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UNDERSTANDING YOUR FINANCIALS: BALANCE SHEET

The Balance Sheet

Whether you are an existing firm reaching between $1-2 million in revenue or just starting out, you might be at a tipping point in terms of needing to get serious about your financials. You most likely are a dynamic, relationship-driven entrepreneur who has had great success building your business but maybe not specifically in the area of finance. You can't be a subject matter expert in everything, this quick guide will give you the tips you need to know about a balance sheet.

To get you started, the basics of a balance sheet include three main sections:

1. Assets
2. Liabilities
3. Equity/Net worth

You should remember that a balance sheet is just as important as an income statement and at the end of the day, a balance sheet should always balance.

Example Company
Balance Sheet

Assets		**Liabilities**	
Current assets		Current liabilities	
Cash	2,100	Notes payable	5,000
Petty Cash	100	Accounts payable	35,900
Temporary Investments	10,000	Wages payable	8,500
Accounts receivable	40,500	Interest payable	2,900
Inventory	31,000	Team payable	6,1000
Supplies	3,800	Warranty liability	1,100
Prepaid Insurance	1,500	Unearned revenues	1,500
Total Current Assets	**$80,600**	Total Current liabilities	$61,000
Investments	**$36,000**	Long-term liabilities	
Property equipment		Notes payable	20,000
Land	5.500	Bonds payable	400,000
Land improvements	6,500	Total long-term liabilities	420,000
Buildings	180,000	Total liabilities	$48,100
Equipment	201,000		
Less: accum depreciation	(56,000)	**Stockholders' Equity**	
Intangible assets		Common stock	110,000
		Retained earnings	220,000
Goodwill	105,000	Accum other comprehensive income	9,000
Trade names	200,000		
Total intangible assets	305,000	Less: treasure stock	(50,000)
		Total stockholders equity	289,000
Total Assets	$770,000	Total liabilities & stockholders' equity	$770,000

Remember

- A balance sheet is just a point in time (snapshot)
- It provides a view into the strength and stability of a company
- You will find historical trends (up and down)

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ASSETS

Assets are the items that you **own**. They are something of value to you and underlines the strength of your business. Assets can also be classified as short and long term.

What assets should be included?

- Current assets
    - Cash, accounts receivable, notes receivable, and inventory
- Fixed assets
    - Buildings and equipment
- Intangibles
    - Goodwill
- Long term / other assets
    - Deposits and investments

LIABILITIES

Liabilities are something that you owe both in the short term and long term. You always want to make sure that you have more assets than liabilities.

What liabilities should be on the balance sheet?

- Current liabilities
    - Accounts payable, accrued expenses, taxes, and CPLTD (Current Portion Long Term Debt)
- Long term liabilities
    - Notes payables and loans payable

Now you might be asking yourself.... How do I calculate my equity or net worth? You need to make sure what you OWN is more than what you OWE. That more than anything will determine the strength of your company.

Net worth

- Net Income
- Assets – Liabilities = Net worth
- Roll forward retained earnings:
  Ending Balance + Contributions – Distributions + Net income

Tangible net worth

- Assets - Intangibles – Goodwill – Liabilities = Tangible net worth

Other terms you need to know

- Paid in capital
- Distributions
- Contributions
- Net income
- Treasury stock

Key ratios and covenants to consider

- Current ratio
    - Current assets / Current liabilities
    - Generally > 1.0x-1.25x
- Quick Ratio
    - (Cash + Cash equivalent + Account receivables) / Current liabilities
    - Generally > 1.0x
- Tangible net worth covenant
    - Must be > $XXX
    - Percentage of accounts receivable
    - Percentage of revenue
- Leverage covenant
    - Total debt / Net worth
    - Generally < 3.0x-4.0x