Keeping Track of Your Money: Crash Course Entrepreneurship #15

Crash Course: Business - Entrepreneurship
https://youtube.com/watch?v=_HK5gpg39pY
https://nerdfighteria.info/v/_HK5gpg39pY

You know what conversation starter will make you the life of the party?

Spreadsheets. Ha... maybe not unless it's a wild accounting party, or if everyone really loves math.

Even then… ehhhh. Honestly, "spreadsheets" are kind of the vegetables of the business world -- the very idea of them makes some people queasy. But that's ok!

They can be intimidating, but they're not impossible to understand. Today we're going to learn to love 'em, because basic accounting can make or break a business. If we lose track of expenses or overestimate a revenue stream, we might end up questioning where all the money has gone.

The key is using organized systems and knowing the right vocabulary. And by the end of this episode, we'll be bookkeeping pros... or at least able to talk about balance sheets and profitability with an accountant. I'm Anna Akana, and this is Crash Course Business: Entrepreneurship. [Theme Music Plays] Every entrepreneur has to seriously think about /how/ we're going to take in money and where we're going to put it.

The place (and it could be a digital place) where customers hand over money in exchange for a product or service is called the point of sale. Cash registers, credit card machines, the checkout page on a website -- these are all points of sale. Now, we want to make the buying process as painless as possible so customers will feel good about doing business with us.

And having a seamless point of sale system is a big part of that. Here are a few options. Some of the most popular electronic systems are created by Shopify, Square, and PayPal.

Both Shopify and Square help you set up e-commerce sites and have hardware to use in physical stores to register sales. And PayPal is an online checkout system that makes it really easy for customers to make purchases. These are great options for entrepreneurs with a lot of transactions or who are selling a product.

If your business isn't set up for immediate transactions, you can send customers invoices -- basically, itemized records -- to get paid. Many freelancers do this! Customers may want to pay by credit card, so you might still look into one of those systems we mentioned.

If you're using a system that can process credit cards, there will probably be a 2-4% processing fee, so you'll want to take that extra cost into account when pricing your products. Then, of course, we're going to need somewhere to put all the revenue, like a business bank account. This is just like a personal account, except it has a business name on it.

Unless your personal account is just under your mattress. In which case, it's VERY different. This move is all about organization.

Imagine scrolling through your transaction history if you only had one account for both you and your business. It's just a swamp of latte receipts, supply runs, grocery bills, production costs, and more. Some of those were personal lattes and some were business lattes.

When tax season rolls around in a few months, are you really going to be able to remember the difference? Most importantly, we want to be able to tell, at a glance, the financial health of our business. If calculating profit becomes a guess-and-check walk through of every purchase we've made this year, that simple "revenue minus expenses" equation is suddenly much more complicated.

To get set up in the US, you'll need your tax identification number, the official name your company is operating as, and most likely proof from your Secretary of State as to what kind of business entity you're running. Depending on whether you've decided to be an LLC, a corporation, a co-op, or something else, you may need additional forms. Start with your current bank and see what they offer for business accounts.

But don't be afraid to shop around. Can you find free checking? Free savings?

Better loyalty rewards? After getting money from customers and storing it safely, we want to keep track of how much we have, and how much we've spent. And some idea of how well we're doing would also be nice.

We can track almost anything and make tons of beautiful graphs, but there are three essential reports to measure our business's financial success. These three reports are also well understood by other business people who might be trying to help us out in the future. An income statement, sometimes called a profit and loss statement or PNL, is a report that shows how much money we've spent and how much we've made during some period of time, usually a month or a year.

Basically, it tracks the total revenue, total cost of goods sold, the total expenses, and comes up with our net income at the bottom -- which is total revenue minus costs of goods sold; minus selling, general, and administrative expenses; minus all our other expenses like depreciation of equipment or taxes. It's important to write down every revenue stream and every expense so we're getting a complete picture of what our net income is. The second report is a balance sheet.

This is a snapshot of our business's financial health at any point in time. So on the income statement, we looked at just December or just 2019, but here we're looking at all our money for all time. And there are three sections: The balance sheet will show our assets -- not just our cash, but anything we could convert into cash within one year like property, equipment, investments, or intellectual property.

Assets are broken up into two categories. Current Assets are anything we could convert into cash within one year, like cash or inventory. And Fixed Assets are purchased for long-term use, so we probably can't convert them quickly into cash, like land or buildings.

It also shows our liabilities -- all our financial obligations and debts, like loans, mortgages, revenue we're still waiting on, and expenses. Like with assets, liabilities are broken up into two categories. Current Liabilities are debts that must be satisfied within one year from the balance sheet date.

And Long Term Liabilities are debts that aren't due within one year of the date of the balance sheet, like mortgages. And it shows our equity -- or the amount of money that would be returned to our shareholders if all our assets were turned into cash and all our debt was paid off. Many of us may not have shareholders yet, but we may have a friend or family member lying around that we just gotsta pay back.

These three things /balance/ -- hence the name balance sheet. Equity is really just assets minus liabilities, which we rearrange to make the business equation Assets equals Equity plus Liabilities. Finally, the third statement we should be familiar with is a cash flow statement which tells us how much money has moved in and out of our business in a specific time period (again, like in a month or a year).

There are three sections to this statement too: The operations cash flow shows how much cash was spent or earned from running the business. So this includes revenue, expenses, and taxes. The investment cash flow shows how much our business sold or spent on property, plant, and equipment, or PP&E;.

This is stuff like selling old equipment or purchasing a new building. And the financial cash flow shows the amount of money our business got in loans or paid in dividends to shareholders. We can remember these three sections with a made-up word “OIF.” And all three are added up to show the net cash flow for our business.

Since we’re looking at a specific snapshot in time, we can add in whatever cash we had from before to see the total amount of cash our business is sitting on. Let’s look at an example in the Thought Bubble. Ronnie has his own event planning business, and this year he’s planned some weddings, quinceaneras, bat mitzvahs, and fancy pool parties.

But is his business doing well? On his income statement for January through April, we see he paid for SG&A; costs like his website and his monthly accounting software subscription, but he had revenue from planning three events. His net income is positive, meaning he made a profit for these months.

Nice! On his balance sheet, we can see he received a bank loan, which is a liability. This loan is considered a current liability if it will be paid off within a year of the balance sheet date, otherwise it would be a long-term asset.

He spent almost all of this cash from the loan on event decor and a tech setup -- a computer and tablet and one of those headset things all official event planners seem to have. All this stuff, plus any cash he has from his net income are his assets. Now, to calculate Ronnie’s equity, we subtract the total liabilities from the total assets and there’s how much he actually owns!

Boom. Balance. Finally, on his cash flow statement, we see three categories.

The operations cash flow includes revenue from his customers and any cash leftover from the loan. So his operations cash flow is positive. The investment cash flow includes the money he spent purchasing new decorations and upgrading his tech setup.

Since he didn’t earn any money here, his investment cash flow is negative. And the financial cash flow has the bank loan that funded all his upgrades. His financial cash flow is positive because that money came into his business.

So overall, Ronnie’s making money, though he does still need to pay off that bank loan. Hopefully that new decor and tech will get him even more business! Thanks, Thought Bubble!

To create these statements, we can make our own spreadsheet for free, but that might require lots of data entry. [Yay spreadsheet fun...] Accounting software can be really efficient. And depending on our price range, many accounting software systems have options for generating invoices and can play nice with our point of sale system. Since many people are intimidated by anything accounting-related (not us, of course!) there are tons of great choices.

HubSpot has collected a list with a quick analysis and cost breakdown and we put a link in the description. Some of the most common choices are Quickbooks, Freshbooks, and Xero. Quickbooks is by Intuit, the same company that creates TurboTax, and is probably the most well-known software for businesses. It can invoice people and interacts with many point of sale systems. Freshbooks is also popular and offers very similar options to Quickbooks, but is usually recommended for subscription-based businesses. And Xero is what Square recommends.

So if you’re using Square as your point of sale system, you might try Xero because they work really well together and pricing can be a bit friendlier. Do your research to make sure whatever you pick works well with the systems you already have, but ultimately, you’ll get very similar results with any of these. As we make more money, we might want to bring on a key partner like a bookkeeper to handle the data, or an accountant to manage projects and taxes.

There are even services like Bench or SLC Bookkeeping that will act as virtual accountants, but a local firm will also be glad to help you. If this is the path you want to take, you should still review your income statements, balance sheets, and cash flow statements regularly and know what they say. This is all the behind-the-scenes action of your business, and you don’t want to miss out or get taken advantage of.

Remember, you’re in charge! So consult everyone you need to understand reports and strategize, but make sure you’re still the one making the final call. So we have these three reports as printouts or PDFs, but how do we read them?

Ahh yes. Mmmhmm, very good. Oh!

Uh, this says my gross margin is half my dividend payout ratio! That can’t be right. There are hundreds of different metrics we can use to see how efficient and profitable our company is, called accounting ratios.

Because there are so many of these, we suggest pulling up our old friend Investopedia to research what could matter to /your/ business. This is where finding a key partner who knows their stuff can really help too! And finally, we’ll say it again: don’t forget to file your taxes.

You’ll probably have to submit one or more of your financial reports along with the tax forms. Good thing you’re prepared. Depending on the country and type of business, there will probably be different requirements.

In the US, you can find most of what you need online. For federal taxes, visit IRS.gov. For State taxes, look on your Secretary of State’s website or visit your state department of revenue.

And for city or municipal taxes, Drop a haypenny in the town fountain and whistle "she'll be comin' round the mountain. No, seriously, you also check your city’s website. The bottom line is[... on your income statement!

But really,] bookkeeping can be fun, or at the very least understandable. Set up systems to manage your revenue, and invest in software or people to keep your business organized and profitable. Next time, we’ll keep talking about money and look at funding options for when you’re just starting out.

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