

***It sounds extraordinary but it's a fact that
balance sheets can make fascinating reading.
– Mary Archer***

ACCOUNTING

This chapter exposes the entrepreneur to business accounting issues involved in starting a business. Rather than trying to provide all the answers, this chapter is oriented towards raising most of the important issues an entrepreneur should consider when starting a business and creating the three critical financial documents necessary for a standard business plan: ***The Monthly Cost of Living Worksheet***, the ***One-Year Cash Flow Projection***, and the ***Sources and Uses Explanation***.

- **Monthly Cost of Living Worksheet**

The purpose of the Monthly Cost of Living worksheet is to determine whether you need to draw cash out of the business in order to live. First, estimate your family's monthly *personal* expenses (count only the money you would spend if you did not start a business). Remember, this is just an estimate and exact amounts are not required. The family's monthly personal costs are reduced by monthly "take home" income you (or your spouse) expect to receive from sources *other than* the new business. If your monthly expenses exceed income from other sources, the shortfall needs to be drawn (and budgeted) in your first year's business plan. If your personal living expenses are "covered" by other income, then you don't need to draw any money out of the business.

- **One-Year Cash Flow Projection**

The purpose of the One-Year Cash Flow Projection is to plan the business' first year cash flow (the amount and source of revenue coming in to the business and the amount and type of expenses associated with operating the business). Basically the total Sources of Cash *must at least equal* the total Uses of Cash. That is, you can't spend money you don't have.

- **Sources and Uses Explanation**

A number is assigned to every item shown on the ***One-Year Cash Flow Projection***. For every amount you place on this document, you need to explain (annotate) how you arrived at the dollar amount. The annotations should be numbered and the annotation number should match the number on the ***One-Year Cash Flow Projection*** line item.

The most important annotation in the ***One-Year Cash Flow Projection*** is in the Sources of Cash, entitled, "3. Cash Receipts from the Business." At a minimum, the student must be able to provide the following information: (a) the number of customers (on average) the business intends to serve (contract with) on a daily, weekly or monthly basis; (b) the number (and types) of products sold or hours of services billed per customer; and (c) the sales price of the various products sold or billing price of services rendered. If the business owner does a good job on annotating this line item in terms of number of customers and amount spent by each, he/she will get a much clearer picture

of the nature of his/her marketing plan, sales prices, staffing, and equipment and facility needs.

For example, suppose you are planning to operate a child-care business out of your home. You estimate that you need to have 6 children (on average) per day for 5 days per week. You have determined that a reasonable market rate for you to charge is \$15 per day per child. You plan on running the child-care business 50 weeks out of the year. On the **One-Year Cash Flow Projection**, in the Sources of Cash, entitled “3. Cash Receipts from the Business,” you would enter \$22,500. In the annotations (which follow) under “3. Cash Receipts from the Business” you would explain the \$22,500 amount by stating: 6 customers (children) per day x \$15 each x 5 days per week x 50 weeks per year is \$22,500 for the year. In addition, and more importantly, you can plan your marketing, pricing, staffing, and facility to acquire and accommodate your expected customer volume.

Sources of Cash - List the amount of your personal savings and the amount of any loans you expect to put into the business in the first year. The hardest part is estimating the amount of money your business will generate during the first year. This is one of the most difficult and most useful exercises. In estimating the amount of money your business will generate, you must determine the sales price of your product (or service) and the number of products (or customers) you need to sell.

Uses of Cash - List the amount of cash you intend to spend in your business for each line item. You may need to add expense descriptions that are not listed. You don't have to use all the descriptions listed. Remember that you won't be spending money for assets you already own and plan on using in your business. Remember that a numbered annotation must explain how you estimated the amount of each expense item. Note that your personal draw, line 24, is the annualized (times 12) number from the **Monthly Cost of Living Worksheet**.

By completing the **One-Year Cash Flow Projection**, you may determine that you need more sales (or service volume) and/or you need to charge a higher price in order to cover your first year cash needs. Many of your marketing decisions will be affected by your analysis performed on the **One-Year Cash Flow Projection**.

THE BOTTOM LINE:

This section of your business plan provides a detailed snapshot of your personal and business financial outlook and provides some (not all) of the basic information you will need if plan on pursuing financing.