



FRED

Fast Resources for Enterprise Development



Wyoming Small Business
Development Center

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RECORD-KEEPING IN SMALL BUSINESS (Part 2 of 2)

Description: *Advice on record-keeping for small business, with information resources*

How To Analyze Your Records

To chart the progress of your business, you should become familiar with various forms of financial statements analysis and measurement.

Financial statements indicate which items need more attention. For example, profits may be too low or rent unnecessarily high. Perhaps there is a way to use the business vehicles more efficiently, to increase inventory turnover or to reduce long distance telephone bills.

In analyzing financial statements, carefully examine all items that do not seem realistic. Answer the following questions:

- Why are certain expenses at a particular level?
- Are there any ways to reduce or avoid certain expenses?
- Should you incur all of your expenses?
- Does the level of profit justify your investment, time and effort?

Financially significant items should be analyzed regularly. For example, examine payroll as a percentage of total administrative expenses. Keep in mind that, if your business is a proprietorship, your salary is not a payroll expense; however, if your business is a corporation, your salary should be a payroll expense.

Analyzing Payroll Expenses

In justifying payroll and other expenses, answer the following questions:

1. Are accurate records maintained for time spent on various jobs and functions?
2. Is the eight-hour day of each employee accounted for appropriately?
3. When employees are paid overtime, is the additional expense reflected in charges to the customer?
4. Is the level of payroll expense appropriate for your type of business?



5. Are you billing on a guaranteed price basis or on an hourly basis?
6. When using guaranteed price basis for billing, does actual time spent exceed time estimated for the job?
7. Do employees work with a minimum of wasted effort and time?
8. Are you operating at maximum efficiency? What strategies can be implemented to maximize efficiency?

Ratios

Accountants use various ratios to evaluate financial statements, such as ratios that assess liquidity, solvency and profitability.

$$\frac{\text{Current ratio}}{\text{Total Current Assets}} \\ \text{Total Current Liabilities} \\ = \\ \text{times you can pay current} \\ \text{liabilities}$$

The current ration tests a company's short-term debt paying ability.

Liquidity ratios indicate the availability of cash and the firm's ability to pay liabilities.

- **Current ratio:** Current assets/Current liabilities
- **Acid test (liquidity ratio):** Cash, cash equivalents and receivables/Current liabilities
- **Day's sales in receivables:** Accounts receivable/Credit sales divided by 360
- **Inventory turnover:** Cost of sales/Average inventory

Capital and Long-term Solvency ratios indicate the firm's ability to meet debts when due.

- **Equity/debt ratio:** Total equity/Total debt
- **Total equity to fixed assets:** Total equity/Net fixed assets

Profitability ratios indicate your firm's performance.

- **Gross profit margin:** Gross Profit/Sales
- **Net income to sales:** Net income/Sales
- **Operating income to sales:** Income before income taxes/Total assets
- **Return on total assets:** Net income and interest expenses/Total assets
- **Return on total equity:** Net income/Total equity

Other Important Factors

In addition to accounting records, you will need to keep separate records for accounts receivable, payroll and taxes, petty cash, insurance, business equipment and perhaps other items.

Accounts Receivable

A good record-keeping system should provide you with a detailed report of accounts receivable, including current information on customers and a running balance of their accounts. To maintain a good accounts receivable system, record credit charges on a regular basis. It is essential that you follow up on all late paying and delinquent customers.

Accounts receivable should be aged at the end of each month. This means

organizing the accounts into those that are current; 30-, 60-, and 90-days old and older. This arrangement helps you to take appropriate, timely actions.

One example of a timely action is to transfer delinquent accounts to a notes receivable account. Notes receivable are loans the business makes to others, either inside or outside the business. Each note receivable should contain specific terms of credit and interest and should be signed by the customer.

An additional timely action to decrease the number of bad accounts and avoid the effort of collecting payments from slow-paying customers is to issue a formal complaint with your local credit bureau.

Payroll and Taxes

Current Internal Revenue Service (IRS) regulations require that you withhold federal income tax and social security (FICA) from each employee. You must remit the amount for taxes to the IRS on a quarterly, monthly or more frequent basis. A detailed reporting system for payroll will help you make timely tax payments.

Gather specific information about each employee on individual employee record cards. All employees should fill out the federal Form W-4, which indicates their filing status and the number of exemptions they claim. Use this information to compute the federal withholding and social security (FICA) deductions for each payroll check. Prepare Employees Quarterly Federal Tax Return (Form 941) by totaling each employee's withholding for federal taxes and social security. File Form 941 with the IRS.

Each payroll period, total the accumulated withholdings of both federal taxes and social security for all employees. If this total exceeds \$500 for any month, you must deposit this amount by the 15th day of the following month in a depository bank (an authorized financial institution or a federal reserve bank). Generally, when the total exceeds \$3,000, you must deposit this amount within three business days. Any overpayment in taxes is paid back to you quarterly.

At the year's end, you are required to prepare not only the information normally required for that quarter, but also summaries of each employee's total earnings and withholdings for the year (Form W-2). Provide this form to each employee and the IRS.

A Word of Caution

It is very easy to fall behind in making tax payments. If you find yourself short of cash, do not be tempted to delay payment of taxes. The IRS will not bill your business for taxes due nor will it notify you of late payments. Delayed payments can easily add up to a large sum; the debt may impede the growth of your business and may even force you to close your business, to say nothing of the federal penalties incurred for late payments.

The IRS has made significant improvements to navigate their website for businesses to access information.

<http://www.irs.gov/businesses/index.html>

With a good record-keeping system, you can simplify the process of filing taxes to the point where the information needed to complete the forms is automatically generated. Setting up such a system is a rather technical task and you may need to seek guidance.

Petty Cash

Sometimes a petty cash fund is needed to purchase small items required on a day-to-day basis. If this is necessary, draw a check to petty cash for a nominal amount.

Problems often arise when cash is easily available; therefore, if possible, avoid a petty cash fund. However, very often the convenience of having a small amount of cash available will facilitate the smooth operation of your business. Be sure to balance this fund monthly, based on the cash balance plus receipts for all expenditures.

Insurance

Most businesses have several types of insurance. For each policy, you should have the following information:

- Clear statement of the type of coverage.
- Names of individuals covered.
- Effective dates and expiration date.
- Annual premium.

Review your insurance policies on a regular basis. In addition, annually consult an insurance specialist, who will review the total insurance package to determine what coverage is appropriate and ensure that premiums remain in line with prior quotations.

Business Equipment

Keep an accurate list of permanent business equipment used on both a regular and stand-by basis. The list should describe the equipment and provide serial numbers, date of purchase and original cost. Keep the list available for insurance or other purposes. You will also need this information to prepare accurate depreciation schedules.

Accounting Services

You have several choices in who should maintain your accounting system. You can:

- Maintain the books yourself.
- Hire a bookkeeper on a full-time or part-time basis.
- Hire an accountant to set up your books.
- Set up a hybrid system in which you maintain the day-to-day

Very few small businesses can get by without some professional accounting assistance.

reports, while an accountant does the period-end record preparation, summaries and reconciliations and the returns for sales tax, excise tax and payroll taxes.

In making the choice, you must decide whether you have the ability and time to set up and maintain good records or if you should engage an outside accounting service. It is usually suggested that you hire an accountant to do the final year-end preparations and to advise you. No matter what you choose, you should remain familiar with your books and participate in the record-keeping process. This will maximize the services provided by the accountant and allow you to keep track of your business.

Selecting the Accounting Service

If you decide to hire an outside service, find an accounting firm that will work closely with your business and provide you with the information necessary to develop a successful operation. Interview several accounting professionals and compare their level of accounting knowledge, computer literacy, knowledge of and experience with small business accounting and any specialized knowledge required in your business.

Deciding to hire an accountant or not, you should remain familiar with your books and participate in the record-keeping process.

There are many types of professionals you may consider, such as a certified public accountant, an enrolled agent or an accredited accountant.

- **Certified Public Accountant (CPA)**—A person who has passed the American Institute of CPAs' national examination, which tests an individual's ability in accounting, auditing, law and related areas.
- **Enrolled Agent (EA)**—An individual who has passed a two-day exam prepared by the IRS, covering many areas of federal taxation. This person is generally considered a tax specialist.
- **Accredited Accountant**—An individual who has passed a rigorous examination prepared by the Accreditation Council of Accountancy and Taxation, a national accounting accreditation board affiliated with the National Society of Public Accountants and the College for Financial Planning in Denver, Colorado. Accredited accountants specialize in small business accounting.

When selecting an accountant, the cost of the accountant's fees must be weighed against the benefits received. Frequently, the accountant's professional advice can increase profits to more than cover the expense. Monthly services by an accounting firm will provide you with complete and timely information about your business's financial picture, and cumulative knowledge of your business operations will qualify the accountant to render professional advice to you as the business grows.

Advice and Assistance

In addition to bookkeeping, an accountant can advise you on financial

management. He or she can assist with cash flow requirements and budget forecasts, business borrowing, choosing a legal structure for your business and preparation and advice on tax matters.

Cash Flow Requirements

An accountant can help you work out the amount of cash needed to operate the business during a certain period—for example, a three-month, six-month or one-year projection. The accountant considers how much cash you will need to carry your accounts receivable, to increase inventory, to cover current invoices, to acquire needed equipment and to retire outstanding debts. Additionally, the accountant can determine how much cash will come from collection of accounts receivable and how much will have to be borrowed or provided from other sources.

In determining cash requirements, the accountant may notice and call attention to danger spots, such as accounts that are in arrears or delinquent areas or areas of excess expenditure.

Business Borrowing

An accountant can assist you in compiling the information necessary to secure a loan: the assets the business will offer for collateral, the present debt obligations, a summary of how the money will be used, and repayment schedules. Such data show the lender the financial condition of the business and your ability to repay the loan. Remember, lenders have two very definite requirements:

1. That the business have adequate collateral to secure the loan.
2. That the business will be able to repay the loan.

An accountant can advise on whether you need a short- or long-term loan. In addition, your accountant may introduce you to a banker who knows and respects his or her financial judgment.

Legal Structure

It is wise to discuss the type of business organization that best fits your needs with an accountant and an attorney. They can point out the advantages and disadvantages of the various forms of business organization, such as a:

- Proprietorship—An extension of individual ownership.
- Partnership—Multiple proprietors.
- Corporation—A completely separate legal entity.
- Limited Liability Company—A hybrid between a corporation and a proprietorship.

In addition, they can advise you on immediate plans regarding management, financing, long-range plans to bring others into the business and estate planning, all of which affect the type of business you choose.

Tax Considerations

This is an area in which an accountant can provide much advice and assistance. Your accountant can suggest methods to record and document the various types of information necessary for taxes.

Appendix A: Financial Status Checklist of Things You Should Know:

Daily

- The balance of cash on hand.
- The bank balance.
- Daily summaries of sales and cash receipts.
- Any errors or problems that have occurred in collections.
- A record of monies paid out, both by cash and by check.

How a business is taxed depends upon its form of ownership.

Weekly

- Accounts receivable (particularly those accounts that appear to be slow paying).
- Accounts payable (be aware of the discount period mentioned above).
- Payroll (be aware of the accumulation of hours and the development of the payroll liability).
- Taxes (be aware of any tax items that are due and reports that might be required by government agencies).

Monthly

- If you engage an outside accounting service, provide records of receipts, disbursements, bank accounts and journals to the accounting firm. This will allow the firm to maintain good records and present them to you for review, consideration and support in decision making.
- Make sure that income statements are available on a monthly basis, and certainly within 15 days of the close of the month.
- Review a balance sheet that indicates the balance of business assets and the total current liability.
- Reconcile your bank account each month so that any variations are recognized and necessary adjustments made.
- Balance the petty cash account on a monthly basis. If you allow this account to extend for a longer period, it may create substantial problems.

- Review federal tax requirements and make deposits.
- Review and age accounts receivable so that slow and bad accounts are recognized and handled.

Appendix B: Information Resources

The U.S. Small Business Administration (SBA) has many services available to the entrepreneur. An extensive selection of information on most business management topics, from how to start a business to exporting your products is available from the online library, at <http://www.sba.gov/library/pubs.html>. In addition, SBA offers a number of programs and services including training and educational programs, counseling services, financial programs, and contract assistance, and sponsors the following organizations that provide assistance to small business owners:



Development Centers (ASBDC) is a partnership program uniting private enterprise, government, higher education and local nonprofit economic development organizations. We are dedicated to the sound development of small business throughout America.

Service Corps of Retired Executives (SCORE), a national organization of over 13,000 volunteer business executives who provide free counseling, workshops and seminars to prospective and existing small business people.

Small Business Development Centers (SBDCs), sponsored by the SBA in partnership with state and local governments, the educational community and the private sector. They provide assistance, counseling and training to prospective and existing business people. In Wyoming, call (800) 348-5194 to find the office nearest you.

Small Business Institutes (SBIs), organized through SBA on more than 500 college campuses nationwide. The institutes provide counseling by students and faculty to small business clients. For more information about SBA business development programs and services, call the SBA Small Business Answer Desk at 1-800-U-ASK-SBA (827-5722).

Other U.S. Government Resources

Many publications on business management and other related topics are available from the Government Printing Office (GPO). GPO bookstores are located in 24 major cities and are listed in the Yellow Pages under the "bookstore" heading. You can request a Subject Bibliography by writing to Government Printing Office, Superintendent of Documents, Washington, DC 20402-9328.

Many federal agencies offer publications of interest to small businesses. There is a nominal fee for some, but most are free. Below is a selected list of government agencies that provide publications and other services targeted to small businesses. To get their publications, contact the regional offices listed in the telephone directory or write to the addresses below:

Consumer Information Center (CIC): The CIC offers a consumer information catalog of federal publications.

Contact Information:

CIC
P.O. Box 100
Pueblo, CO 81002

Consumer Product Safety Commission (CPSC): The CPSC offers guidelines for product safety requirements.

Contact Information:

CPSC
Publications Request
Washington, DC 20207

*U.S. Consumer Product
Service Commission*

<http://www.cpsc.gov/>

U.S. Department of Agriculture (USDA): The USDA offers publications on selling to the USDA. Publications and programs on entrepreneurship are also available through county extension offices nationwide.

Contact Information

USDA
12th Street and Independence Avenue, SW
Washington, DC 20250

U.S. Department of Commerce (DOC): DOC's Business Assistance Center provides listings of business opportunities available in the federal government. This service also will refer businesses to different programs and services in the DOC and other federal agencies.

Contact Information:

DOC
Office of Business Liaison
14th Street and Constitution Avenue, NW
Room 5898C
Washington, DC 20230

U.S. Department of Health and Human Services (HHS): Provides information on Employee Assistance Programs.

Contact Information:

Public Health Service Alcohol, Drug Abuse and Mental Health
Administration
5600 Fishers Lane
Rockville, MD 20857
Drug Free Workplace Helpline: 1-800-8434971.

National Institute for Drug Abuse Hotline: Provides information on preventing substance abuse in the workplace.

Contact Information:

1-800-662-4357.

The National Clearinghouse for Alcohol and Drug Information:

Provides pamphlets and resource materials on substance abuse.

Contact Information:

1-800-729-6686.

U.S. Department of Labor (DOL): The DOL offers publications on compliance with labor laws.

Contact Information:

Employment Standards Administration
200 Constitution Avenue, NW
Washington, DC 20210

U.S. Department of Treasury: The IRS offers information on tax requirements for small businesses.

Contact Information:

Internal Revenue Service (IRS)
P.O. Box 25866
Richmond, VA 23260
1-800-424-3676



<http://www.irs.gov/businesses/index.html>

U.S. Environmental Protection Agency (EPA): The EPA offers more than 100 publications designed to help small businesses understand how they can comply with EPA regulations.

Contact Information:

EPA
Small Business Ombudsman
401 M Street, SW (A-149C)
Washington, DC 20460
1-800-368-5888 except DC and VA 703-557-1938 in DC and VA

U.S. Food and Drug Administration (FDA): The FDA offers information on packaging and labeling requirements for food and food-related products.

Contact Information:

FDA Center for Food Safety and Applied Nutrition
200 Charles Street, SW
Washington, DC 20402

For More Information

A librarian can help you locate the specific information you need in reference books. Most libraries have a variety of directories, indexes and encyclopedias that cover many business topics. They also have other resources, such as:

Trade association information: Ask the librarian to show you a directory of trade associations. Associations provide a valuable network of resources to their members through publications and services such as newsletters,

conferences and seminars.

Books: Many guidebooks, textbooks and manuals on small business are published annually. To find the names of books not in your local library check Books In Print, a directory of books currently available from publishers.

Magazine and newspaper articles: Business and professional magazines provide information that is more current than that found in books and textbooks. There are a number of indexes to help you find specific articles in periodicals.

In addition to books and magazines, many libraries offer free workshops, lend skill-building tapes and have catalogues and brochures describing continuing education opportunities.

Author: U.S. Small Business Administration

Source: U.S. Small Business Administration

All Wyoming SBDC regional offices maintain a business library. Contact the office closest to you for a list of books available for checkout. Fred document #101 lists all contact information for all offices.

This information is provided by:

Wyoming Small Business Development Center

P.O. Box 3922

Laramie, WY 82071

Phone Toll-Free: 1-800-348-5194

FRED toll-free number: 1-877-700-2220

SBDC website: www.uwyo.edu/sbdc