Records
 - The proof you have of the transactions in your system
 - Primarily kept for government users



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What Are the Major Components of an Accounting System?


- Chart of Accounts
 - The categories into which you will separate transactions
 - Plan your chart of accounts based on the reports you want to end up with
 - Be sure to include accounts for anything that has tax implications, like transactions that might be deductible expenses



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What Are the Major Components of an Accounting System?

- General Ledger
 - Where transactions are recorded and categorized
 - May or may not be visible depending on your system
 - Uses the double entry accounting system (i.e. debits and credits)



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What Are the Major Components of an Accounting System?

- Reports
 - Useful outcome of accounting systems
 - Most accounting systems have a wide variety of reports

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Major Financial Reports

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What Are the Major Financial Statements?

- Balance Sheet
 - A listing of critical account balances at a particular point in time, usually the end of a month
 - Similar in concept to a bank balance
 - Contains a lot of useful information about the health of a business at a particular point in time

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What Are the Major Financial Statements?

- Balance Sheet

WISE ADVERTISING AGENCY Balance Sheet May 31, 19XX	
Assets	
Cash	\$13,705
Accounts receivable	3,860
Prepaid insurance	460
Supplies	360
Land	5,500
Car	\$4,500
Less: Accumulated depreciation	125
Total assets	\$28,160
Liabilities	
Accounts payable	\$ 125
Unearned agency revenue	10,000
Loan payable	6,000
Interest payable	60
Salaries payable	80
Total liabilities	\$16,335
Owner's equity	
Gary Wise, capital	11,925
Total liabilities & owner's equity	\$28,160

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What Are the Major Financial Statements?

- Income Statement or Profit & Loss Statement
 - A summary of transactions that occurred in a particular period of time, usually a month, quarter or year
 - Similar in concept to a bank statement
 - Contains a lot of useful information about the health of a business over a particular period of time

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What Are the Major Financial Statements?

- Income Statement or Profit and Loss Statement

MORTON'S TAXI SERVICE Income Statement For the Year Ended December 31, 19XX	
Taxi revenue	\$144,360
Less expenses	
Salaries expense	\$41,640
Auto rental expense	12,400
Gasoline expense	14,430
Maintenance expense	1,500
License expense	6,200
Tires expense	970
Total expenses	77,140
Net income	\$ 67,220

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What Are the Major Financial Statements?

- Statement of Owner's Equity
 - A summary of owner's equity transactions that occurred in a particular period of time, usually a month, quarter or year
 - Shows the changes in status of an owner's investment/return
 - Has more to do with an owner's activities than the business' health

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What Are the Major Financial Statements?

- Statement of Owner's Equity

VISTA TRANSIT Statement of Owner's Equity For the Month Ended January 31, 19XX		
Beginning balance, Jan. 1		\$ —
Increases		
Owner investments	\$40,000	
Net income	450	40,450
		\$40,450
Decreases		
Owner withdrawals		250
Ending balance, Jan. 31		\$40,200

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What Are the Major Financial Statements?

- Cashflow Statement
 - A summary of all cash transactions that occurred in a particular period of time, usually a month, quarter or year
 - Most accounting systems will produce a cashflow statement based on recorded transactions, but only after the transactions are entered
 - If your business runs tight on cash, this statement should be created in advance for planning purposes

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What Are the Major Financial Statements?

- Cashflow Statement

MATRIX CORPORATION	
Statement of Cash Flows	
For the Year Ended December 31, 19XX	
Cash flows from operating activities	
Details	
Net cash provided (used) by operating activities	\$ 70,000
Cash flows from investing activities	
Details	
Net cash provided (used) by investing activities	(15,000)
Cash flows from financing activities	
Details	
Net cash provided (used) by financing activities	4,000
Net increase (decrease) in cash	\$ 59,000
Cash balance, January 1, 19XX	31,000
Cash balance, December 31, 19XX	\$ 90,000
Schedule of noncash investing/financing activities	
Details	\$ 12,000

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What Can I Learn from a Balance Sheet?

- Balances of Critical Accounts
 - Cash
 - Accounts Receivable
 - Accounts Payable
 - Owner's Equity

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What Can I Learn from an Income Statement?

- Critical Figures
 - Revenue
 - Expenses
 - Net Income

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What Are Some Other Important Things to Look At?

- Critical Business Ratios
 - Current Ratio
 - Measure of whether or not a firm has enough resources to pay its debts over the next 12 months
 - Should be greater than 2, but varies greatly by business type
 - Profit Margin on Sales
 - Measure of profitability in a period
 - Should ideally be an upward trend



What Are Some Other Important Things to Look At?

- Critical Business Ratios
 - Times Interest Earned
 - Measure of earnings versus required interest charges
 - Higher ratios mean a smaller percentage of your earnings are going to creditors
 - Accounts Receivable Turnover
 - Measure of how many times receivables turn over in a year, and therefore average collection period
 - Consider the credit terms you offer – the longer the collection period, the more funds are tied up in receivables, restricting cashflow



What Are Some Other Important Things to Look At?

- Critical Business Ratios
 - Return on Assets or Return on Investment (ROI)
 - Measure of profitability on investments, or how well the investments were used
 - Varies greatly based on risk and return expectations of the owner



What Are Some Other Important Things to Look At?

- Trends
 - Changes in Account Balances or Critical Figures Across Successive Periods
 - Used to Measure a Huge Variety of Things
 - Trending Sales Will Indicate Business Growth
 - Trending Interest Will Indicate Reduction of Interest Expenses
 - Trending Accounts Receivable Turnover Will Indicate Results of Increased Collection Efforts



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What Are Some Other Important Things to Look At?

- Trends



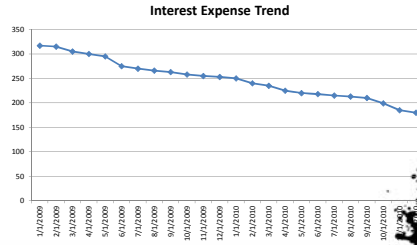
Sales Trend

Period	Sales
1/1/2000	45000
3/1/2000	100000
5/1/2000	95000
7/1/2000	90000
9/1/2000	100000
11/1/2000	35000
1/1/2001	55000
3/1/2001	125000
5/1/2001	95000
7/1/2001	100000
9/1/2001	95000
11/1/2001	105000
1/1/2002	40000
3/1/2002	70000
5/1/2002	115000
7/1/2002	105000
9/1/2002	100000
11/1/2002	110000
1/1/2003	40000

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What Are Some Other Important Things to Look At?

- Trends



Interest Expense Trend

Period	Interest Expense
1/1/2000	320
2/1/2000	310
3/1/2000	300
4/1/2000	290
5/1/2000	280
6/1/2000	270
7/1/2000	260
8/1/2000	255
9/1/2000	250
10/1/2000	245
11/1/2000	240
12/1/2000	235
1/1/2001	230
2/1/2001	225
3/1/2001	220
4/1/2001	215
5/1/2001	210
6/1/2001	205
7/1/2001	200
8/1/2001	195
9/1/2001	190
10/1/2001	185
11/1/2001	180
12/1/2001	175

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What Are Some Other Important Things to Look At?

- Trends

Accounts Receivable Turnover Trend

Date	Turnover
1/1/2000	22.8
2/1/2000	22.5
3/1/2000	22.8
4/1/2000	23.0
5/1/2000	23.2
6/1/2000	23.0
7/1/2000	23.2
8/1/2000	23.3
9/1/2000	23.4
10/1/2000	23.5
11/1/2000	23.4
12/1/2000	23.4
1/1/2001	23.5
2/1/2001	23.6

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Budgets

Budgeting is critical in business, no matter what size your business is

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Small Business Budgeting

- What is a Budget?
 - Forecast of all cash sources and cash expenditures.
 - Most commonly covers a 12-month period
 - At the end of the year, anticipated income and expenses developed in the budget are compared to the actual performance of the business
 - Contains 3 main elements: Sales, Expenses & Profit.

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Small Business Budgeting



- Why Do You Need A Budget?
 - Helps you decide whether you have enough money to achieve your financial goals
 - Allows you to anticipate problems before they occur and alter your plans to prevent potential problems
 - Help convince a loan officer that you know your business and have anticipated its needs

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Small Business Budgeting

- The Budgeting Process
 - Before you can create a budget
 - ✓ Do a reality check
 - ✓ Based on figures that can be supported by reasonable expectations.
 - Specify a timeframe
 - ✓ Often based on fiscal year, but you may also want to budget on a monthly, quarterly or semi-annual basis
 - Estimate Income and Expenses

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Small Business Budgeting

- You must answer three questions:
 - ✓ How much net profit do you want the business to generate during the calendar year?
 - ✓ How much will it cost to produce that profit?
 - ✓ How much sales revenue is necessary to support both profit and costs?


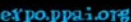


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Small Business Budgeting

**AAA Pool Supply Company
Budget**

	Amt. (\$)	% of Sales
Sales	523,063	100%
Cost of goods	366,144	70%
Gross profit margin	156,919	30%
Operating expenses:		
Advertising	3,605	0.7%
Depreciation	4,000	0.8%
Insurance	2,900	0.6%
Legal and accounting expenses	4,142	0.8%
Office expenses	2,995	0.6%
Rent	24,000	4.6%
Repair & maintenance	437	0.1%
Salaries	34,650	6.6%
Telephone and utilities	6,683	1.3%
Miscellaneous	8,507	1.6%
Total operating expenses	91,919	17.6%
Net Profit	65,000	12.4%


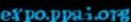


Payroll




Payroll for Small Business

- All wages are subject to federal employment taxes unless the payments are specifically exempted under the Internal Revenue Code.
- Wages subject to federal employment taxes generally include all pay that you give to an employee for services performed.
- The pay may be in cash or in other forms. It includes salaries, nonqualified deferred compensation, vacation allowances, bonuses, commissions, and fringe benefits.

Payroll for Small Business

- Each state has adopted its own unique set of employment laws. As a result, each state has its own policies, procedures, forms, and requirements.
- Almost all states have adopted a state income tax. Each employee's wages are subject to state income tax withholding.
- These amounts are deposited with the appropriate state tax agency and quarterly and/or annual reports are prepared to summarize the payroll activity of the employer throughout the reporting period.

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Payroll for Small Business

- There are generally three types of federal employment taxes:
 - Employee Income Tax Withholding
 - ✓ Amount withheld from employee's wages to offset projected income tax
 - Federal Insurance Contributions Act (FICA)
 - ✓ Consists of 2 components (Social Security & Medicare)
 - ✓ Provides for old age, survivors and disability insurance (OASDI) and hospital insurance (HI)
 - ✓ The OASDI component is financed through the social security portion of FICA and the HI component (for persons 65 or older) is financed through the medical portion
 - Federal Unemployment Tax Act (FUTA)

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Thank you so much for your time and attention.



Questions?



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