Financial Statements in Plain English

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We will cover

• The two main financial statements:
  • Profit and Loss Statements
  • Balance sheets
• How to tell if your financial statements are wrong in less than 97 seconds
About Ruth King
First – Why Should You Care?

• Keep you from being surprised

• Make good business decisions based on accurate information
The Good News!

• I don’t expect you to become a bookkeeper!
The Good News!

- You can delegate the day-to-day bookkeeping.

- You cannot abdicate the financial side of your business. You must review and take action.
The Difference between P&L’s and Balance Sheets

- P&L is for a specific period of time.
- Balance sheet started the day the business started and will end the day the doors are closed.
Profit and Loss (P&L) Statements

• Each department has its own P&L.

• This is your score card.

• If you have a great month – you can’t celebrate a long time.

• If you have a bad month – you can’t be frustrated for a long time.
Profit and Loss Statements

- Profit and loss (P&L) statements are sometimes called income statements
- Tells you profit or loss – not how much money you have in the bank!
Profit and Loss Statements

- Revenue (sales)
- Cost of goods sold (COGS)
- Overhead
- Net Operating Profit
- Other income/expense
- Net Profit
Revenue

- What did you sell? (NOT what did you collect)
- Did you make budget?
- Recurring revenue generated?
Cost of Goods Sold (Direct Exp)

• An expense incurred because you sold something:
  • Materials
  • Labor
  • Parts and equipment
  • Commissions/SPIFF’s
  • Freight
Cost of Goods Sold (Direct Exp)

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  - Labor
  - Parts and equipment
  - Commissions/SPIFF’s
  - Freight
Cost of Goods Sold (Direct Exp)

• Watch out for:
  • Materials waste
  • Unbillable labor
  • Meeting labor estimates
  • Paying for commissions when the company hasn’t been paid
  • Excessive freight charges
Cost of Goods Sold (Direct Exp)

- Watch out for financial fruit salad:
  - Apples and oranges accounting
  - Make sure revenues and direct expenses are in the same month
  - Make sure all material expense has been assigned to a job and is not inventory
Profit and Loss Statements

• What’s gross profit?
• Is it the same as gross margin?
Profit and Loss Statements

- Gross profit is revenues minus COGS
- Gross margin is gross profit divided by sales

- Gross profit is always dollars
- Gross margin is always percentage
### Why Gross Margins Don’t Matter

<table>
<thead>
<tr>
<th>Customer</th>
<th>Sell Price</th>
<th>GP</th>
<th>GM</th>
<th>OH/hr</th>
<th># Hours</th>
<th>Net Profit</th>
<th>Net Profit/hr</th>
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</thead>
<tbody>
<tr>
<td>JE</td>
<td>$12,903.00</td>
<td>$5,227.01</td>
<td>40.51%</td>
<td>60.20</td>
<td>39.00</td>
<td>2879.21</td>
<td>$73.34</td>
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<td>RP</td>
<td>$11,293.00</td>
<td>$4,918.10</td>
<td>43.55%</td>
<td>60.20</td>
<td>53.50</td>
<td>1697.40</td>
<td>$31.11</td>
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<td>MC</td>
<td>$13,248.00</td>
<td>$5,119.03</td>
<td>38.64%</td>
<td>60.20</td>
<td>48.50</td>
<td>2199.33</td>
<td>$45.33</td>
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<td>CF</td>
<td>$15,078.00</td>
<td>$7,074.60</td>
<td>46.92%</td>
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<td>38.00</td>
<td>4787.00</td>
<td>$125.09</td>
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<td>EK</td>
<td>$9,686.00</td>
<td>$4,495.27</td>
<td>46.41%</td>
<td>60.20</td>
<td>53.50</td>
<td>1515.37</td>
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<tr>
<td>IR</td>
<td>$23,752.00</td>
<td>$11,809.49</td>
<td>49.72%</td>
<td>60.20</td>
<td>81.50</td>
<td>6903.19</td>
<td>$84.67</td>
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<td>GP</td>
<td>$3,948.00</td>
<td>$2,488.82</td>
<td>63.04%</td>
<td>60.20</td>
<td>25.00</td>
<td>983.82</td>
<td>$39.96</td>
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<td>HT</td>
<td>$5,644.00</td>
<td>$2,272.84</td>
<td>40.27%</td>
<td>60.20</td>
<td>59.00</td>
<td>-1278.96</td>
<td>-$21.37</td>
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<td>DT</td>
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<td>$4,971.12</td>
<td>45.11%</td>
<td>60.20</td>
<td>72.00</td>
<td>636.72</td>
<td>$8.11</td>
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<tr>
<td>RR</td>
<td>$12,082.00</td>
<td>$6,498.91</td>
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<td>60.20</td>
<td>54.00</td>
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<td>KP</td>
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<td>60.20</td>
<td>32.75</td>
<td>3019.27</td>
<td>$92.85</td>
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<td>HG</td>
<td>$16,620.00</td>
<td>$6,852.43</td>
<td>41.23%</td>
<td>60.20</td>
<td>103.00</td>
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<td>$6.03</td>
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<td>DP</td>
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<td>60.20</td>
<td>150.00</td>
<td>2682.84</td>
<td>$17.50</td>
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<tr>
<td>DG</td>
<td>$2,519.00</td>
<td>$1,624.76</td>
<td>64.50%</td>
<td>60.20</td>
<td>14.75</td>
<td>736.81</td>
<td>$49.49</td>
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<tr>
<td>DG</td>
<td>$8,534.00</td>
<td>$4,336.98</td>
<td>50.82%</td>
<td>60.20</td>
<td>54.00</td>
<td>1086.18</td>
<td>$20.13</td>
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<td>LP</td>
<td>$8,822.00</td>
<td>$1,712.35</td>
<td>19.41%</td>
<td>60.20</td>
<td>15.25</td>
<td>794.30</td>
<td>$52.00</td>
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<tr>
<td>ML</td>
<td>$7,489.00</td>
<td>$3,808.91</td>
<td>50.86%</td>
<td>60.20</td>
<td>39.00</td>
<td>1461.11</td>
<td>$37.91</td>
</tr>
<tr>
<td>RT</td>
<td>$8,545.00</td>
<td>$4,390.42</td>
<td>51.38%</td>
<td>60.20</td>
<td>30.25</td>
<td>2569.37</td>
<td>$84.58</td>
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<tr>
<td>RS</td>
<td>$10,931.00</td>
<td>$3,559.13</td>
<td>32.56%</td>
<td>60.20</td>
<td>90.00</td>
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<td>-$20.11</td>
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<td>TJ</td>
<td>$9,868.00</td>
<td>$3,910.69</td>
<td>39.63%</td>
<td>60.20</td>
<td>60.00</td>
<td>298.69</td>
<td>$4.68</td>
</tr>
</tbody>
</table>
Profit and Loss Statements

- Gross margin should be consistent each month.
- Gross profit can vary from month to month.
- Each member of your team could have a different gross margin.
Overhead

• Expenses you incur to stay in business. Each department gets a piece of overhead:
  • Rent
  • Utilities
  • Receptionist
  • Unapplied labor
  • Marketing/advertising
  • And much more
Net Profit

- Net Operating Profit:
  - Gross profit minus overhead

- Other income/expense

- Net Profit
Revenue (sales)
- _Cost of goods sold_
= Gross Profit
- _Overhead_
= Dept. Net Operating Profit

As a department manager you are responsible to this point on a P&L
Balance Sheets

• “I never look at the balance sheet. In fact, I never print the report out of QuickBooks. What good is it?”
Balance sheets

• True profitability
• Can you pay your bills?
• Are your building up too much inventory?
• Are you headed for a collection problem?
• Are you building up too much debt?
• Assets = liabilities + net worth
Assets

- Current assets
  - Cash or things turned into cash within one year

- Long term (fixed) assets
  - The stuff
Liabilities

- Current liabilities
  - Things that have to be paid within a year

- Long term liabilities
  - Notes, loans
Net Worth (equity or capital)

- The fudge factor!
Balance sheets

- Assets = liabilities + net worth
Balance sheets

• Current ratio = current assets / current liabilities

• Increasing current ratio usually means increasing profitability
P&L Critical Ratio

• Compensation % (productivity ratio)

\[
\text{total payroll + payroll taxes} \\
\text{sales (revenue)}
\]

• As low as possible
Remember

- P&L is for a specific period of time
- Balance sheet started the day you started your business and will end the day you close the doors
Your Financial Statements Are Wrong If...

• Financial statements are reported on a cash basis rather than an accrual basis
Your Financial Statements Are Wrong If...

- Financial statements are reported on a cash basis rather than an accrual basis

- The balance sheet doesn’t balance
Your Financial Statements Are Wrong If...

- Financial statements are reported on a cash basis rather than an accrual basis
- The balance sheet doesn’t balance
- There is negative cash on your balance sheet
Your Financial Statements Are Wrong If...

- Negative payroll taxes on your balance sheet
Your Financial Statements Are Wrong If...

• Negative payroll taxes on your balance sheet

• Negative loan payments on your balance sheet
Your Financial Statements Are Wrong If...

• Negative payroll taxes on your balance sheet

• Negative loan payments on your balance sheet

• There is no inventory or inventory is the same number each month
Your Financial Statements Are Wrong If...

• There is no rent or unusually high rent on your P&L
Your Financial Statements Are Wrong If...

- There is no rent or unusually high rent on your P&L

- Negative or unusually high/low gross margin
Your Financial Statements Are Wrong If...

- There is no rent or unusually high rent on your P&L
- Negative or unusually high/low gross margin
- There is no inventory or inventory is the same number each month
Your Financial Statements Are Wrong If...

- AR and AP aging reports don’t match the values on the balance sheet
Your Financial Statements Are Wrong If...

- AR and AP aging reports don’t match the values on the balance sheet
- Net profit doesn’t match current retained earnings
Contact Ruth

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  • 678–296–4123 (cell/text)
Get results

Thank you for your precious time!

Implement!