FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

Managing Your Small Business Finances

Use financial management skills to help your business

Learning Objectives

- At the end of this module, you will be able to:
  - Identify basic accounting practices.
  - Position your business for future financing.
  - Recognize the need for debt collection.
  - Identify financing sources available.

About FDIC Small Business Resource Effort

- The Federal Deposit Insurance Corporation (FDIC) recognizes the important contributions made by small, veteran, and minority and women-owned businesses to our economy. For that reason, we strive to provide small businesses with opportunities to contract with the FDIC. In furtherance of this goal, the FDIC has initiated the FDIC Small Business Resource Effort to assist the small vendors that provide products, services, and solutions to the FDIC.
- The objective of the Small Business Resource Effort is to provide information and the tools small vendors need to become better positioned to compete for contracts and subcontracts at the FDIC. To achieve this objective, the Small Business Resource Effort references outside resources critical for qualified vendors, leverages technology to provide education according to perceived needs, and offers connectivity through resourcing, accessibility, counseling, coaching, and guidance where applicable.
- This product was developed by the FDIC Office of Minority and Women Inclusion (OMWI). OMWI has responsibility for oversight of the Small Business Resource Effort.

Executive Summary

- Small business owners need to know the concepts of financial management included in the simple, everyday bookkeeping tasks.
- Understanding more sophisticated concepts like credit and collections policies, managing your cash flow, major purchases and projects, and financial position analysis will further help you manage the financial side of your business.

Basic Bookkeeping *(Slide 1 of 3)*

- Maintain thorough records to help you:
  - Track company performance.
  - Make better decisions.
  - Give accurate information when applying for funding.
  - Keep within your budget.
  - Comply with tax regulations – federal, state, and local taxes.
  - Track and dispense payroll.
- Invest in business accounting software – look for free trials before you buy to make informed decisions, e.g., QuickBooks Simple Start.
- Record data and run reports regularly.
- Keep personal and business finances separate, e.g., bank accounts, credit cards.
- Attend bookkeeping/accounting workshops – there is always more to learn.

Basic Bookkeeping *(Slide 2 of 3)*

- Hire an accountant to help:
  - Set-up your business – sole proprietorship, corporation, or partnership.
  - Set-up the initial accounting system – assets, liabilities, equity, sales/revenue transactions, balance sheet, debits and credits, double/single entry accounting, accounts receivable, and accounts payable.
  - Create a budget – how much do you need to operate your business? How much should you get paid? How much should be invested back into the business? How much for expenditures?
  - Close books monthly, quarterly, or annually.
  - File income tax quarterly or annually.
  - Prepare financial statements.

Basic Bookkeeping *(Slide 3 of 3)*

- Set-up an accounting system to help:
  - Record day-to-day transactions, journal entries, general ledger, and trial balance.
  - Track cash or accrual method.
    - Cash – record income when payment is received.
    - Accrual – record income prior to receiving payment .
  - Track single-entry or double-entry accounting.
  - Prepare quarterly, annual taxes.
  - Close the books.
  - Prepare financial statements.

Other Financial Concepts to Help Your Business

- Aside from bookkeeping skills, you want to take some more sophisticated actions, such as:
  - Setting credit and collections policies.
  - Managing your cash flow.
  - Timing major purchases and projects.
  - Analyzing your financial position.

Setting Credit and Collections Policy *(Slide 1 of 4)*

- Cash is the most commonly accepted and reliable form of payment. Many small business operate as "cash-only" merchants. This decision will depend on your specific business industry, location, types of transactions, and financial condition.
- Pros of cash-only business:
  - Cash payments ensure that businesses receive funds immediately.
  - Cash is the simplest form of payment and involves less bookkeeping.
  - Limited risk of fraud when accepting cash only.
  - Cash only businesses don't have to worry about third parties or fees associated with other payment options, e.g., credit card or bank fees.
- Cons of cash-only business:
  - Customers who don't carry cash will have to walk away from a purchase they would otherwise make.
  - Credit card payments are an expected option and customers may be irritated by the lack of this option and choose not return to the business.
  - Keeping large sums of cash on business premises increases risk and increases the amount of time managing cash finances, e.g., making trips to the bank.
  - IRS Form 8300 is required if a business receives more than $10,000 cash from one buyer as a result of a single transaction or two or more related transactions. The same rule applies to cash equivalents such as traveler's checks, cashier's checks, money orders, and bank drafts.

Setting Credit and Collections Policy *(Slide 2 of 4)*

- Credit and debit cards are popular, convenient, flexible, and have become increasingly important in business commerce. Decide which credit cards you want to accept: Visa, MasterCard, Discover, and/or American Express.
  - Pros of accepting credit and debit cards:
    - Cards are evolving to be the most common form of customer payment.
    - Businesses can easily accept credit card payments.
    - Convenience of using credit cards increases likelihood of impulse purchases.
  - Cons of accepting credit and debit cards:
    - Increased risk of fraud – understand and take measures to protect your customer's privacy and secure personal information.
    - You will be charged a processing fee based on volume and amount of transactions.
    - Additional time required to manage credit card record and bookkeeping.

Setting Credit and Collections Policy *(Slide 3 of 4)*

- Checks are another payment option. Be aware of some risk with checks due to the potential of insufficient funds. Decide what forms of identification (ID) you will require. Be cautious of fraud – does the address on the check match the ID? Consider common check policies including:
  - Checks must be from a local or in-state bank.
  - Checks should not be written and accepted for more than the purchase amount.
  - Checks should not be accepted that are starter checks, unnumbered checks, or non-personalized.
  - Accepted checks should be deposited as quickly as possible – banks may refuse to honor checks dated back six months or more.
- Other credit policies to consider:
  - Send an invoice with payment terms of COD (cash on delivery), Net 30 days, or Net 10 days (payment due within 30 or 10 days of receiving invoice).
  - Require signing a sales contract.

Setting Credit and Collections Policy *(Slide 4 of 4)*

- Collecting overdue accounts:
  - Develop or invest in a software program for tracking and reporting aging accounts receivable. The same customer could have multiple entries with different payment terms.
  - Decide when collection efforts should begin: one day/one week/one month after missed payment.
  - Decide who will collect on past due accounts – you, a collection agency, or a lawyer. Collecting yourself is the least expensive method, but may be too time consuming. Debt collectors and lawyers get paid 15% to 50% (33% is standard) of the collected amount. Arrange fee amount prior to handing over accounts.
  - Hire debt collectors or lawyers only after you have already tried to collect.
  - Determine size of debt to turn over to debt collector/lawyer. Small accounts are typically not advantageous to a lawyer, but will be collected by a collection agency.

Managing Your Cash Flow

- Understand cash flow – inflows (sales of goods or services) and outflows (accounts payable).
- Understand cash flow gap – time lag between inflows and outflows.
- Analyze cash flow gap by knowing:
  - Amount of cash you have and what is needed to cover the gap.
  - Amount of cash necessary to operate your business and when the cash is needed.
  - Amounts of accounts payable and accounts receivable.
  - How income and expenses affect the amount of cash needed to expand your business.
  - How much inventory you should have on hand.
  - How credit terms and policies can affect your cash flow.
- Look for ways to barter your product or service for other products or services.

Timing Major Purchases and Projects

- Decide when to purchase new equipment or update existing equipment. A major purchase is defined in the accounting world as items or projects that will have a service period of more than a year.
  - Determine what amount of capital purchases would require a financial analysis based on your company size, e.g., any purchases over $10,000.
  - Do a formal financial analysis: what costs, benefits, and risks are involved?
  - Decide if your purchase/project requires financing or can you lease.
  - Find out the tax incentives.
  - Consider implementing the project in phases if possible.
  - Identify hidden costs - installation, training sessions, maintenance and repairs, insurance, utilities, supplies, taxes, payroll, and benefits costs for new employees needed to operate the equipment, or any other incidental costs.

Analyzing Your Financial Position *(Slide 1 of 3)*

- Analyze your financial position by answering these questions:
  - What financing options are available to you based on your financial and business life cycle (start-up, acquired, growing, aging) position?
  - Do you appeal to financial institutions? Can you prove your business is or will be successful or profitable and how?
  - What is your business experience, expertise, and managerial experience?
  - How much money do you need? This will dictate what options are available to you, e.g., debt/equity financing, financial institutions, or government loans.
  - Do you have a business plan?
  - How much personal capital do you have? What are you using for collateral?
  - Is a home equity loan or line of credit right for you?
  - What is your gap analysis?
  - Do you have any contributions from friends or family? Are they gifts or loans? Do you have formal contracts in place?

Analyzing Your Financial Position *(Slide 2 of 3)*

- Decide if you can self-sustain your cash flow (bootstrapping) by looking at these areas:
  - Collecting accounts receivable. Don’t leave money on the table without trying to collect.
  - Managing inventory. Having too much inventory is costly. Find the right balance for your business.
  - Examining accounts payable cycle. If you are offered Net 30 or 45, take all 30 or 45 days. Just don’t be late or it will affect your credit score.
  - Controlling expenses. Purchase used furniture or equipment when it makes sense. Be cautious of costly maintenance agreements on leased equipment.

Analyzing Your Financial Position *(Slide 3 of 3)*

Financial Sources

- Angel Investors
- Asset-based financing
- Bank lending (lines of credit, short-term commercial loans)
- Bank lending (secured and unsecured)
- Business alliances
- Commercial finance companies
- Consumer finance companies
- Credit cards
- Credit unions
- Crowd sourcing
- Debt financing
- Equity financing
- ESOPs
- Factoring
- Franchising
- Initial public offerings
- Insider financing
- Insurance companies
- Leasing
- Limited private offerings
- Personal financing
- Small Business Administration
  - SBA Microloans
  - SBA express loans
  - SBA regular 7(a) program
  - SBA CAPlines
  - SBA Export Working Capital Loan Guarantee Program
  - SBA International Loan Program
  - SBA Section 504 (Community Development Companies)
- State and local public financing
- Trade credit
- Venture capital (and SBIC)

Key Takeaways from This Module

- Putting solid practices into place early will help save you time and money.
- Managing your financial records regularly is an important factor in financial success.
- Your cash flow is much more than just debits and credits.

Sources and Citations

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