

# Chapter 9

## **Plan and Track Your Finances**

**9.1 Finance Your Business**

**9.2 Pro Forma Financial Statements**

**9.3 Record Keeping for Businesses**

# Assess Your Financial Needs

Itemize **startup costs**.  
Determine the amount of  
**capital** required to start  
your business.

STARTUP COSTS Walters Electric	
Item	Estimated Cost
<b>Equipment and supplies</b>	
Computers (3 @ \$1,500)	\$ 4,500
Scanner	175
Cash registers (2 @ \$1,800)	3,600
Fax machine	400
Supplies	300
Subtotal	<u>\$ 8,975</u>
<b>Furniture and fixtures</b>	
Desks (4 @ \$400)	\$ 1,600
Chairs (8 @ \$75)	600
Subtotal	<u>\$ 2,200</u>
<b>Vehicles</b>	
Delivery truck	\$10,000
Automobile	8,000
Subtotal	<u>\$18,000</u>
<b>Remodeling</b>	
Drywall replacement	\$ 1,000
Electrical work	2,500
Paint	1,000
Carpet	3,000
Subtotal	<u>\$ 7,500</u>
<b>Legal and accounting fees</b>	<u>\$ 3,000</u>
<b>Total</b>	<u><u>\$39,675</u></u>

# Personal Financial Statement

**net worth** = assets — liabilities

**personal financial statement** = personal assets — personal liabilities

PERSONAL FINANCIAL STATEMENT			
Felicia Walters			
Assets		Liabilities	
Cash	\$ 5,000	Car loan	\$ 6,900
Checking account	13,500	College loan	4,000
Certificate of Deposit	6,000	Credit cards	1,300
Stock	10,000		
Computer equipment	3,000		
Coin collection	<u>2,500</u>		
Total assets	\$40,000	Total liabilities	<u>\$12,200</u>
Total assets – Total liabilities = Net worth			
\$40,000 – \$12,200 = \$27,800			

# Equity Capital

## ■ **debt-to-equity ratio**

- the relation between the dollars you have borrowed and the dollars you have invested in your business

■ The higher percentage of your own money that you have invested, the easier it will be for you to get others to invest.

## ■ **equity capital**

- the money invested in a business in return for a share in the profits of the business

■ Sources of **equity** include:

- Personal Contributions
- Friends and Relatives

## ■ **Venture Capitalists**

- individuals or companies that make a living investing in startup companies

# Debt Capital

## ■ debt capital

- money loaned to a business with the understanding that the money will be repaid
  - usually with **interest**

## ■ Friends and Relatives

- determine how the loan will affect your relationship
- prepare a formal agreement regarding repayment terms

# Commercial Bank Loans

## ■ secured loans

- loans that are backed by collateral

## ■ unsecured loans

- loans that are not guaranteed with collateral only made to creditworthy customers

## ■ collateral

- property that the borrower forfeits if he or she defaults on the loan

## Types of secured loans include the following

1. line of credit
2. long-term loan
3. accounts receivable financing
4. inventory financing

## Reasons a bank may not lend money include:

- ☐ The business is a **startup.**
- ☐ A **lack of:**
  1. a solid business plan
  2. adequate experience
  3. confidence in the borrower
  4. personal investment

# Other sources of loans include:

1. Small Business Administration
2. Small Business Investment Companies
3. Minority Enterprise Small Business Investment Companies
4. Department of Housing and Urban Development
5. The Economic Development Administration
6. State Governments
7. Local and Municipal Governments



# Cash Flow Statement

## ■ cash flow statement

- an accounting report that describes the way cash flows into and out of your business over a period of time

# Forecast Receipts

Estimate monthly cash receipts

FORECASTED RECEIPTS			
Walters Electric			
January 20—			
Cash sales			
	Quantity		
	Sold	Price	Total
CFL bulbs	20	\$ 15	\$ 300
Indoor light fixtures	10	155	1,550
Outdoor lights	6	175	1,050
Subtotal			<u>\$2,900</u>
Accounts receivable			<u>\$ 300</u>
Bank loan			<u>\$1,000</u>
Total			<u><u>\$4,200</u></u>

# Forecast Disbursements

estimate monthly cash disbursements

FORECASTED DISBURSEMENTS	
Walters Electric	
January 20—	
Disbursement	Amount
Cost of goods	\$2,400
Rent	900
Utilities	100
Salaries	2,000
Advertising	700
Supplies	100
Insurance	75
Payroll taxes	175
Other	50
Total	<u>\$6,500</u>

# Prepare the Cash Flow Statement

- **net cash flow** = cash receipts — cash disbursements
- Tracking monthly cash flow statements
  - enables you to anticipate periods of **positive and negative** cash flow

## Economic Effects on Cash Flow

- Changes in the **economy** can dramatically effect the cash flow of businesses.
- Business owners should make conservative estimates.

## PRO FORMA CASH FLOW STATEMENT

Walters Electric  
January–June 20—

	Jan	Feb	Mar	Apr	May	June
Cash receipts	<u>\$4,200</u>	<u>\$5,410</u>	<u>\$5,750</u>	<u>\$6,320</u>	<u>\$7,375</u>	<u>\$8,130</u>
Cash disbursements						
Cost of goods	\$2,400	\$2,520	2,520	2,640	3,300	3,480
Rent	900	900	900	900	900	900
Utilities	100	100	100	100	100	100
Salaries	2,000	2,000	2,000	2,000	2,000	2,000
Advertising	700	700	700	700	700	700
Supplies	100	115	130	150	150	150
Insurance	75	75	75	75	75	75
Payroll taxes	175	175	175	175	175	175
Other	50	50	50	50	50	50
Total disbursements	<u>\$6,500</u>	<u>\$6,635</u>	<u>\$6,650</u>	<u>\$6,790</u>	<u>\$7,450</u>	<u>\$7,630</u>
Cash Flow	<u><u>-\$2,300</u></u>	<u><u>-\$1,225</u></u>	<u><u>-\$ 900</u></u>	<u><u>-\$ 470</u></u>	<u><u>-\$ 75</u></u>	<u><u>\$ 500</u></u>

# Income Statement

## ■ income statement

- shows **revenues/sales and expenses** incurred over a period of time
  - Expenses- expenses paid to operate your business
  - COGS
- Gross revenue/sales-**returns**=net sales
  - **The customer returned the product & received their money back so you LOST that sale**
- shows the **profit or loss** for the time period

# Prepare a Pro Forma Income Statement

- The long-term growth of your business can be demonstrated by a pro forma income statement prepared for **multiple years**.
- The **pro forma income statement** consists of:
  - Revenue \$75,000
  - Cost of goods sold \$20,000
  - Gross profit \$\_\_\_\_\_
  - Operating expenses \$25,000
  - Net income before taxes \$\_\_\_\_\_
  - Taxes \$2,000
  - Net income/loss after taxes \$\_\_\_\_\_

## PRO FORMA INCOME STATEMENT

Walters Electric, 20 —

	Year 2	Year 3
Revenue	\$115,000	\$125,000
Cost of goods sold	55,400	60,000
Gross profit	<u>\$ 59,600</u>	<u>\$ 65,000</u>
Operating expenses		
Salaries	\$ 26,705	\$ 27,315
Rent	10,800	10,800
Utilities	1,230	1,260
Advertising	1,200	1,200
Insurance	900	900
Supplies	600	615
Other	615	615
Total operating expenses	<u>\$ 42,050</u>	<u>\$ 42,705</u>
Net income before taxes	\$ 17,550	\$ 22,295
Taxes	7,020	8,918
Net income/loss after taxes	<u><u>\$ 10,530</u></u>	<u><u>\$ 13,377</u></u>



# Balance Sheet

- **balance sheet**

- a financial statement that lists
  - what a business **owns**
  - what a business **owes**
  - how much a business is **worth at a point in time**

- **assets = liabilities + owner's equity**

# Prepare a Pro Forma Balance Sheet

- **fixed assets (FA)**

- used for many years
- Building, land, or equipment

- **current assets (CA)**

- items that are used up in normal business operations
- Supplies, materials, inventory, cash, a/r

- **accounts receivable (A/R)**

- the amounts owed to a business by its credit customers

# Debt-liability-owe

## **long-term liabilities (LTL)**

debts that are payable over a year or longer

Loans, mortgage

## **current liabilities (CL)**

debts that must be paid in full in less than a year

a/p, short term loan

## **accounts payable (A/P)**

amounts owed to vendors for merchandise purchased on credit

### **allowance for uncollectible accounts**

the amount a company estimates it will not receive from customers

### **depreciation**

the lowering of an asset's value to reflect its current worth

## **Equity**

Ownership in the company, amount you invested

**capital**

## PRO FORMA BALANCE SHEET

Walters Electric  
December 31, 20—

### Assets

#### *Current assets*

Cash	\$ 1,000
Accounts receivable	8,000
Less allowance for uncollectible accts.	-500
Inventory	14,000
Total current assets	<u>\$22,500</u>

#### *Fixed assets*

Equipment	\$ 8,975
Less depreciation	-1,795
Furniture	2,200
Less depreciation	-220
Vehicles	18,000
Less depreciation	-3,600
Total fixed assets	<u>\$23,560</u>
Total assets	<u><u>\$46,060</u></u>

### Liabilities

#### *Current liabilities*

Accounts payable	\$12,000
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#### *Long-term liabilities*

Loans payable	\$17,900
Total liabilities	<u>\$29,900</u>

### Owner's Equity

Felicia Walters	<u>\$16,160</u>
Total liabilities and owner's equity	<u><u>\$46,060</u></u>

# Recording Transactions

## ■ Transaction

- any business activity that changes assets, liabilities or net worth

## ■ Journals

- accounting records of the transactions you make for
  1. sales
  2. cash payments
  3. cash receipts
  4. purchases

## ■ General ledgers

- A general ledger is made up of accounts.

## ■ Account

- an accounting record that provides financial detail for a particular business item

## ■ Subsidiary ledger

- used for accounts payable to show in detail the transactions with each vendor from whom merchandise is purchased on account

## ■ Aging table

- a record keeping tool for tracking accounts receivable shows how long it takes customers to pay their bills

# Aging Table

Customer	Amount	0–30 days	31–60 days	over 61 days
E. Kwon	\$175.23	\$175.23		
P. Mossett	\$106.20		\$106.20	
M. Stern	\$82.34			\$82.34
Totals	\$363.77	\$175.23	\$106.20	\$82.34
Percent of total	100%	48%	29%	23%

# Business Records

- A business **checking account** should be established.
- **check register**
  - booklet (or electronic register) where you record information for each check written
    - amount
    - date
    - name of person or business receiving your payment
- **Balance Your Account**
  - You should balance your account each time a transaction occurs.
- **Reconcile Your Account**
  - Each month you should reconcile your bank statement with your check register.
- **Payroll**
  - a list of people who receive salary or wage payments from a business



## BANK RECONCILIATION

Bank statement balance	\$2,151.00	Balance from checkbook	\$2,501.15
Add outstanding deposits	<u>660.00</u>	Add deposit not recorded	<u>0.00</u>
Subtotal	\$2,811.00	Subtotal	\$2,501.15
Deduct outstanding checks:		Deduct bank fees	<u>12.00</u>
#345                   \$ 60.00		Balance less fees	\$2,489.15
#366                   105.60			
#369 <u>150.00</u>		Add interest earned	<u>6.25</u>
Total outstanding checks	<u>315.60</u>		
Adjusted bank balance	<u><u>\$2,495.40</u></u>	Adjusted checkbook balance	<u><u>\$2,495.40</u></u>

## ■ Income Tax

- Businesses that earn a profit must pay income tax **quarterly**

## ■ Payroll Taxes and Deductions

- deduct taxes from employees paychecks
  - submit taxes to the government
- unemployment insurance taxes
- Social Security taxes
- voluntary deductions

## ■ Sales Tax

- Sales taxes are based on a percentage of sales.
- Each month you deposit sales tax into a government owned account.