# Bookstore Finances Textbook

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# Bookstore Finances

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To learn more about the Professional Booksellers School, visit **https://www.professionalbooksellers.com**. Students in the Professional Booksellers School must be an individual member or work for a bookstore that is a member of either their regional booksellers' association and/or the American Booksellers Association.

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**Professional Booksellers School Mission Statement**

The purpose of the Professional Bookseller Certification Program is to provide independent booksellers with an education, training, and accreditation process that will:

1. Elevate the trade of independent bookselling to a standard approaching that of other professionals in similar industries related to education and public literary engagement.
2. Offer a standardized baseline knowledge across all aspects of the independent bookselling industry, as well as professional development opportunities for career booksellers.
3. Create an opportunity for mentorship, guidance, innovation, teaching, and information sharing among book industry members that will compensate people for their time and expertise.

**The Professional Booksellers School is made possible by the generous investment of:**

- New Atlantic Independent Booksellers Association
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- Midwest Independent Booksellers Association
- New England Independent Booksellers Association
- California Independent Booksellers Alliance
- Great Lakes Independent Booksellers Association
- Southern Independent Booksellers Alliance
- Pacific Northwest Booksellers Association
- American Booksellers Association
- Bookshop.org
- Libro.fm
- Batch for Books
- Penguin Random House
- HarperCollins Publishers
- Sourcebooks
- Ingram Content Group
- Booklog
- Basil Bookseller Software
- Anthology
- MVB US

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# About This Course

## DISCLAIMER

This course is intended for educational purposes only. Financial information is NOT the same as professional financial advice. We are not your accountants or financial advisors; we are here to present information to you. This course is not intended to create a financial advisor relationship between students and instructors. All of your situations are unique, so please consult with an accountant and/or financial advisor to obtain advice about how to handle your specific questions/situation.

### CHAPTER OUTLINE

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## COURSE OVERVIEW

Bookstore Finances is designed to educate on the day-to-day and long term finance-related needs of an independent bookstore, considering both high-level financial topics such as taxes and accounting and deep dives into financial reporting and strategy. A mix of webinars, handouts, and assignments will be used to guide the student toward creating financial systems and strategies for real-time applications. This course is geared toward store owners and/or managers who handle finances on a day-to-day basis and is for educational purposes only, meaning no certification is earned for this course.

This course will provide a thorough overview of financial systems, reports, and strategies for an independent bookstore. At the conclusion of this course, students will be able to:

- Demonstrate confidence in finance and a general understanding of bookstore finance basics.
- Employ necessary language to confidently speak to accountants, bookkeepers, financial advisors, and other finance professionals.
- Customize their Chart of Accounts to make it work better for them.
- Efficiently and successfully complete the ABACUS survey.
- Implement practical tips and strategies immediately to improve their understanding of their store's finances.
- Establish a financial rhythm that makes sense for them.

More information can be found on the syllabus, located here.

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# Coursework

## HOMEWORK

Homework will be assigned each week and will help you work toward completing your course project as well as prepare you for the upcoming class.

Homework will have five parts:

- Document a current financial system.
- Fill in the reporting grid.
- Fill in the action grid.
- Answer the review questions at the end of the textbook chapter and check your answers.
- Read the textbook chapter for the next class.

We may also include other pieces to the homework based on what you're learning in class.

The two grids and everything you need to document your systems can be found in your workbook, and you will type everything directly into it. After each class, you will be expected to document what you are currently doing for the financial system learned in that class.

90 days after the course ends, the Discord server will be wiped, so your information will not be held. Generally, we will not ask you to share your store's specific financial numbers with us. PBS takes confidentiality very seriously!

If you're an active student, you'll complete your homework assignment(s) for the previous class in the workbook, then post a message in your personal Discord homework channel that the homework is complete and tag your instructors for that class. If there are any supporting documents that go with the homework, you should upload those documents to your homework Discord channel as well.

Assignments should be completed and noted in Discord by the next scheduled class to be guaranteed feedback. If you turn in an assignment late, feedback is not guaranteed, although make sure to tag your instructor, who will give feedback if they have time. Instructors will comment on the assignment inside of your personal Discord homework channel to give feedback.

There will be no grades, as this is not a certification course, however, we will be giving "credit" for assignments as a way for active students to track their own progress in the course. After each class, your instructors will credit your homework based on the following scale:

0 - Not Turned In
1 - Turned In, But Incomplete
2 - Turned In, Complete

Since there are 13 classes in this course, the total amount of possible credits you could receive is 26. Active students will be given an overall evaluation at the end of the course, along with recommendations from your instructors on what you should focus on going forward.

If you're an auditing student, you will not receive credits or a course evaluation. Feel free to complete the assignments and do the course project on your own! Instructors have limited capacity and auditing students are not guaranteed feedback, but if instructors have extra time, they may offer guidance, so feel free to post in your homework channel and tag instructors if you want to try to seek feedback (although again, it's not guaranteed).

No work will be accepted after August 16 without prior permission.

If you need an extension on a homework assignment, please reach out to your instructor for that class.

## COURSE PROJECT

Throughout the course, you will build a personalized financial dashboard inside your workbook. At the end of the course, you will have a ready-to-use document that will do three things:

First, it will house documentation of all of your current financial systems that you will be able to review, edit, and use any time. This is meant to be a living document that you use in training others and share among owners, managers, bookkeepers, and accountants to ensure you're all on the same page.

Next, you will have a reporting grid, which is a list of financial reports, how often you want to run and analyze them, and specifically what you want to look for in those reports. After each class, you should fill in this grid with any reports you learned about that you want to track.

Finally, you will have an action grid, which will serve as metrics tracking and a decision making document. After each class, you should fill in the action grid with specific metrics you learn about that you want to track, the threshold or goal for that metric that makes sense for you, and the actions you want to take when the metric is hitting the threshold (green), getting away from you (yellow), or completely off (red).

When you put the grids and documentation together, you will have a fully functional financial dashboard that will help you make decisions, take actions, and efficiently run your store operations to ensure your store's financial health.

The reporting and action grids can be found at the beginning of your workbook. The documentation section is also in the workbook and can be found under each class. The workbook has clear instructions on the homework under each class section, including a checklist of the things you should do each week so you don't forget anything.

# Expectations

## INSTRUCTOR EXPECTATIONS

- Bring a diversity of expertise and perspectives.
- Share the best information available to us.
- If we don't know an answer, we will research and get back to you.
- Create a warm and inclusive community to support your learning.
- Model respect.
- Be available during office hours for discussion about your specific questions and needs.
- Give clear and thorough feedback to your homework.
- And of course, celebrate with you when we reach the end of the course!

## STUDENT EXPECTATIONS

- Follow the Code of Conduct.
- Carve out and protect this class time the best you can, and actually show up and participate in class.
- Participate through attendance, discussion, and completing assignments.
- Attend instructor office hours to ask questions and gather feedback.
- Bring solution-oriented discussions to help each other improve and grow.
- Tap into the knowledge available in the small group settings.
- And finally, honor the diversities of experience and knowledge gathered here.

# Professional Booksellers School Code of Conduct

The Professional Booksellers School, Inc. (PBS) values the dignity of everyone with whom we interact. Our safety and anti-harassment policies are critical to ensuring that this core value guides how we speak and how we act. All participants in PBS courses and events are required to adhere to PBS's code of conduct, as described below. This includes booksellers, PBS staff, instructors, speakers/presenters, guests, donors, volunteers, and all affiliated students.

PBS is committed to a broad vision of diversity, equity, and inclusion. This includes providing a harassment-free experience for everyone, regardless of race, color, religion (creed), gender, gender expression, age, national origin (ancestry), ability, marital status, sexual orientation, or military status, in all of its activities or operations. We do not tolerate harassment, discrimination, or other disrespectful or unlawful behavior based on any of these characteristics. We are committed to providing an inclusive and welcoming environment for our students, staff, volunteers, instructors, donors, subcontractors, vendors, and clients.

Behaviors that violate this policy include, but are not limited to:

- Offensive verbal comments related to any protected category above
- Inappropriate physical contact
- Unwelcome propositions, attention, words, or conduct of a sexual nature
- Unwelcome virtual contact inside or outside of PBS settings
- Inappropriate or obscene jokes, remarks, or gestures
- Intimidation, stalking, or trolling
- Disrespect towards difference of opinion
- Sustained disruption of speakers, conversations, classes, or events
- Unauthorized screenshots, photography, or audio or video recording

PBS expects all participants in its programs to follow established rules throughout official classes, office hours, virtual platforms, and related social gatherings.

PBS takes any violation of this policy seriously. Accordingly, participants who violate this policy may, in the judgment and discretion of PBS, be asked to stop; may be expelled from a PBS class or event, without refund if applicable; may be prevented from attending future PBS classes or events; may be banned from virtual platforms; and may have future PBS participation privileges revoked.

If you are being harassed, observe someone else being harassed, or have concerns about potential violations of this policy, please notify PBS staff immediately. PBS will take all appropriate action in response to protect anyone affected by violations of this policy.

# Professional Booksellers School Privacy Statement

**For Stores**

PBS asks for both public (address, etc) and private (square footage, POS, sales levels) information from stores who are members. We ask for this private information to help us understand and support students. The only public-facing information, in our website directory, is the store's name, address, contact information, and regional trade association. PBS uses both private and public information to analyze the effectiveness of our courses and our school, but reports only aggregate data. All other store information is protected and available only to PBS staff.

**For Individuals**

PBS asks for both public (bookstore, job title) and private (home address, demographic, years of experience) information from individuals who are members. The only public-facing information is the student's name, bookstore, job title, and earned certifications. PBS uses both private and public information to analyze the effectiveness of our courses and our school, but reports only aggregate data. All other information is protected and available only to PBS.

**For Homework**

We recognize that homework can contain personal or sensitive information. Student homework assignments are uploaded into formats available only to the individual student, PBS staff, and instructors, with the exception of projects delivered live in class. These projects are announced well in advance and student presentations are never recorded. All student homework for PBS is owned by the student, not PBS or the student's employer, and is confidential and protected. **All shared, spoken, shown, submitted, and typed information is protected and confidential and not to be discussed, saved, or shared outside of applicable PBS classes, platforms, or events without express permission.**

# Tour of Class Tools

We have a variety of tools for communication and keeping you informed of all things. If you need help with any of the tools or would like a brief Discord tour, please let the Dean know.

## COURSE TEXTBOOK

We have provided this course textbook to help you process the information we go over in class. This is your main course resource.

## EMAILS

You will receive two emails each week. One will be before class to remind you about class and how to participate, as well as any special information regarding the next class; the other will be post-class and give you homework reminders and other details as needed.

## DISCORD

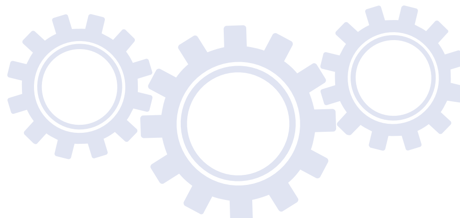
Discord is the tool we use for all course communication. We will share links to handouts and other documents in Discord in the appropriate class channel. Make sure you accept the Discord invite sent via email at the beginning of the course. You can access the server here.

## COURSE WORKBOOK

Each student has their own course workbook, which is a Google Drive document that is linked in your personal homework channel on Discord. You'll complete each homework assignment in the workbook. If you need to share an outside document, you can upload those to your personal homework channel in Discord, which only you and the instructors will see.

## ZOOM

Zoom is where we'll have our live classes. Please use the chat to participate in class and talk to each other. Instructors will keep an eye on the chat as well to ensure any questions get answered. If you want to ask a question during class, please use the "raise hand" function. Also feel free to use emojis to express how you're feeling!



# How To Use This Textbook

## WATCH FOR THESE FEATURES

### REVIEW QUESTIONS

At the end of each chapter, you will find review questions to answer to quiz yourself on some of the main concepts in that chapter. Answers to the questions are given as well.

### REAL-LIFE SCENARIOS

Within chapters, you will find example and real-life scenario boxes that will provide specific examples and scenarios for a concept.

### KEY TAKEAWAYS

- At the end of each chapter, you will see a box with bullet points of the key takeaways of that chapter. This is a bulleted list of the main points and concepts you just learned.

## KEY TERMS

At the end of each chapter, you will see a list of key terms introduced in that chapter. All Key Terms can be found in the glossary at the end of this textbook (Appendix B).

## DIG DEEPER

After the main content is presented, you will see a Dig Deeper section, which gives additional detail and content related to the subject of that chapter. This information is not necessary for the course or to complete homework, but gives a higher degree of content if you'd like to learn more.

## CHAPTER INTRODUCTION PAGES

Each chapter will have an introduction page that will include a chapter outline, Learning Outcomes, which list what you will be able to do by the end of that class and textbook section, and Why It Matters, which explains the importance of the concepts taught in that class/section and how they apply.

## COMMON TERMINOLOGY USED IN THIS BOOK

You will see sections and terminology that repeat throughout this book.

When you see the term **course**, it is referring to the course as a whole, all 13 classes. Conversely, when you see the term **class**, it is referring to one specific class within the course.

The term **basics** refers to a summary of the key basic lessons taught in that chapter.

There are **appendices** at the end of this textbook listing: formulas, terminology, tax forms, further reading, online resources, and sources used for the creation of this course.

**Templates and resources** will give specific examples of documents instructors use in their own stores and will typically be links to those documents. These will also sometimes be documents that could not be incorporated directly into the textbook.

Finally, **sources** are the materials instructors consulted for research when developing the course.

From now on, any time you see a bolded word, it means that word can be found in the glossary.

*Chapter 1*

# Introduction to Bookstore Finances

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Understand the structure of the course.
- Understand the requirements for your course project of creating a financial dashboard.
- Identify common terminology and concepts that will be used throughout the course.
- Identify the financial statements you will learn about in this course.
- Understand the basics of financial dashboards.

## CHAPTER OUTLINE

**1.1** The Role of Finance in a Bookstore
**1.2** Money Emotions
**1.3** Common Terminology & Concepts
**1.4** Cash vs Modified Cash vs Accrual Accounting
**1.5** Introduction to Financial Statements & Budgeting
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## WHY THIS COURSE MATTERS

Your financial reports and systems help you understand the overall financial health of your business and help you manage your store operations. Your financial dashboard provides critical information about your revenue, expenses, profitability, and your ability to meet your financial obligations. It's important that you understand how these all work together and how to analyze your reports and build efficient systems so you can extract good information on how your business is performing and how you can improve.

Understanding and being able to analyze your financial reports and data helps you make operational and strategic decisions and to take appropriate action when something goes awry.

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## 1.1 THE ROLE OF FINANCE IN A BOOKSTORE

What exactly do we mean when we say "finance"? **Finance** encompasses the systems of money across your business, including operations, strategy, and management. While it does have roots in scientific fields like math, statistics, and economics, there is an art to finance as well. Human emotions also play a huge role in finance and how decisions are made.

What about finance inside of a bookstore specifically? Bookstores are businesses, so the general financial reports like **Profit & Loss Statements (P&L)**, **Balance Sheets**, and **Cash Flow Statements** apply, along with debt and tax management, budgeting, accounting, and bookkeeping. But as we all know, bookstores are our own little world. We also contend with co-op, events, low margins, filling out the ABACUS survey, and working with publishers and credit reps.

This means that when managers of bookstore finances look at the traditional reports, you're looking for different things and tracking different metrics. It also means that bookstores may have versions of reports for different parts of our business, for example, a general P&L and an events P&L. On top of that, there are many different bookstore models, with more cropping up every day.

The way a pop-up or mobile bookstore handles finances is going to be different from a traditional brick-and-mortar, which is different from a nonprofit, or a co-op, or a worker owned store, or an online store, or a boutique store.

The role of finance inside your particular store is ultimately up to you, as only you know the particular ins, outs, and quirks of your community, your store mission, and your model. For some stores, money will play a larger role, and for other, more mission-based stores that aren't as profit-driven, it will play a smaller role. At the end of the day, though, we all need money to operate, so in this course, we hope to give you a good foundation that you can then use to build robust systems that will ensure your finances can support your mission and goals.

## 1.2 MONEY EMOTIONS

Finance is a lot of dense and dry information, and yet money can bring up a LOT of emotions. Maybe this is because you grew up poor and were always stressing about whether you'd have food. Maybe you made some not-so-great financial decisions in the past and don't want to repeat your mistakes. Maybe you have a lot of money and have some guilt surrounding that. Money can trigger really strong emotional reactions, and it's important that we acknowledge that.

As you move through this course, explore your own money story and emotional connections to money, as that will help you make better financial decisions. What are your experiences, especially in childhood, that shaped how you think about money?

Try to find at least one story, memory, or fundamental idea that you're holding onto that has shaped your life surrounding money, and ask yourself how you want to change that story now.

Remember to have some self compassion and forgive yourself for past money mistakes. This subject can get overwhelming, and that's OK. Find calming techniques and ways to move forward.

It's important to get comfortable with being uncomfortable. The information we give in this course is not the end-all-be-all solution to everything finance. Make sure you're asking questions, talking things through with a trusted confidante and your financial advisor and/or accountant, sharing your concerns, and working with others to find the best way to move forward financially. Make sure you're consistently checking in with yourself and giving yourself the grace and the space you need.

You may want to keep a money emotions journal during this course and explore the sensations and feelings that come up for you as we discuss certain subjects. There are also some great recommendations in the "Further Reading" appendix of books and articles to read regarding money emotions.

## 1.3 COMMON TERMINOLOGY & CONCEPTS

You will learn many terms and concepts throughout this course, but there are some common terms and concepts that are important to understand upfront. There is also a full glossary of terms at the back of this textbook.

One basic concept when it comes to finance is that everything must add up, both logically and mathematically. For example, if you're projecting high sales, your inventory levels shouldn't be low. Something else to consider is the **80/20 rule**: 80% of the time, you should look forward, because you can impact what happens next. You should only spend 20% of your time looking back and analyzing. You can learn from your data and use it going forward, but you can't change it, so take the information and see what you can do now.

It's also important to know the difference between accounting and bookkeeping. **Accounting** is the overall process of presenting and interpreting your financial data, and it includes things like tax returns, auditing, reporting, and analysis. **Bookkeeping**, on the other hand, focuses more on recording and organizing your financial data, and it includes things like invoicing, billing, reconciling transactions, and data entry. Bookkeeping is administrative and concerned with accurately recording your financial transactions, whereas accounting is the analysis and interpretation of the data recorded while bookkeeping.

Both accounting and bookkeeping are kept based on a fiscal year, which is the 12-month accounting period that a business uses for financial and tax reporting purposes.

When your fiscal year ends is important for reporting, taxes, inventory, and more.

**Financial statements** or reports are a set of documents that show your store's financial status at a specific point in time that you choose when you run the reports. Financial statements include your Cash Flow Statement, Profit & Loss Statement, and Balance Sheet. Each financial statement tells you something different about your business.

Finally, it's important for you to understand the difference between cash flow, income (or revenue), sales, and profit. **Cash flow** is the real-time money flowing in and out of your business. **Income or revenue** is the total amount of money you generate from your primary operations, regardless of the form of that money. For example, income includes not just sales, but also co-op, credits, and adjustments. **Sales** is income specifically from products that you sold. Finally, **profit** is the money you have left after all income and expenses, including owner compensation, are accounted for. Cash flow, income, sales, and profit are all different ways of looking at money, and profit, income, and sales do not always directly convert to cash.

## 1.4 CASH VS MODIFIED CASH VS ACCRUAL ACCOUNTING

There are two main types of accounting: cash and accrual. There is also a form of accounting called "modified cash."

**Cash Accounting** means you record transactions when the money changes hands. In cash accounting, you don't have to keep track of things like accounts payable and receivable because you would only record the cash when you actually pay invoices, as that's when it leaves your account.

**Accrual Accounting** means you record transactions when they actually happen, regardless of when the money is exchanged. You record income in the period when it's earned and expenses in the period when they're incurred. For example, if you send an invoice to a school and deliver the books before it's paid, in accrual accounting, you would record the sale when you send the invoice, regardless of when the school pays you.

**Modified Cash Accounting** means you use a combination of cash and accrual accounting. For example, you may record most transactions when the money changes hands, but you keep track of accounts payable and receivable, and you categorize inventory as an asset.

## 1.5 INTRODUCTION TO FINANCIAL STATEMENTS & BUDGETING

The easiest way to understand your financial statements is to use the metaphor of a car. The car metaphor is introduced in *Accounting for the Numberphobic* by Dawn Fotopulos, which is a book recommended in our "Further Reading" appendix.

Your **Chart of Accounts** is a listing of every category related to your business. You can view this as your navigation system; it is a road map of how your store organizes all its financial information. You set this up one time, then maybe review on an annual basis.

Your **Cash Flow Statement** shows you the flow of money into and out of your business. There is an official "Statement of Cash Flows" you may use with your accountant; however, most stores track cash flow in other ways. However you track your cash flow, you can view this as your gas gauge; it shows you if you have enough gas (cash) to operate. This is the most important statement for you to review often. Cash is king, and knowing your monthly cycle of cash is important for financial planning. For example, you might have a high amount of cash during the holiday season, but you'll be paying it out during the first quarter. You want to be looking at cash flow at least weekly. If you run out of gas, none of the other reports will do you much good!

Your **Balance Sheet** shows you how much your business is worth as a whole. You can view this as your oil gauge; it shows you the overall health of your business at any moment in time and captures the full results of all your business operations since inception. Your Balance Sheet shows your value as a business and includes your assets, liabilities, and equity. It shows the relationship between your actions and how they affect your business.

Your **Profit & Loss Statement (or P&L)** shows you how much profit you're making (or not). You can view this as your speedometer; it shows you how fast your business is moving, i.e. whether your profit is growing or shrinking. As you'll see later in the course, the profit showed can possibly be misleading if the owner takes a draw versus a salary. The P&L should be reviewed at least once per month.

And finally, your **Budget** is your lane assist – you use it to predict what you think will happen, and to make sure your business doesn't go off the road completely or crash into the car next to you.

## 1.6 INTRODUCTION TO FINANCIAL DASHBOARDS

Going back to our car metaphor, your **financial dashboard** is your traffic light to indicate if you're good to go, need to be cautious and look at something first, or need to stop completely and re-evaluate.

Unlike a profit and loss statement, a balance sheet, or a chart of accounts, a financial dashboard is not an official, universally recognized document. Everyone's dashboard will look different depending on personal preferences and the selected information. A robust dashboard will bring together all your information in one place to give you a complete view of your business in real-time.

When creating your own dashboard, it's important to choose meaningful key measures and to choose the right metric for each measure. Throughout this course, you'll be introduced to many key measures you

could potentially use, and it will be up to you to utilize the grids in your workbook to document which measures you want to track. You will also set thresholds and specific metrics for those measures as we go along. These metrics could be a dollar amount, a straight number, or a percentage, depending on what makes sense for the data you're tracking. It's important to remember that the same data can tell you different stories based on how you look at it, and you can use different metrics for the same data to gather information.

Different dashboards can exist for different roles and views of what you want to look at regularly. Bookstore staff may want to check on sales and inventory, but they shouldn't see payroll numbers unless your store has open books. Your accountant will always want access to a balance sheet, but they don't need to see individual vendor balances. The same goes for different store models and sizes. If you're a nonprofit, your board will need a different dashboard from your staff. If you're a pop-up or bookmobile or a one-person shop, what you want to look at will be different from what large brick-and-mortar stores want to see. And if you're new to finances, you may want to start with a stripped down dashboard and build from there, whereas if you've done this for a while, you may want something more robust. Don't overwhelm yourself. You don't want your list of reports and metrics and actions to be unwieldy, or you'll never use it. You can always add, edit, and customize later.

## QUESTIONS TO ASK WHEN CREATING A FINANCIAL DASHBOARD

When you're putting together your own financial dashboard, there are some questions you should ask yourself:

- What are your financial goals?
- What metrics do you want to track?
- What data do you want to review/track regularly?
- How do you want to look at your data?
- How often do you want to look at your data?
- How often do you want to change your data and make changes to your business?

You should also pay attention to who needs to collect the information for the dashboard and run the reports to check if you're meeting your thresholds. Do those folks have access to your accounting software/POS/system where the information is stored? If some of your data is tracked outside of your accounting software/POS or there are folks who need to view the dashboard who don't have access to those systems, then you'll need to create something separately.

The biggest question to ask yourself is: What actions will you take if you notice a red flag or a downward trend on your dashboard? The green, yellow, and red thresholds on your action grid in your workbook will tell you this. Dashboards are really great, but having the data means nothing if you don't use it!

## SUMMARY

### Why It Matters

Understanding and being able to analyze your financial reports and data helps you make operational and strategic decisions and to take appropriate action when something goes awry.

### 1.1 The Role of Finance in a Bookstore

Finance encompasses the systems of money across your business, including operations, strategy, and management. The role of finance inside your particular store is ultimately up to you, as only you know the particular ins, outs, and quirks of your community, your store mission, and your model.

### 1.2 Money Emotions

Money can trigger really strong emotional reactions, and it's important that we acknowledge that. Have some self-compassion and forgive yourself for past money mistakes. This subject can get overwhelming, and that's OK. Find calming techniques and ways to move forward.

### 1.3 Common Terminology & Concepts

- Everything has to add up, both logically and mathematically.
- Use the **80/20 rule**, looking forward 80% of the time and backward 20% of the time.
- **Bookkeeping** is more administrative and concerned with accurately recording your financial transactions.
- **Accounting** is the analysis and interpretation of the data recorded while bookkeeping.
- **Financial statements** are a set of documents that show your store's financial status at a specific point in time that you choose when you run the reports.
- **Financial statements** include your Cash Flow Statement, Profit & Loss Statement, and Balance Sheet. Each financial statement tells you something different about your business.
- **Cash flow** is the real-time money flowing in and out of your business.
- **Income or revenue** is the total amount of money you generate from your primary operations, regardless of the form of that money.
- **Sales** is income specifically from products that you sold.
- **Profit** is the money that you have left over after all income and expenses, including owner compensation, are accounted for.

### 1.4 Cash vs Modified Cash vs Accrual Accounting

- If you're on a **cash accounting basis**, it means you record transactions when the money changes hands.

- If you're on an **accrual accounting basis**, it means you record transactions when they actually happen, regardless of when the money is exchanged.
- If you're on a **modified cash accounting basis**, it means you use a combination of cash and accrual accounting.

**1.5 Introduction to Financial Statements & Budgeting**

- Your **Chart of Accounts** (navigation system) is a listing of every category related to your business.
- Your **Cash Flow Statement** (gas gauge) shows you the flow of money into and out of your business.
- Your **Balance Sheet** (oil gauge) shows you how much your business is worth as a whole.
- Your **Profit & Loss Statement** (or P&L) (speedometer) shows you how much profit you're making.
- Your **Budget** (lane assist) is used for forecasting and to ensure you don't get too far off track.

**1.6 Introduction to Financial Dashboards**

A robust financial dashboard will bring together all your information in one place to give you a complete view of your business in real-time. When creating your dashboard, it's important to choose meaningful key measures and choose the right metric for each measure. Different dashboards can exist for different roles and views of what you want to look at regularly, as well as for different business models.

**KEY TAKEAWAYS**

- This course is intended for educational purposes only. Financial information is NOT the same as professional financial advice. We are not your accountants or financial advisors; we are here to present information to you.
- The information we will give you in this course is meant to be useful for multiple different business models, and we expect that you will take the information and use it to customize your own financial dashboard.
- Homework will have five parts, helping you build a financial dashboard throughout the course:
  - Document a current financial system.
  - Fill in the reporting grid.
  - Fill in the action grid.
  - Answer the review questions at the end of the textbook chapter.
  - Read the textbook chapter for the next class.
- Don't worry if you didn't process everything immediately. You will hear these terms and concepts over and over again throughout the course.

## KEY TERMS

- Accounting
- Accrual Accounting Basis
- Balance Sheet
- Bookkeeping
- Budget
- Cash Accounting Basis
- Cash Flow
- Cash Flow Statement
- Chart of Accounts
- Finance
- Financial Dashboard
- Financial Statements/Reports
- Fiscal Year
- Income/Revenue
- Modified Cash Accounting Basis
- Profit
- Profit & Loss Statement
- Sales

## REVIEW QUESTIONS

- What is the 80/20 Rule?
- What is the difference between accounting and bookkeeping?
- What are some examples of financial statements/reports?
- What is the difference between cash, modified cash, and accrual accounting?
- What are the four parts to your homework each week?

## ANSWER KEY

- You should look forward 80% of the time and backwards 20% of the time.
- Bookkeeping is more administrative and concerned with accurately recording your financial transactions. Accounting is the analysis and interpretation of the data recorded while bookkeeping.
- Profit & Loss Statement, Cash Flow Statement, Balance Sheet.
- Cash accounting basis means you record transactions when the cash changes hands. Accrual accounting basis means you record transactions when they actually happen, regardless of when the cash is exchanged. Modified cash accounting means you use a combination of cash and accrual accounting.
- Document a current financial system; Fill in the reporting grid; Fill in the action grid; Read the textbook chapter for the next class.

*Chapter 2*

# Daily Store Finance

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Create a daily cash and credit card reconciliation system.
- Implement internal controls to reduce chances of theft or embezzlement.

## CHAPTER OUTLINE

**2.1** The Basics
**2.2** Daily Reconciliations
**2.3** Petty Cash Procedures
**2.4** Internal Controls
**2.5** Managing Store Credit Cards
**2.6** Monitoring Available Cash
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Fraud & Loss Prevention

## WHY THIS MATTERS

Keeping track of cash is a critical oversight tool for business owners. When employees know you are paying attention to the money coming in and going out, there is less chance of theft. Having a structured daily routine allows for catching errors or issues quickly. When you closely monitor cash inflows and outflows, cash planning and longer term forecasting become much easier. Building strong internal controls for your business helps mitigate risk, protect assets, ensure accurate information, and encourage adherence to internal policies and external regulations and laws.

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## 2.1 THE BASICS

Daily Store Finance refers to the fundamentals of daily finance, including cash handling and **reconciliation** and **internal financial controls**. Having a regular daily reconciliation process will ensure the legitimacy of your finances.

In this chapter, you will learn why you need to reconcile cash daily, example procedures for daily register reconciliation, how to reconcile cash and credit cards with your accounting system, and how to monitor and replenish petty cash. You will also learn how to put internal controls in place to reduce the chances of theft or embezzlement and get some tips on managing store credit cards and monitoring available cash.

If you'd like to dig deeper, you may also review the section on fraud and loss prevention at the end of this chapter.

## 2.2 DAILY RECONCILIATIONS

Balancing and reconciling cash and sales is an important part of your business. Although bookselling is so much more, at its core it is still a business, and building systems to handle cash creates a foundation for everything you do in your store. Employees will know that cash handling is important when management and ownership ensures that efficient systems are implemented. Cash reconciliation can easily slip through the cracks if you don't have strong systems.

Although different stores will have different processes for daily reconciliations, some steps generally remain the same. The following are the steps our instructors have found most useful for their reconciliation processes.

The first step is to run your "daily activity" report from your Point of Sale system (POS). This is sometimes called an "X Tape" or a "Z Tape." It's important to run this report after you close for the day so that no transactions take place between when you run the report and when you perform your reconciliation.

Next, count the cash and any checks in the cash drawer and add it up. If you have a base amount to leave in the **till**, subtract that amount from the total you counted. The difference will be your bank deposit. Compare the amount of the cash counted to what your POS reported as your total cash sales for that day, then document the over/under, or the difference between the cash you actually have and what your POS thinks you have. If the amount is substantially off, recount and double check your math to ensure you aren't missing a cash sale.

To prepare for the next day, recount the till to ensure it balances to the amount you wish to leave in to start the day. This is also a good way to catch small mistakes, like if you missed a penny or had two $1 bills stuck together. It's also useful to ensure the till has the correct amount of bills and rolls of coin to make it easier for opening the next day.

After the till is ready for the next day, make sure you lock it in a secure place prior to leaving the store. Ensure your bank deposit is either made immediately or also kept in a secure place.

When opening the store, it's important to recount the till again to ensure the day is starting with the correct amount of cash. This is another control that could catch mistakes made when counting the closing cash.

This may seem like a lot of work and math, but having controls in place are important to control theft. If you have employees who will work the till, you should train them on your Opening and Closing cash procedures, how to track what bills the customer actually gave them, and how you would like them to keep the till organized.

Even if you do not have a brick-and-mortar store, you should create a cash reconciliation process that happens at the start and end of each pop-up or event, and ensure that you have a safe or another secure place to hold money until you make your deposits.

At a minimum, consider identifying a starting register cash amount for each day, with plenty of small bills and rolls of coin. Your reconciliation paperwork should clearly document any money the register is over or short for the day.

The detailed daily activity report (the "X" or "Z" Tape) should be attached to the reconciliation so further investigating of discrepancies can be initiated. Staff need to know where to put the monies from the day and the paperwork.

As your store evolves, you may continue to expand and develop your system, so make sure to revisit what you are doing and why on a regular basis to ensure your store continues to be efficient.

## RECONCILING TO YOUR ACCOUNTING SYSTEM

In addition to reconciling cash each day, it's also important to check your credit card processor to verify the amount collected with your POS system. It's possible that the amount may be off if you made sales that do not post until the next day. Document any discrepancies so you can clear those on subsequent days.

Once everything is verified, you can create an entry into your accounting system to categorize your sales for the day. Stores can do this in a variety of ways. In some accounting systems, this may be a journal entry, and in others, it may be categorizing deposits. Or, you may have an integration between your POS and accounting systems that creates the entry for you.

No matter your system, what's important is that you properly categorize the sales transactions of the day, including cash, credit

card, gift card, deposits for prepaid books, subscription service activities, and school sales, if you categorize those separately.

On days where you have events, pop-ups, book fairs, take tons of preorders, or have anything else outside of your regular store operations, your procedure will look different. Nevertheless, it's daily reconciliation that keeps mistakes from slipping through the cracks.

## 2.3 PETTY CASH PROCEDURES

**Petty Cash** is an accessible store of money kept by a business for making change for the registers and is often used for small expenditures. Your store may or may not keep petty cash on hand; however, if you do and you have employees, it's important that they know the procedure for handling and using the petty cash.

You may have a separate store of petty cash, or you may authorize your employees to use cash directly from the register using a "paid out" transaction. Or, instead of petty cash, you may just authorize certain employees to make purchases as needed.

No matter your policy, any cash used for store expenses, whether from a petty cash stash or directly from the register, should be documented.

## 2.4 INTERNAL CONTROLS

**Internal controls** are a key part of building a strong financial system. No matter the size of your store, we recommend creating basic controls to reduce the chances of theft or embezzlement. As your store grows in terms of the number of staff or level of complexity, you should review your internal control procedures and make adjustments if necessary, and make sure you don't cede too much control over cash related activities.

While each store is different, the following are the controls that our instructors have found most helpful.

First, make sure you're depositing cash and checks regularly, and if you can, make sure whoever is preparing the deposits is not the same as the person who does the monthly bank reconciliation. If you're a small store or do not have employees, perhaps your outside bookkeeper could do the reconciliation while you make the deposits.

Another control is to track voids and refunds. First, make sure you have clear procedures for when it is allowable to void a sale and how to process merchandise refunds. One example is to require a log in when making a void or a refund to track who is responsible for each transaction. That basic control is a great way for your staff to know they are accountable and responsible for what happens when they ring up a customer.

The reason for controls around voided sales is because an employee could void a cash sale and pocket the cash. Controls ensure this doesn't happen.

You may want to have a bookkeeper verify that void paperwork is done and nothing unusual occurred.

For refunds, if you have staff, make sure they are trained to inspect the items returned and make sure they can be resold. Periodically review your daily transaction reports for refunds to ensure they seem reasonable. Consider adding a process to watch for cash refunds or ensure a supervisor or manager is signing and/or approving those. If you allow for returns without a receipt, consider requiring customers to provide a driver's license and/or tracking those returns with forms. Internal theft can occur with employees issuing fraudulent cash or merchandise credits returns.

If you notice an uptick in voids and/or refunds from a particular employee, you will want to further investigate and keep a close eye on them. Could it be a training issue, or is it something more?

Some additional controls to consider are running a monthly report showing inventory items that had a price change and a report that shows who edited inventory to catch mistakes and ensure only employees who are authorized are making changes.

Also, consider monitoring “no sales” activity at the register if that is something your system can track. Sometimes excessive “no sales” may indicate that a cashier is making change for a sale that was not recorded.

Consider enabling void and or “no sale” passcodes that only supervisors or managers know, and perhaps change these passwords quarterly.

You may also want to consider not making change for customers that want to break large bills. Finally, if you have a safe, make sure you keep the keys locked away.

## 2.5 MANAGING STORE CREDIT CARDS

Most stores use credit cards for a portion of their purchasing activities, including inventory and operational expenditures. It is important to have clear policies and procedures for issuance and usage of store credit cards. You may want to consider issuing different cards for different purposes, which may help with tracking, but may also help with limiting unauthorized use.

Stores should maintain a list of credit cards issued to each staff member with the credit limit. It is also a good idea to make a copy of the cards and keep it on file so you have easy access to the card number. Keep the card issuer customer service phone number there as well, in case of a lost or stolen credit card. When new cards are issued, activate them before providing them to the employee. The phone number associated with the cards should be the store phone number.

It is a privilege to have a store credit card, and there need to be clear expectations

regarding the types of expenses to put on a credit card, even if you're the only one using it. Receipts should always be required, along with clarification of the expense item if the vendor or visited store doesn't have obvious line item descriptions on the receipt. This helps with knowing how to enter the expense into your accounting system.

Just like bank statements for your bank accounts, credit card statements should be reconciled monthly, and promptly. You should know the cutoff date for the credit card statement and set up email notifications for when the statement is available online. Verifying the prior statement balance matches to your accounting report is a good place to start because it is too easy to date things back in time when you use QB, so matching the balance is a way to catch mistakes.

If you purchase from Faire or similar places, this can become challenging because you receive that inventory but don't have to pay for 60 days, so your accounting system may show a credit card charge two months before it is actually charged. In this case, you may want to create an outside system, like an Excel or Google spreadsheet or Airtable table, to reconcile any timing differences between your accounting system and credit card statement.

Be diligent about receipts and make recurring entries in your accounting system if you can to save time and keep data entry as simple as possible.

## 2.6 MONITORING AVAILABLE CASH

It's essential to monitor your bank account daily. This can be delegated depending on your size and takes just a few minutes a day.

The first thing you need to be able to do this is online banking. Review your online banking daily, checking to see what the bank balance is and reviewing what checks have cleared. Your bank balance minus outstanding checks is your available cash. If you know this number each day, you will know how much you can spend and/or how much you may need to borrow.

If your accounting software is completely up to date, then you could use that, but frankly, it is nearly impossible to keep your bookkeeping in perfect alignment with your bank account at any given moment, so using your online banking allows you to know daily how much cash you have "available" and ensure that you don't spend more than you have. Monitoring your bank account(s) in this way is also a way for you to monitor for fraud.

One way to simplify things depending on your size and volume is to consider ways to do electronic payments to vendors. The upside to this is that it helps eliminate check fraud, but it reduces your float of checks in transit and may be more costly to administer when you are paying many vendors. Consider **Batch for Books**, which is free! Research the options and do what works for you.

When monitoring your bank accounts, consider ensuring you have enough cash to operate and/or to have an emergency fund. There are many ways to do this, but in an ideal world, you would bring in enough cash year round to allow you to build up inventory for any seasonal sales periods you may have.

## SUMMARY

### Why It Matters

Building strong **internal controls** for your business helps mitigate risk, protect assets, ensure accurate information, and will encourage adherence to internal policies and external regulations and laws.

### 2.1 The Basics

Daily Store Finance refers to the fundamentals of daily finance, including cash handling and **reconciliation** and **internal financial controls**. Having a regular daily reconciliation process will ensure the legitimacy of your finances.

### 2.2 Daily Reconciliations

Although different stores will have different processes for daily reconciliations, some steps generally remain the same:

- Run a daily activity report in your Point of Sale system (POS).
- Count the cash and any checks in the cash drawer and add it up. If you have a base amount to leave in the **till**, subtract that amount from the total cash you counted. The difference will be your bank deposit.
- Compare the amount of cash counted for the day to what your POS reported as your cash total, then document the over/under.
- Recount the till, then lock it in a safe place.
- Count the till again when opening the next day.
- Reconcile with your accounting system.

### 2.3 Petty Cash Procedures

**Petty Cash** is an accessible store of money kept by a business for making change for the registers and is often used for small expenditures. Your store may or may not keep petty cash on hand; however, if you do and you have employees, it's important that they know the procedure for handling and using the petty cash. Any cash used for store expenses should be documented.

## 2.4 Internal Controls

- Deposit cash and checks regularly, and if you can, make sure whoever is preparing the deposits is not the same as the person who does the monthly bank reconciliation.
- Track voids and refunds and have clear procedures for when it is allowable to void a sale and how to process refunds.
- Run a monthly report showing inventory price changes and a report that shows who edited inventory to catch mistakes and ensure only employees who are authorized are making changes.
- Consider monitoring “no sales” activity at the register if that is something your system can track.
- Consider not making change for customers that want to break large bills.

## 2.5 Managing Store Credit Cards

Most stores use credit cards for a portion of their purchasing activities, including inventory and operational expenditures. It is important to have clear policies and procedures for issuance and usage of store credit cards and clear expectations regarding the types of expenses to put on a credit card.

Just like bank statements for your bank accounts, credit card statements should also be reconciled monthly, and promptly. Be diligent about receipts and make recurring entries in your accounting system if you can to save time and keep data entry as simple as possible.

## 2.6 Monitoring Available Cash

Review your online banking daily, checking to see what the bank balance is and reviewing what checks have cleared. Your bank balance minus outstanding checks is your available cash. If you know this number each day, you can know how much you can pay and/or how much you may need to borrow.

## KEY TAKEAWAYS

- Having a procedure for daily reconciliations is important to track your cash and decrease the possibility of theft.
- Internal controls are a key part of building a strong financial system. No matter the size of your store, we recommend creating basic controls to reduce the chances of theft or embezzlement.
- It is important to have clear policies and procedures for issuance and usage of store credit cards and clear expectations regarding the types of expenses to put on a credit card, even if you're the only one using it.
- If you monitor your available cash each day, you can know how much you can spend and/or how much you may need to borrow.

## TEMPLATES & RESOURCES

- **Example**: Melissa's Till Reconciliation Sheets for Closing and Opening
- **Example**: Melissa's Daily Workflow - Cash/Credit Card Reconciliation Excel
- **Example**: Steve's Cash Receipts Form and Closing Tape

## KEY TERMS

- Internal Controls
- Petty Cash
- Reconciliation
- Till

## REVIEW QUESTIONS

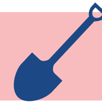
**True or False**: Your store should count your register cash at the beginning of each day and compare it to the register closing cash from the previous day.

**True or False**: Monitoring voids is an unnecessary time waster.

**Multiple Choice**: What are ways that you can control theft:
A. Trust your employees to not steal
B. Have separation of duties
C. Reconcile and deposit whenever you have time
D. Have checks and balances between staff and supervisors/managers
E. B & D

## ANSWER KEY

- TRUE
- FALSE
- E

D I G  D E E P E R 

## FRAUD & LOSS PREVENTION

Fraud and loss prevention is not new to retail or bookselling in particular, but here are a few things to watch for.

Check fraud has continued to plague businesses. This is when someone gets a hold of one of your checks and then creates a fraudulent check drawn on your account. It is best to catch this kind of fraud early. Banks offer services to help prevent this (often called "positive pay"), but generally your bank will charge a fee for this service, and you need to provide them with lists on a regular basis of checks that are issued on your account. You can avoid this type of fraud by not issuing live checks, but not everyone accepts ACH or wire transfers (and those methods can cost extra as well). One option is for you or someone on your staff to monitor your bank account on a regular basis, so you may catch this quickly and recover funds or reverse fraud. If you wait until the bank statement is reconciled, it may be too late.

Another prevalent fraud is for someone to text or email posing as an owner, manager, or director telling an employee to do something unusual like buy a gift card on the company credit card then fax/text/email copies of the cards, or asking via email to wire money to someone. The larger your organization, the more prevalent this is, but if you have solid systems in place to prevent this or have strict procedures, most scams can't break your system.

Other fraud can arise with employees voiding cash sales or issuing fraudulent refunds. Employees may also be selling items for an unauthorized discount, giving item discounts away, or using a fake credit card to make purchases.

Thieves also like to pass counterfeit bills. If you start having a problem, consider implementing pens or counterfeit detector machines. **Here is a poster** you can show employees about watching for counterfeit bills.

Thieves also like to pass fraudulent checks, so consider putting procedures into place to protect your store from accepting fraudulent checks. Ideas include checking ID and writing that information on the face of a check and/or using a check approval vendor. For your website, if you are getting fraudulent transactions, consider implementing fraud prevention like No Fraud.

## DIG DEEPER

Even trusted accounting employees can find ways to break the system. Ensuring that your store has systems in place that are being monitored is one of the best ways to protect against theft.

Another way for theft to occur is in accounts payable. For example, someone creates a fake vendor in your accounting system and enters invoices that are paid to that vendor. The checks get deposited, and it is hard to tell that something is going wrong. Consider limiting who and how a vendor can be added to your system, and consider implementing systems that require someone to approve invoices. For example, you could require that every expense invoice that is entered have the owner’s initials in addition to a manager approving the expense, with limited exceptions. This system is very rigid but helps prevent just anything from getting entered and paid.

Loss prevention can also be extended to inventory theft, and that list can be exhaustive as well. There are so many ways for bookstores to get stolen from, but with good planning and procedures, you can limit it.

*Chapter 3*

# Vendor, Debt, & Tax Management

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Track your debt and understand your financing options.
- Create a tax calendar.
- Create a system for managing your invoices.

## WHY THIS MATTERS

From a business perspective, bookstores deal with vendors every day, and they are the source of many of our financial transactions. On a practical level, developing systems for handling vendor finances and paperwork will create efficiencies. On a gut level, building relationships with your credit representatives and staying in regular communication with them will give you the emotional leverage and goodwill that you need to get through tough times.

Knowing how debt and taxes work are also key parts of owning or managing a business. Missing tax deadlines can have serious impacts on your store. Utilizing debt can help your store manage cash flow during low profitability periods when you may need to build inventory.

## CHAPTER OUTLINE


**3.1** The Basics
**3.2** Vendor Management
- **3.2.1** The Importance of Payment Terms
- **3.2.2** Working With Credit Representatives
- **3.2.3** Managing Vendor Paperwork & Cash Flow
- **3.2.4** Paying Vendors
- **3.2.5** Two-Way Accountability
- **3.2.6** Damage Claims & Credits

**3.3** Debt & Tax Management
- **3.3.1** How to Build Business Credit
- **3.3.2** Why Debt Can Be Beneficial
- **3.3.3** Financing Options
- **3.3.4** Keeping Track of Outstanding Balances
- **3.3.5** Typical Business Taxes
- **3.3.6** Tax Filing & Reporting

Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Vendor Management: Checklist of Files to Have Handy
**Dig Deeper**: Debt & Tax Management: Banking Relationships & Other Required Tax Reporting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## 3.1 THE BASICS

Vendor, Debt, and Tax Management are crucial to running your business. Developing systems for handling the paperwork and finances surrounding vendors, debt, and taxes will create efficiencies that make day-to-day finances much easier.

This chapter will cover a variety of topics: working with and paying your vendors, managing vendor paperwork and cash flow, how to build business credit, why debt can be beneficial, tracking and paying off debt, financing options, typical business taxes, and keeping track of tax filings.

If you'd like to dig deeper, you may also review the sections at the end of this chapter, which include a checklist of files to have handy and information on creating and maintaining banking relationships and other required tax reporting.

## 3.2 VENDOR MANAGEMENT

Bookstores deal with vendors every day who are the source of many financial transactions, not to mention most of the paperwork that will bury you unless you develop a good paper handling workflow or handle everything electronically. Developing systems for handling your vendor finances and paperwork will create efficiencies and staying in regular communication with your credit representatives will give you the goodwill you need to get through tough times.

### 3.2.1 THE IMPORTANCE OF PAYMENT TERMS

The first step to managing vendor finances is the establishment of **terms accounts** with your main suppliers. There are several good reasons to have payment terms, or lines of credit, with all your vendors. This will allow you to:

- Spread large payments out for longer periods while avoiding fees.
- Maximize cash flow or the cash in your business bank account for as long as possible.
- Gain leverage against the vendor in case of damages or errors.
- Build trust and a relationship with your vendor.

Setting up accounts with vendors is an important step to minimizing your **Cost of Goods Sold**, which you'll learn about in a later chapter. In the beginning, when you're unproven, vendors may force you to pay for purchases upfront on a "prepaid" basis. Over time, though, it's important to get your accounts set up for terms. Having terms means you can send in an order and the vendor will ship your order, but the bill won't come due for another month. That's called having Net 30 terms. It's possible to get terms for 60 days, 90 days, or even 120 days with certain publishers or for certain promotions. Taking advantage of terms means maximizing the amount of time you have to sell merchandise before you pay for it.

Don't be afraid of having terms accounts with publisher vendors and Ingram. If you use a credit card and aren't able to pay it off each month, you will rack up interest charges, which will cut deeply into your bottom line. Having a terms account is no different than having a credit card you use for purchases, but with terms, you get an even longer time to pay without any interest charges being added to your bill. Most of the time, you'll sell at least some of the books from that order before the bill is due. The more accounts you have set up with terms, the better your reputation in the industry. Over time, your credit record will allow you to add new vendor accounts and get terms with them too.

Using terms helps keep cash in your bank account for other things you might need to pay, such as payroll or rent. Establishing good vendor terms and credit for your business will also allow you to obtain a business credit card that can be separate from your personal credit card, which will make your bookkeeping much easier.

The typical pattern for setting up terms accounts might be to start with an Ingram account, then move to buying directly with some of the larger publishers like Macmillan, Penguin Random House, and HarperCollins. At any given moment, when a bookstore adds up all the bills they owe to all publishers plus Ingram, an average bookstore could have accounts payable of around $30,000-$50,000 or more, but that number doesn't necessarily have to be scary.

This is known as **productive debt**, because it is tied directly to your productivity, or sales. Credit in this case aids your business in potentially earning profits, which can build capital and ultimately fuel expansion or whatever else you'd want to do with more profits, such as increasing wages or putting money into a savings account.

As long as you're careful with cash flow and keep track of your orders and the bills coming due so you don't overextend, using terms will help you grow your business or keep it sustainable for the long term. If some books or entire sections are selling well and you run low on them, you can order more of what's selling with the reasonable expectation that you will be able to pay for it. If you don't order them, you'll miss out on potential sales, which may make it harder to pay your overhead costs, too. It's a case of, "if you stock it, they CAN buy."

You always want to have fresh inventory coming in, both to fulfill special orders and for your regular customers who love to browse and see what's new in their favorite sections. If you never have anything new, customers will get bored and stop looking. It's a sure sign of a failing store when your displays stop being fresh and your shelves always have the same things on them. Terms allow you to keep things fresh for your customers as long as you use them carefully.

Terms will also give you the flexibility to handle unexpected large event and school orders.

If your payment record is solid, the publisher will be willing to raise your credit limit for you to get the books for a big author event. And, using terms and keeping your credit card paid off gives you wiggle room to stock sidelines and other items for which you need to pay upfront. Paying early on some terms accounts may get you another partial point of discount, such as with Ingram and Macmillan, and that can add up if you order a lot from those vendors.

Finally, paying on terms establishes your store as a well-run business. The act of extending credit, using that credit, and paying it off on time, builds an ongoing relationship between your business and the vendor. It also gives you leverage that can be helpful. For example, if you don't pay an invoice until the damage credits are received from that shipment, and a credit representative emails to ask where the payment is, you can then can point to the damage claim you're still waiting for, and the credit representative will back off and ensure you get the credit memo pretty quickly after that.

If you haven't already paid an invoice, it's also easier to handle shortage discrepancies when something doesn't arrive with an order that's supposed to. Please note that while it's fine to not pay a bill until damage credits are received, this does not work for returns credits. You shouldn't wait for or depend on returns credits to pay current, open bills unless you're truly cash strapped.

### 3.2.2 WORKING WITH CREDIT REPRESENTATIVES

It's important to establish relationships with your publisher credit representatives. They can provide you with your most recent statements, your store's terms, take credit card payments (if able), identify credit memos, provide ACH payment information, and more. They can also help you "flex" your credit limit if you have a big book fair or event and can help if you have a rough month and need more time to pay your bill.

There are several ways to determine who your publishing credit representative is. Usually, you will see your credit representative's name, email address, and phone number at the top left corner of the monthly statement from the publisher. You can also call the financial department of the publisher/vendor. Typically, if you call customer service, there is an option to speak to the credit department.

Finally, you can ask your sales representative to help you locate your credit contact. This is usually a last resort option if you are not having your phone calls or emails answered. Your sales representative can also advocate for you if you have issues with your credit representative.

Once you have their information and know the best way to communicate with your credit representative, the next important step is to determine when you should communicate with them.

It's important to contact your credit representative in the following situations:

**If you're going to be late with a bill payment.** If you know you will be late with your payment for the month, you must get in touch with your credit representative as soon as you know. The most important thing you can do is be upfront if you are struggling with payments. If you make a late payment with no notification, it's possible that your orders will be held until payment is made. Depending on how late the payment is, it could result in outside collection on behalf of the publisher, and your account could be closed. If you have a returnable account and are cash strapped, one way to help pay off your balances is to return inventory.

**If you need to stretch your credit limit for a major event.** There are times where you have the opportunity to do a major event, and if you don't have access to a credit card or don't have the savings to prepay for books, you can talk with your credit representative. Keep in mind, though, that your payment and order history will be reviewed to determine if they will grant you a credit limit increase, even temporarily.

**If you're preparing a payment and want to ensure you have the most up-to-date account status.**

**If you want to change from one type of account to another (e.g. prepaid versus terms).** When you first filled out your new store applications, in some cases, you had the choice to create a prepaid account or to set up terms. You can ask your credit representative to change the type of account you have if needed. If you've been on a prepaid account for at least a year without issues, it may be time to ask for terms.

## SAMPLE LATE PAYMENT EMAIL

I hope this email finds you well. This is [NAME] from [BOOKSTORE], account number [ACCOUNT NUMBER]. I would like to first apologize for the delay in payment of invoice(s) [INVOICE #] dated [DATE].

We are committed to remitting payment as soon as the funds are available. If all goes well, we are hoping to do this by [DATE]. If we aren't able to make the payment in full, we will pay [$AMOUNT] on a [WEEKLY/MONTHLY] basis until the total due is paid in full. If we do a partial payment, our first installment will arrive no later than [DATE]. I kindly request you bear with us. Thank you for your cooperation and understanding during this time.

Best,
[NAME], [TITLE]

**If you need to free up available credit from a return to get an order released.** Let's say you made a return a month ago, but the invoice for the returned merchandise is due at the end of the month, and you still don't see a credit memo for it. This is the perfect time to reach out to your credit representative and let them know so they can note the account. Make sure you know the monetary value of the merchandise you returned, which is the wholesale price, not the retail value.

### 3.2.3 MANAGING VENDOR PAPERWORK & CASH FLOW

You will usually see three types of financial paperwork from your publisher vendors: packing slips, invoices, and statements.

Packing slips are sent with each shipment and list the items and quantities that were shipped. Sometimes, they also show items that were backordered and *not* shipped. Occasionally, there will be information about the price for each book, the discount you received, and the total amount to be billed for the shipment.

You may be tempted to use packing slips to receive the order into your point of sale system; however, we recommend using the invoice for the order to both receive and pay. Invoices officially list what you owe for that shipment, as per the vendor's records. They will show the items shipped, quantities, discount for each item, any freight charges, special promotional discounts, and the total amount due. Invoices also show what payment terms apply to the order and the date payment is due, and the correct remittance address for the vendor if you need to mail a check. If the vendor has a payment portal, they'll provide that information on the invoice as well.

Invoices can be found in various ways. Some smaller publishers include them inside or in a pocket on the shipment box. Some publishers have their own portals on which you can look up invoices and credit memos. You can easily get invoices and credit memos on **Batch for Books** from the publishers that use it. Ingram and Ingram Publisher Services invoices and credit memos are on iPage, and you can set them up to be automatically emailed to you directly. Many publishers will also email invoices and credit memos, and this is always faster than snail mail. If you're unable to find an invoice, get in touch with your credit representative, customer service, or your sales representative for help.

Vendors will also send you monthly statements that show all of the invoices and credit memos that are still open on your account with "open" meaning *unpaid*, or in the case of credits, *unused*. Occasionally, the information on monthly statements will not be completely accurate, for example, if your recent payment arrived to the vendor just after they issued the statement. Sometimes, they'll show many invoices as "open" even while also showing your payments for all of those invoices. But in most cases, comparing your statement to what your accounting system shows you owe will help you see what you need to track down and report back:

missing shipments, missing credit memos, incorrectly applied payments, and so on. If your statement is inaccurate because they got your payment after it was issued, you can contact your credit representative for an updated statement so you're working off the most current information as you prepare a payment.

When the monthly statement arrives, it really helps to compare the statement to your bookkeeping records for that vendor to see if they've applied payments correctly, if they've used the credits you told them to use, if they show something as unpaid that you already sent payment for, and occasionally, if they show an open invoice for a shipment you never received.

Accurate receiving is important, as you need correct inventory records for tax and cost of goods sold purposes. If you use your point of sale system to determine cost of goods sold, the receiving process is the only way the cost is attached to your goods while also maintaining accurate inventory records.

During receiving, you tell your point of sale system how many of each item you received, exactly how much it cost, and how much you will charge customers for that item. This is why it's important to use your invoice when receiving and not your packing slip. Your packing slip may not even have the correct total for an order, even though it shows you *a* total. The packing slip total may not account for shipping or the discounted cost of the items.

Providing correct invoice information that includes shipping charges and matching the invoice to the receiving batch in your point of sale system ensures that your cost of goods sold is accurate when you run reports. It's also a great time to catch errors in invoicing, for instance, if they did not apply the correct discount, added freight charges when you're supposed to get free freight, or if they don't have your sales tax permit on file and charged you sales tax.

Receiving with the correct financial information is far too important and detailed to let just anybody do it, and we recommend creating a careful checklist and written instructions for training purposes once you've determined your system.

The easiest way to ensure the accuracy of the remittance information you send for vendor payments is to ensure your invoices are in your accounting system and to pay them from there. Paying invoices from your accounting system also prevents duplicate invoice payments, produces accurate profit & loss and balance sheet reports, tracks invoice due dates so you can use your terms to the max, and makes it easy to issue payment for many invoices at once.

Batch for Books makes this process easy. You can sync Batch with your accounting system to automatically enter invoices, or you can use a data-extraction service like Melio or AutoEntry to look at your invoice PDFs or images and to create invoice entries that will

automatically upload to your accounting system. Finally, you can enter invoices manually if needed.

We recommend choosing one day per week or two days per month to handle invoice payments. Organize the invoices that have been approved for payment first by vendor then by date. Then group the invoices into payment methods: ACH, Batch, paper check, etc. Before you get started each month, make sure you've done everything you can within your accounting software to save time, such as setting up each vendor record with your terms, account number, their remittance address, and the default purchase account for that vendor.

### 3.2.4 PAYING VENDORS

There are many ways to pay vendors, including:

- Paper checks
- Credit cards
- Automatic Clearing House (ACH), also known as Electronic Funds Transfer (EFT), which includes Melio and others.
- Ingram iPage online payment
- Batch for Books
- Vendor's electronic payment portal or payment link
- Through your accounting software, such as Quickbooks

You should try to only use credit cards to pay vendors if you're able to pay them off each month. Some credit cards will give you cash back or points for travel, so for those inevitable credit card purchases, it pays to research the most useful card for you.

If cash flow is tight, instead of using a credit card, you could make smaller weekly payments to vendors instead of one big payment at the end of the month.

Electronic payments tend to be easier than paper checks, as you don't need to worry about printing and mailing them. They're also more secure and have less potential for fraud. An easy way to set up electronic payments is to email all your vendors for ACH payment information and set them up in your bank account or accounting software. You'll only need to do this once, then you're set up as long as the ACH information stays the same.

One issue with publishers is that, if they are not on Batch, it can be hard to get them to apply payments properly. This means it's important to always send remittance information for your payments.

This can be part of the paper check stub listed on a remittance enclosure with your check, or, if you make payments electronically, as an email that you send to the dedicated email address for remittance listing the invoices and credit memos you're paying. You'll have to ask your credit representative for the appropriate remittance email address.

Sometimes, despite your best efforts, vendors still make mistakes, so keep a copy of your remittance information handy to compare to your next monthly statement.

Check to see if it's accurate, and if you find discrepancies, call or email customer service or your credit representative to get it fixed ASAP. Sometimes you'll see a large unapplied payment as a credit on your account and invoices showing as unpaid that you meant to pay with that unapplied payment.

### Prioritizing Payments

There are 2 main rules for prioritizing vendor payments:

Pay your main suppliers first, as these are your biggest bills. Generally, this means Ingram and at least one large publisher.

If you can't pay everything, make partial payments with all main suppliers after making sure you've paid your number one supplier in full.

If you have trouble paying bills, you'll learn which vendors will put you on credit hold very quickly, and these are the ones to pay first. The smaller vendors will often cut you more slack, but those smaller bills sometimes feel easier to pay since the amounts are more manageable.

## 3.2.5 TWO-WAY ACCOUNTABILITY

Sometimes it feels as if all the power in your relationship with your vendors is on their side, but this isn't always the case. Remember, we are their customers, and they are supposed to provide us with customer service. If you keep track of damage claims, co-op claims, submitted orders, and submitted payments with remittance information, and you regularly check on the vendors' completion of these items, on those occasions when they make mistakes or neglect to follow through,

### SAMPLE EMAIL TO CHANGE VENDOR ACCOUNT TYPE

Dear [CREDIT REPRESENTATIVE NAME],

Our store has been purchasing regularly from you for [LENGTH OF TIME], and as we streamline our systems and improve our bookkeeping practices, we'd like to set up our account with you on a terms basis instead of continuing as a prepaid account. Our account number is [ACCOUNT NUMBER].

I have attached our credit sheet to assist with this, which includes contact information for invoices, statements, and other correspondence related to our account. Could you please let us know what else you need to set this up?

Thank you!

you will have the paper trail (literally or electronically) to call them, in a polite way, to account. If you have a good system for reporting problems and tracking the fixes, it will pay off and save you time.

Vendor files are not meant to be saved for five years or more, rather, these are active, working files that are in process. Once you've completed the process, whether it's entering the invoice into your accounting software for payment, receiving the credit memo for the damage claim, or updating the remittance address for that publisher, this paperwork can generally get shredded or deleted. If you work electronically only, it's a simple matter of emptying the folder into your trash.

If you struggle with organization or document chaos, use the "Checklist of Files to Have Handy" in the Digging Deeper section at the end of this chapter.

### 3.2.6 DAMAGE CLAIMS & CREDITS

Damaged books and shortages are a fact of life, unfortunately. The key to handling them gracefully is setting up a system. The first step is to create an easily accessible cheat sheet in your organizer of choice for how each of your vendors prefers you make damage claims, whether it's by email, through iPage, through Batch, through their own customer portal or hub, or on the phone.

Next, set up a regular place and procedure for reporting damages and shortages, preferably on a daily or weekly basis so the stack doesn't grow too daunting.

Organize your damages in piles by vendor, with invoices, so you can process them for each vendor all at once. It's fine to report damages from multiple shipments or invoices in a single email, as long as you provide the necessary information for each damaged book. Mark on your invoices which title was damaged so it will be easy to match up later with the credit memo when it arrives. When making the damage claim, you will need to provide your store account number, the invoice number, the title and ISBN of the damaged book(s), and a short description of the damage.

At the same time, you'll want to report whether you want no-charge replacements for the damaged items, or if you want credit memos issued and to reorder at your own convenience. This is a matter of preference. t does seem easier, procedurally, to get credit memos consistently and reorder the damaged books if necessary with your next restock order. Another reason to get credit memos instead of replacements is to avoid the replacements also getting damaged.

Occasionally, if the damages are significant or if they suspect that carrier mishandling caused the damages, vendors will require you to return the damaged books using a "call tag," which is a shipping label, usually for UPS, and they won't issue the damage credit until they receive the book(s). In this case, you'll have to repack the damages, print out

the label they send you, and apply the label to the package, or keep the box packed and ready for the label the delivery person will bring with them.

Make sure to keep a copy of the call tag along with the original invoice with damages marked and a copy of the damage report in a special file until the credit memo arrives.

If you get a shipment with the box badly damaged, or that has been repacked in any way by the carrier, or with other suspect handling, take photos of it before you open it or unpack it, because your vendor may want that documentation. If the box is bigger than necessary and contains only a couple of books and no packing paper or a token air pillow, you may want to document that with a photo as well.

Once you've made the damage reports, you can set up a file, physically or virtually, for tracking the damage claims to make sure that the credits issued come through and match up correctly with your original claim.

It is fine to not pay an invoice that has a damage on it until the credit memo for that damage arrives, even if it was one book out of a 15 box order. Sometimes the number of damages can be substantial, enough so that if you don't follow through on making the claims and watching for the accurate credits, you would lose a fair amount of money.

You will also need to decide how you want to handle the damaged book(s) during your receiving process, as there are implications for your accounts payable, inventory value, and liabilities. It doesn't have to be complicated. Never request replacements so you don't have to deal with a new invoice number or an invoice for zero dollars arriving with a shipment. Never receive damaged inventory so it is never in your system. Finally, don't pay the invoice until you have the matching credit memo to go with it.

Credit memos are issued to bookstores by publisher and wholesale vendors for various reasons, such as in response to a damage claim or shortage, overstock returns, and automatic co-op or other various kinds of co-op claims. Credits will show up on your monthly statement just like invoices. A credit memo will clearly state that it is a billing adjustment or a credit. When you enter these into your accounting software, be careful that they're recorded as vendor credit and not as an invoice. The process is the same, and it can be easy to accidentally enter a credit as an invoice if you're not paying attention.

Getting credits applied correctly means indicating in your remittance information which credit memos you are using along with which invoices you are paying, then tracking credits in exactly the same way you track invoices, either in your accounting software, on Batch, in a spreadsheet, or on the vendor's monthly statement. Just like invoices, you could receive credit memos through email, snail mail, the vendor portal, and/or on Batch. Some vendors who aren't on Batch will automatically apply credits to your account; however, we find it much easier to not have credits automatically applied.

It's fine to say no if the vendor asks. This is a setting on your account that your credit representative can make according to your preference.

When cash flow is tight it can be worth it to do an overstock return for credit to the publisher you need to pay. Once the return is packed up and on the way, you can usually get a "return in transit" (RIT) deduction for the value of the return if you let your credit representative know and send them a copy of the return memo and tracking information for the shipment. Basically the return in transit deduction is a notation on your account of the amount that you're going to be credited once everything is processed. That can help keep you out of trouble if you're over your credit limit, late with payment, or need a holding order to be released for an event.

## 3.3 DEBT & TAX MANAGEMENT

Knowing how debt and taxes work are key parts of owning or managing a business. Understanding and managing debt and taxes takes flexibility and planning. Although tax reporting and ensuring payments may seem like low level tasks, they are important and demand the concentration and focus of ownership or key management. Missing tax deadlines can have serious impacts on your store.

Debt can play an important role in growing your business. As a broad concept, using debt is called leverage.

### SAMPLE EMAIL TO REPORT DAMAGES

I'm reaching out on behalf of [BOOKSTORE] to report a damaged item from a recent shipment. Below, I have listed the invoice #, ISBN, title, quantity, and a brief description of the damage.

**Account:** [ACCOUNT NUMBER]
**Invoice:** [INVOICE NUMBER]
[ISBN] - [TITLE] - [QUANTITY]
**Damage:** Back cover is bent at both the outer upper and lower corners.

This damage is not surprising given that the books were (choose 1):
__X__ in too large a box, loosely packed, with no packing material around the books to mitigate damage during shipment.
_____ packed tightly in a flimsy box with no cushioning to prevent corners, edges, and spines from being damaged.
_____ packed in such a way that heavier items on top crushed more fragile items underneath.
_____other problem, describe here:_____________

If you could share this packaging feedback with the appropriate shipping manager, we would appreciate it. We request to receive a credit for these damaged items, and we will reorder at our convenience. To expedite payment, please send itemized digital credit memos, call tags, or questions to this email address or paper itemized credit memos to: [STORE ADDRESS] so we can process and pay the invoice. Thank you!

**Leverage** is an investment strategy of using borrowed money to increase the potential return on investment. Utilizing debt can also help your store manage cash flow during low profitability periods when you may need to build inventory.

## 3.3.1 HOW TO BUILD BUSINESS CREDIT

**Business credit** is a business's ability to borrow funds, which depends on many factors. Building business credit is important because it helps keep business and personal finances separate. Over time, creating spending power and having access to funding is an excellent financial planning tool. The longer the store is in business and paying its debts punctually, the more opportunities for financing at competitive rates.

Paying the store's bills – vendors, loans, tax authorities, etc. – on time and consistently is the key to building good business credit. That sounds easy when there are ample funds in the bank. It may take slow, steady progress over several years to get to where paying bills isn't a "rob Peter to pay Paul" situation.

Start with knowing the balances owed, to whom, and by when. Set up calendar reminders and email notifications, build a spreadsheet, and set time aside at the beginning of each week to plan that week's payments. Figure out a process that works for your store and stick with it.

One thing stores should have to help create vendor accounts and build business credit is a credit sheet, which saves time and makes the account creation process much easier. A credit sheet should include information generally found in credit applications, like legal business name and contact information, number of years in business, owner/partner names, addresses, and contact information, accounts payable contact name, number, and email address, one bank reference, and three trade references (vendors you've ordered from and paid the bills on time).

Along with having an updated Credit Sheet, getting a **Data Universal Number System (DUNS) number** from Dun & Bradstreet is a good idea. DUNS numbers are used by lenders and potential business partners to help determine the reliability and financial stability of the business they are considering working with. The greatest benefit of a DUNS number for your store is that anyone seeking to better understand your business credit history and credit worthiness will likely look to Dun & Bradstreet to find this information.

Likely, many of your vendors and lenders are reporting to Dun & Bradstreet about their payment history with your store. Dun & Bradstreet also offers guidance on how to build business credit.

Besides Dun & Bradstreet, there are other companies that seek to assist small businesses with establishing credit or maintaining a good credit standing, but Dun & Bradstreet is the gold standard. Sign up with them if you haven't already done so.

## 3.3.2 HOW DEBT CAN BE BENEFICIAL

Debt can be scary and potentially risky, but if well planned and executed, it can be beneficial and help transform your store. While unaffordable financial obligations or debts that offer no long-term benefits could hurt your store, good and responsibly managed debt will help you reach your goals, and as mentioned above, build credit.

Financing beyond startup is important because you need access to cash to ensure employees get paid and that taxes and vendors are paid on time. Liquidity is essential to run a bookstore. Sometimes you may need to borrow, and there are a plethora of traditional and nontraditional financing options for you to do so.

## 3.3.3 FINANCING OPTIONS

First and foremost, getting terms from your vendors is the first step in building credit and financing purchases over time. There are also traditional and nontraditional financing options.

### Traditional Financing Options

Having a **line of credit** is a traditional way for a business to have access to cash. With a line of credit, you can take money from it when you need cash, then pay it down when your cash flow gets better, much like a credit card, but generally with less interest. Bookstores may draw from their line of credit in August to early November, when you're building up inventory for the holidays and are less profitable, then pay it off after holiday season when you're flush with cash. You should apply for a line of credit *before* you actually need it so you have it available when you *do* need it.

Negotiating the terms of the line and trying to get a multiple year deal with a bank is always a good idea. Often, banks who are willing to give you a line of credit at a good rate will also want you to have your operating accounts with them, so choose wisely. Find a banker you feel you can trust and who will treat you and your business as an important part of their customer base. Monthly payments for most lines of credit are interest only, and generally, you need to be at a zero balance for at least 30 days per year, so if you need cash year round, you may want to consider getting a **fixed term loan** instead.

Fixed term loans are often designed for projects that you don't want taking up cash resources that you need to operate day-to-day, like expanding or remodeling. A term loan is generally more permanent than a line of credit, where you pay it off through a series of fixed payments. If you are considering a term loan, you will want to do a projection of your cash flow to see if you can make the payments based on the options the bank gives you.

Some term loans may require amortizing over the repayment period. For example, let's say you borrow $10,000 for three years. If the loan is fully amortized, it means you will pay a fixed payment that includes principal and interest each month until the balance is paid over the three years, so at least $277.78 per

month in principal alone. Some term loans may allow for a smaller monthly payment, but then have a balloon (lump sum) payment at the end. The upside of having a balloon payment is that you will have smaller monthly payments, but the downside is that you need to ensure you have a way to pay off the balloon payment at the end.

How do you know how much you need in a line of credit or term loan? Until you know your cash rhythm, it may be hard to figure out, but if you project your income and expenses in a budget (covered in Chapter 12) and know how much you need to build inventory over time, you can estimate your cash needs to ensure you will have enough. Looking at historical data helps with making projections, and proper accounting and bookkeeping is basically the financial history of your business.

## Nontraditional Financing Options

Besides traditional financing options, many bookstores have had success with a variety of nontraditional financing to meet store needs.

Merchant loans have become popular in recent years. These loans are offered when the company proposing the loan deems your business is eligible, and there is no need to apply.

Let's look at Square Loans as an example of how merchant loans typically work. Many small businesses that utilize Square for credit card sales also take advantage of Square Loans as a source of easy access to capital. A minimum of $10,000 in annual sales is required to access this funding source. Other factors contributing to the loan amount determined by Square include sales volume increasing over time, account history with Square, and a mix of both new and returning customers.

With merchant loans, payments are automatically deducted from credit card sales. Square loans are for an 18-month period, with a minimum payment of 1/18 of the loan every 60 days. That means if a business only makes the minimum payment, half the loan amount will be due at the end of 18 months in a balloon payment. If you take this financing option, you will need to plan on where the money will come from to pay off that balloon amount in the case you don't have enough credit card sales to cover it. Conversely, you could pay 1/9 of the loan amount every 60 days and have no balloon amount due. As with other types of financing, planning out repayment strategies for merchant loans is important.

While Square doesn't charge an interest rate on the loan, they do charge a fee that is typically a factor of 1.1 to 1.16 of the loan amount. For a $5,000 loan, that fee would range from $500 to $800, or 10% to 16% of the loan amount. That is quite a high percentage compared to typical financial institutions, even with an 18-month term.

Crowdfunding continues to be a popular way for individuals and businesses to raise funds by harnessing the power of social networks and the internet.

Kickstarter and GoFundMe are two of the biggest players in this arena. Both have excellent websites explaining how crowdfunding works and tips for building a successful campaign. Most crowdfunding is donation-based, meaning the donors may receive some prizes and/or recognition for their contribution, but the funds collected are not paid back. Equity-based crowdfunding results in contributors receiving shares of the company. There is also debt-based crowdfunding, where contributors are paid back at some time in the future, plus interest.

There may also be grant opportunities for bookstores, even as for-profit entities. There are often grants available for women- or minority-owned businesses. Most of these involve some sort of application process. Amber Grants, Visa's She's Next, Accion, and FedEx are just a few of the organizations that provide grants to small businesses. You have to do the research and make time for the application process, and it is typically highly competitive.

There may also be grants available through city redevelopment funds or local business districts. One example could be getting local funds to cover the cost of a mural on the side of your building that enhances the look of the building and markets your store.

Over the past five to ten years, there have been quite a few bookstores that have created nonprofit organizations to further the mission and community outreach of their stores. RJ Julia Booksellers started a nonprofit called Read to Grow, an organization that promotes literacy in their community.

As a nonprofit organization, there are many more donor and grant options for funding your mission that may provide ancillary support for your store. If you want to pursue starting a nonprofit, work with your tax advisor, as it is not a simple process.

### 3.3.4 KEEPING TRACK OF OUTSTANDING BALANCES

One of the many important things to keep track of financially is what you owe to whom and when it is due. Being able to access that information easily and regularly re-prioritize payments to keep as many vendors happy as possible should be an ongoing part of your financial work.

Credit cards can be an easy way to purchase inventory and pay for a variety of operating expenses. Keep in mind that you will likely need to provide personal financial information and perhaps a personal guarantee when you open your first credit card for the store.

With your credit card or cards, two things to know are your credit limits and the timing of your statement cutoff. When you first open business credit card accounts, you may feel your credit limit is low. It takes time to raise your limits.

Use only a portion of your credit limit - 30% seems to be the most commonly recommended amount - and pay off the balance due every month.

If you do these things, over time you will likely get a higher credit limit.

If not, or if you see a need for more monthly spending using that account, call customer service and ask for an increase.

With credit cards, it's also important to know your statement cutoff, as you can plan cash flow by waiting to charge certain purchases until the day after the statement cutoff. Then it ends up being close to Net 60 terms. Conversely, charge purchases right before the statement cutoff, and you will owe within 30 days. If you manage the timing of your purchases so you have longer to pay, it can really help cash flow. Another tip: if you're sure you'll have the funds to cover it, link your credit card payments to your checking account so the bill is always paid by the due date. You could also set up reminders to pay a fourth of the total bill each week so it's paid off in full by the end of the month.

Make sure you review your monthly credit card statements in a timely manner. You may find it helpful to set up email notifications for your credit card accounts so you know when to go online and print the statements. You would then reconcile the statement against what was recorded in your accounting software. If you find any charges not in your accounting system, first verify they are valid charges (find the receipt), then enter them into your accounting system.

If you have outstanding business loans, setting up email notifications for payment due dates and when copies of statements are available is also helpful.

Many lenders require loans to be paid automatically from your checking account to ensure payments are timely. Know the date that money is taken out and make sure you have the funds in your checking account at the right time to cover the payment. For any outstanding loans, you should have an amortization schedule that provides monthly payment information along with the breakdown between principal payments and interest. You may need to ask your bank for the amortization schedule.

Tracking overall payments is part of cash flow planning, and tracking interest is part your budget/expense planning. In the "Templates & Resources" section at the end of this chapter are two sample amortization schedules (loan calculators) that you can use to plug in debt options, and the principal and interest are broken down for you. There are many templates in Excel besides these two, as well as online tools for creating amortization schedules.

During the early years with tight cash balances, credit card balance transfers can move outstanding balances to new cards with zero interest rate on the balance transfer for a period of time. This can save a lot of money on monthly interest charges. When you apply for a new credit card, read the fine print and understand the 0% interest rate period and whether there is a balance transfer fee. Those fees are typically 3-5% of the balance transfer, but in many cases that is waived when banks are aggressively recruiting new accounts.

Plan to pay off the balance transfer before interest charges start, and you have saved some money. Another option for high credit card balances is to convert them into a fixed term loan, meaning you take out a term loan with your bank to cover the amount charged up on the credit card, then pay off the card with the money from the loan. This allows you to pay off the amount with a fixed monthly payment and much lower interest than leaving the balance on the credit card.

At some point, the store may generate enough cash flow that you build up cash reserves that could be used to pay off some or all of your existing debt. Certainly pay off loans with the highest interest rates first. It may make sense to pay off all your debt, but it may also make sense to keep some debt with favorable terms. Before making early debt payments, talk with your lenders and determine whether if loans are paid off, there could be a line of credit put in place for seasonal borrowing needs.

## 3.3.5 TYPICAL BUSINESS TAXES

Paying and reporting to the various tax authorities is a critical task, as not doing so could result in penalties, interest, and the threat of doors being closed. These obligations need to be paid on or before due dates, and any notifications of missed payments dealt with in a timely manner.

### Sales Tax

Most states require businesses to collect and remit sales taxes on a variety of items. Every state has specific rules related to the collection and remittance of sales tax. When you requested and secured your Reseller Sales Tax Permit from your state, the requirements for reporting and remitting sales tax would have been clarified at that time.

Most states require monthly sales tax reporting and remittance and have a state tax website with a secure login to process monthly sales tax reporting and remit funds via ACH. The sales tax report in your point of sale system should include a breakdown of non-taxable sales as well as taxable sales, which is important, as you don't want to pay any more sales tax than you actually owe.

### Business Property Tax

Although business property taxes vary from city to city, county to county, and state to state, you should be aware of any business property taxes that may be required for your store. Generally speaking, there are two types of business property:

1) "Real" property, which is generally considered land and buildings, and
2) "Business personal property," which may include furniture, fixtures, equipment, and in some places, inventory.

Business property taxes can really add up, so it is a good idea to maintain good records of your furniture, fixtures, equipment, and leasehold improvements and ensure that when you get rid of assets, you remove the item(s) from your records so you don't continue to pay property taxes on them.

### Income Tax

Business income is taxed a variety of different ways depending on the tax structure of the business. Hopefully, while setting up your store, you worked with a tax professional or attorney who explained the pros and cons of the various ways to structure a business from both a tax and a liability perspective.

All businesses except partnerships must file an annual income tax return. Partnerships file an information return with financial information included on a Schedule K-1, which indicates the income or loss passed through to the owner or owner's personal tax return.

#### EXAMPLE #1: C CORP

A.C. Vroman Inc. (doing business as Vroman's, Book Soup, and The 1894) is a C Corporation. The company files a federal and state income tax return, and taxes owed are paid directly by the business, not by the owners. When they pay dividends to shareholders, that income is taxed on an individual basis to the shareholders that receive the dividends.

#### EXAMPLE #2: S CORP

The Well-Read Moose is an S Corporation, which files federal and state income tax returns. This type of corporation is similar to partnerships, where the owner receives a K-1 from the S Corp for their personal tax return. Taxes due are generally paid by the owner, but ask your accountant what the options are in your state.

#### EXAMPLE #3: SOLE PROPRIETOR

Single-member limited liability companies (or LLCs) are typically treated the same as sole proprietorships for income tax purposes. Business income and expenses are reported on the Schedule C for individual tax returns. Single member LLCs can elect C Corp or S Corp tax treatment, which makes this type of entity flexible on how income taxes are paid.

For both single-member LLCs and sole proprietorships, there is the risk of commingling business and personal expenses. Good recordkeeping is critical to ensure you capture eligible business expenses.

Single-member LLCs and sole proprietorships must also be aware of tax cliffs, where a small increase in income can trigger a higher tax bracket or reduction or elimination of certain tax deductions on the owner's personal tax return.

It makes sense to talk with your tax preparer annually to understand any changes in the tax law that could result in a bigger tax payment in the years ahead. On the plus side of the ledger, sole proprietor businesses may be able to deduct home office expenses on their Schedule C. That can be a wonderful deduction, but there are many rules, so please work with your tax advisor to avoid pitfalls and audits, no matter your business structure.

### Local Tax

Local taxes are also something that each store may need to deal with. You might pay a business license fee based on the average number of employees, or alternatively, pay business tax based on sales. If your store has a coffee shop or wine bar, you may also be subject to other taxes or fees. For example, Vroman's is required to have two health permits for its flagship store - one permit for the sundries (packaged candy and drinks) sold at the newsstand and one for the wine bar. They are also required to pay annual fees for maintaining their liquor license for their wine bar.

In summary, keep in mind that each city, county, and state may have taxes or fees that you need to keep track of and report and/or remit for. Things are constantly evolving and changing, so as an owner or manager of a store, keep an eye and ear out for changes so you can remain compliant.

## 3.3.6 TAX FILING & REPORTING

Most of the tax authorities have pretty useful websites besides a place to collect online payments. Setting up user IDs and passwords that you store in a safe place will give you access to filing requirements and due dates. You may find it useful to become familiar with the IRS Electronic Federal Tax Payment System (EFTPS) for tax reporting and payment and your state tax sites for sales taxes, withholding, and unemployment reporting and payment. Make sure you are on the actual governmental sites when you are looking for information, as some websites that may look like experts will show inconsistencies on tax deadlines. Even QuickBooks may be off, so ensure your information comes directly from government websites.

In the “Templates & Resources” section is a template tax calendar. Federal deadlines are applicable to everyone, but state deadlines are unique for each state. You can work with this document to plug in the deadlines that are applicable for your store. You can also use this tool for other non-tax reporting deadlines, like the ABACUS due date.

The key takeaway with taxes is to research, document, and schedule and to keep your procedures simple.

## SUMMARY

**Why It Matters**

Developing systems for handling vendor finances and paperwork will create efficiencies. Building relationships with your credit representatives will give you the goodwill you need to get through tough times. Knowing how debt and taxes work are also key parts of owning or managing a business. Missing tax deadlines can have serious impacts on your store. Utilizing debt can help your store manage cash flow during low profitability periods when you may need to build inventory.

**3.1 The Basics**

Vendor, Debt, and Tax Management are crucial to running your business. Developing systems for handling the paperwork and finances surrounding vendors, debt, and taxes will create efficiencies that make the day-to-day finances much easier.

**3.2 Vendor Management**

The first step to managing vendor finances is the establishment of **terms accounts**. Setting up accounts with vendors is an important step to minimizing your **Cost of Goods Sold**. Terms also allow you to maximize cash flow, give you flexibility, and build business credit.

Building relationships with credit representatives and communicating with them appropriately is important to ensure you're taken care of during tough times, you have the most up-to-date account status, and you have leverage with damages and shortages when you need it.

We recommend using invoices when receiving to ensure you have all the correct information to enter into your point of sale system. This also allows you to catch any invoicing errors during receiving. Paying invoices from your accounting system also prevents duplicate invoice payments, produces accurate profit & loss and balance sheet reports, tracks invoice due dates so you can use your terms to the max, and makes it easy to issue payment for many invoices at once.

Choose one day per week or two days per month to handle invoice payments. Organize the invoices that have been approved for payment first by vendor then by date, then group the invoices into payment methods: ACH, Batch, paper check, etc. Pay your main suppliers first, and at the least, make partial payments if you cannot pay in full. If you cannot pay a balance due in full, communicate this immediately to your credit representative, along with how much, how soon, and how often your partial payments will be.

Set up a regular place and procedure for reporting damages and shortages, preferably on a daily or weekly basis.

### 3.3 Debt & Tax Management

Debt can play an important role in growing your business. As a broad concept, using debt is called leverage. **Leverage** is an investment strategy of using borrowed money to increase the potential return on investment. Utilizing debt can also help your store manage cash flow during low profitability periods when you may need to build inventory.

**Business credit** is a business's ability to borrow funds, which depends on many factors. Building business credit is important because it helps keep business and personal finances separate.

Financing beyond startup is important because you need access to cash to ensure employees get paid and that taxes and vendors are paid on time.

**Traditional Financing Options:**

- With a **line of credit**, you can take money from it when you need cash, then pay it down when your cash flow gets better, much like a credit card, but generally with less interest.
- **Fixed term loans** are generally more permanent than a line of credit, where you pay it off over time through a series of fixed payments.

**Nontraditional Financing Options:**

- Merchant loans may be available, such as Square or Quickbooks loans. These allow you to borrow against future sales and may require a balloon payment at the end.
- Crowdfunding through sites like Kickstarter or GoFundMe are options many stores use.
- There may be small business grant opportunities available through certain corporations and programs, city funds, local business districts, or if you start a nonprofit arm of your store.

One of the many important things to keep track of financially is what you owe to whom and when it is due. Make sure you review your monthly credit card statements in a timely manner. You may find it helpful to set up email notifications for your credit card accounts so you know when to go online and print the statements. You would then reconcile the statement against what was recorded in your accounting software. If you find any charges not in your accounting system, first verify they are valid charges (find the receipt), then enter them into your accounting system. If you have outstanding business loans, setting up email notifications for payment due dates and when copies of statements are available is also helpful.

Business taxes include sales tax, business property tax, income tax, and local tax. Make sure you are on the actual governmental sites when you are looking for information, as some websites that may look like experts will show inconsistencies on tax deadlines. Use a tax calendar to ensure you make payments in a timely manner.

## KEY TAKEAWAYS

- Establish terms with publishers and other key vendors.
- Set up procedures and a workflow for vendor payment processing.
- Utilizing debt can help your store manage cash flow during low profitability periods.
- Building business credit helps with financial planning.
- Set up calendar/reminders for tax reporting and payment deadlines.
- Research, document, schedule, and keep procedures simple.

## TEMPLATES & RESOURCES

- **Video**: Batch for Books Overview with Nathan Halter from Batch
- **Resource**: Loan Payment Calculator – Balloon Loan
- **Resource**: Loan Payment Calculator – Fully Amortized
- **Template**: Tax Payment Calendar

## KEY TERMS

- Batch for Books
- Business Credit
- Cost of Goods Sold
- Data Universal Number System (DUNS) number
- Fixed Term Loan
- Leverage
- Line of Credit
- Prepaid Account
- Productive Debt
- Terms Account

## REVIEW QUESTIONS

**True or False**:

- Having terms accounts with vendors is not beneficial in any way.
- A line of credit ideally should be obtained when you don't need it.
- Not remitting sales tax payments in a timely manner has no ramifications.
- Debt is not beneficial, and you should avoid it at all costs.

## ANSWER KEY

- FALSE
- TRUE
- FALSE
- FALSE

## DIG DEEPER

## VENDOR MANAGEMENT: CHECKLIST OF FILES TO HAVE HANDY

The following are items you will handle all the time, so you need to have a place to keep them. They can be electronic or physical depending on your systems and preferences.

### ☐ Invoices

- File for invoices for shipments that have been received and are ready to be paid.
- Have receivers initial and date the invoice in case you have a question.
- Include Ingram and other wholesalers. You should train your receivers to go into the master inventory record for any received book that has a short discount and make sure it is marked as “no discount” so your loyalty discount won’t kick in on those titles and make you lose money. Then have them circle the discount on the Ingram list so you can see at a glance that the “no discount” procedure was followed.
- Once you’ve approved an invoice for payment, you can enter it into your software, mark it as VERIFIED in Batch when applicable, and for the rest, move into the file you use for items that are going to your bookkeeper.

### ☐ Packing Slips

- File for packing slips awaiting a matching invoice.
- While we generally do not recommend receiving from packing slips because they often don’t include shipping charges or special promotion discounts, if you do sometimes receive from a packing slip, put it in this file until you receive the official matching invoice.
- Double check to ensure all your invoice information is correct in your point of sale receiving batch for that shipment. If it’s not correct, fix it and have your POS recalculate the cost of goods sold for that batch.

### ☐ Statements, Etc.

- File for vendor statements and other financial statements from the bank, credit card company, state tax authority, overdraft notices, and other financial notices like credit card chargebacks.

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## ☐ Credit Memos

- File for incoming credit memos from email and snail mail, waiting to be matched up with the original invoice that had damages, which is either with the damaged books on a special bookshelf for damages, or in a special file for DAMAGES.
- Once the credit memo is received and matched up with original invoice, it can go in the INVOICES file to be approved for payment.

## ☐ Damages

- File for original invoices that had damages on them for which you have submitted a claim and are awaiting the credit memo.
- It's generally helpful to keep the original invoice with the damaged book(s) themselves, but certain vendors like to have you return the books with a call tag that they provide. Those original invoices could be kept in this DAMAGES file with a copy of the call tag until the credit memo arrives.
- When the credit memo arrives and is matched up with original invoice, it can go in the INVOICES files to be paid.

## ☐ Co-Op Claims

- File for co-op claims waiting to be matched up with incoming co-op credit memos.
- If something sits for too long, you can follow up with vendor.

## ☐ Return Memos

- File for copies of overstock return memos and label/tracking info for the return that are waiting to be matched up with return credit memo.

## ☐ Accounts Receivable NYP

- File for copies of account sale invoices for school, library, B2B, and other customers which have not yet been paid. The customer should also receive a copy of the invoice.
- Can follow up with the customer after 30 days to inquire on the status of payment.

## DIG DEEPER

### ☐ Accounts Receivable PAID

- File for the same account sale invoices from the above folder, with attached "Pay In" receipt from the cash register, check stub, or other record of payment, moved from NYP once they're paid by the customer.

### ☐ Monthly Reports

- File for all your monthly reports. Some monthly reports are time sensitive and must be run on a particular day no matter what. If you train staff to do this, have them put the reports in this file so they'll be ready when you do your bookkeeping.

### ☐ Records to Update

- File for update notices from vendors. Publishers send updates to their imprints and distribution clients all the time, usually included with invoices or statements, so place those notices here until you have time to deal with the updates in your accounting software, your POS, or wherever you keep vendor information.
- Publishers sometimes have information on your store incorrect and you need to notify them, so place those incorrect things here to remind you to contact the vendor later.

## DEBT & TAX MANAGEMENT: BANKING RELATIONSHIPS

If you are an owner, it is likely you opened a bank account when you started or acquired your store. If you are a manager or bookkeeper, at least one bank account was already set up, and you may or may not have been involved. Either way, you probably haven't spent too much time thinking much about the bank besides their hours and where their location is so you can make deposits. But having a good relationship with your bank is critical. Ideally, you want to build a relationship with your bank and your banker so the bank will value your business.

First, what type of account or accounts do you need? Each store operation is different, and you need to figure out what works best for you.

One important thing to consider when deciding on bank accounts is how bank fees work. Depending on your volume and size, there may be traditional fees for having an account or fees related to volume, but some business banks may offer to put your bank fees through analysis. Analysis allows your fees to be reduced by any earning credit the bank may provide for your balances. Keep in mind that bank fees may vary from bank to bank and can be negotiable.

Banks can also offer a variety of services that may help create efficiencies. For example, if you need change on a regular basis (every Monday, you need $100 in ones for the register), perhaps you can set up a recurring change order with your bank. Do you want to do mobile deposit with checks? Your bank may have ways to do that to save you time. Do you have multiple accounts and want the money rolled up into a main account each night? Do you want online banking? Of course you do, but online banking may also lead to setting up ACH or tax payment services through your bank. Do you need the ability to transfer funds between accounts? Do you want the bank to help with fraud prevention? Do you want to do stop payments online? Banking has continued to evolve, so it is good to find out about services your bank provides, how those services match your needs, and what they cost.

If you use online banking, it is a good idea to have separate logins for different people who are accessing your account(s). You want to ensure that access is restricted to limit internal theft.

## DIG DEEPER

If you have loans with a bank, make sure you know the loan covenants. **Loan covenants** are things you are required to provide periodically to keep the loan in compliance. This could be a certificate of insurance or annual financial statements, or it could be that it requires you to do an annual inventory. The more proactive you are on a regular basis, the more likely your bank knows you and may be more inclined to work with you if cash flow challenges arise.

### Lunch With Your Banker

Your banker should be your key contact at your bank. You should get to know them, and they should get to know you. Have them on your mailing list, ask them to check out your social media, and try to get them vested in your store. Send them a coupon at the holidays to shop at your store.

You should meet with your banker at least once a year face-to-face. Get them to take you to lunch or coffee so you can talk about your business, the things going right, and the things you want them to help you with. Use them as a resource.

Provide a copy of the store's most recent financials and plan to discuss how the store is doing and any industry data that you think would be useful and interesting for them to know. Have a list of questions for them as well, including:

- Whether the bank is growing – both in lending provided and new deposits.
- Any regional or national economic forecasts and what they are seeing in the local economy with other small businesses.
- Their lending environment. Are they looking to grow their loan portfolio and if so, what types of loans are they looking to fund? Those will likely have the most favorable terms.
- Services they provide or partner with third parties for – credit card processing and ACH payments are a couple areas to inquire about. They may be able to get you a better deal for the store.
- What are ways to reduce and/or eliminate fees? If you are monitoring your fees, have they been going up? If so, how and why?
- If you have a loan or want a loan, talk about loan covenants and how to make them better for you. Often they will want collateral or personal guarantees, so talk about ways to limit those.

## DIG DEEPER

- Ask for things even if you think what you want is unlikely to happen. It shows you are thinking about the best solutions for your store and that you are a savvy business owner or manager.
- Lastly, ask what charitable activities they support in your community and ask them to consider partnering on a book drive to donate books to a local charity. A win-win!

## TAX MANAGEMENT: OTHER REQUIRED TAX REPORTING

Besides the tax reporting mentioned in this chapter, there are many other reporting requirements depending on the size of your store. Outlined below are descriptions of other reporting that you should be aware of. Plan accordingly!

**Form 1099** is one of several IRS tax forms used in the United States to prepare and file an information return to report various types of income other than wages, salaries, and tips. The term “information return” is used in contrast to the term “tax return,” although the latter term is sometimes used colloquially to describe both kinds of returns. Form 1099 is used to report payments to independent contractors, rental property income, income from interest and dividends, sales proceeds, and other miscellaneous income. This has led to the phrases "1099 workers" and "the 1099 economy" to refer to those whose income is reported on Form 1099, in contrast to a "W-2 employee" who receives Form W-2.

There are many different types and requirements for 1099 reporting. Copies of 1099’s are generally sent to the person you paid in addition to a copy to the IRS. Depending on the number of 1099’s you need to prepare, you may need to e-file the forms with the IRS. Please check on those requirements, which can change every year.

**Form W-9** is an IRS form that is used to obtain a company’s information. Generally you would want to get this from new vendors so you can determine if you may need to issue a 1099 to them. The recommendation is to ask all vendors (except inventory vendors) for a W-9 before you pay them. Then you can mark their tax ID and entity type in your accounting system for potential future reporting.

**Garnishments** are generally issued by a federal or state agency to levy money that you owe to employees or vendors. Garnishments are normally obligatory and require you to notify the vendor or employee and promptly start deducting monies from your remittance to them and turn it over to the taxing authority.

## DIG DEEPER

The U.S. Census Bureau may also from time to time send **information requests** that may or may not be mandatory. If you get a request, the best thing to do is to determine if it is mandatory or optional. Once you know that, you can then determine how willing you are to find the information and report on it.

The Department of Labor may also require you to send information on **number of full-time employees (FTEs)** and information regarding **worker's compensation claims**. Similar to the U.S. Census Bureau, determine if these are optional or mandatory before reporting.

**EEO-1** is demographic reporting for private employers with more than 100 employees (or a federal contractor with 50 or more employees). The reporting can be time consuming, but is annual and requires you to track demographics of your employees. Although this likely doesn't affect most bookstores, it is good for you to be aware of it in case the minimum reporting requirement changes or your store grows.

**Forms 1094 & 1095** are informational reporting requirements from the IRS for employers with 50 or more full time employees (including full time equivalents). The 1095 form is required to report information about each employee related to benefits eligibility and acceptance. The 1094 form is a summary of 1095 forms. Although again, this likely does not affect most bookstores, you should be aware of it because the minimum reporting could always change or your store could grow.

*Chapter 4*

# Working With ABACUS

## LEARNING OUTCOMES

By the end of this class, you will be able to:

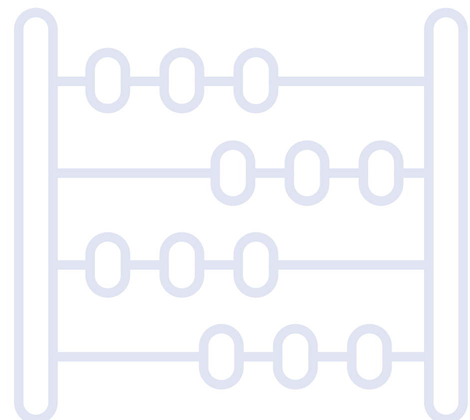
- Successfully complete the annual ABACUS survey released by the American Booksellers Association (ABA).

## WHY THIS MATTERS

**ABACUS**, which gets its name from the ancient Chinese counting tool, is an annual survey in which bookstores report financial information to the American Booksellers Association (ABA). ABACUS is our industry's best tool for analyzing stores' financial performance, and it's completely free. It provides baseline metrics to help you compare your store to industry averages, so it requires group participation to work. The more stores that participate, the better the comparative data. It benefits independent bookstores, the publishing industry as a whole, and the ABA staff members who work on behalf of independent bookstores lobbying with publishers, legislators, vendors, and others.

## CHAPTER OUTLINE

**4.1** The Basics
**4.2** How ABACUS Comparisons Help
**4.3** Where to Find Data for ABACUS
**4.4** Tips & Tricks for Submitting ABACUS
**4.5** Using ABACUS to Create More Profit
**4.6** Using ABACUS to Investigate Expenses
**4.7** Using ABACUS to Determine Store Viability
**4.8** Using ABACUS to Analyze Your Buying
**4.9** ABACUS as a Financial Dashboard
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Taking Action from Your ABACUS Company Report
**Dig Deeper**: New Bookstore Burning Questions



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## 4.1 THE BASICS

During the annual ABACUS survey, bookstores report financial information to the American Booksellers Association (ABA), including relevant data such as size of store, number of employees, and business model, and environment, such as a small town or urban setting. The ABA takes the information and turns it into a useful industry report with various filters, charts, and graphs for measuring and comparing, and provides everyone who participates with a personalized report. ABACUS is our industry's best tool for analyzing stores' financial performance.

ABACUS gives us baseline industry metrics, which is another way of saying a system of measurement, which are useful for both new and existing stores. These baseline metrics help you compare your store to other stores so you can get a data-based idea of how you are doing. It helps those who are considering opening an independent bookstore make realistic plans and projections and those who already have stores to improve operations and hopefully become more profitable or resilient.

In the overall scheme of this course, a huge part of what you will learn will directly relate to filling out the ABACUS survey. It's not the *only* thing to care about, in terms of financial practices, but it's a great thing to become familiar with.

## 4.2 HOW ABACUS COMPARISONS HELP

ABACUS comparisons can help in several ways. Submitting financials to ABACUS helps you to be proactive in paying attention to your financial performance, looking at the different data points, and seeing where you can make a measurable difference, even if it's a small one. ABACUS breaks it down into little pieces that you can think about, and take action on, a bit at a time. It also helps you understand where your gut instincts are correct or off, set goals, and know where to focus your attention. ABACUS even gives you a "Report Card!"

Once you've gotten your report card, you can see where opportunities for improvements in your profitability may be. Where can you save money? Your lease? Labor costs? Credit card fees? Can you improve your cost of goods sold? ABACUS can also help you know where you're doing well when you see that you're ahead of industry average in a certain area.

## 4.3 WHERE TO FIND DATA FOR ABACUS

You can find the data to help you report to ABACUS from a mix of sources: the income and expenses portion of the survey comes from a report out of your accounting software called a **Profit & Loss statement**. If you're not yet using accounting software, you can pull the same information from your company tax return. Other questions may require you to run reports from your point of sale system, e-commerce website, or event ticketing platform.

Sometimes you may need to hunt to find the requested data, or if it's a new question to the survey, it may be something you've never tracked before. If so, don't let that stop you from filling in the survey, but consider how you could begin tracking that information for the next year.

It's helpful to create a cheat sheet that either contains the answers to a question if it's something unlikely to change like your city size or square footage, or where to find the answers if you have to run a specific report each year to gather data. Creating a map between your data and the ABACUS survey will save you a lot of time later.

## 4.4 TIPS & TRICKS FOR SUBMITTING ABACUS

The ABACUS survey is sent out in the summer, so unless you had to file a tax extension, you should already have the information you need to fill in the survey; however, your data may be organized differently than what ABACUS requests. The first step to making ABACUS easy is to go through the ABACUS questionnaire step-by-step and think about how to obtain the requested data.

Sometimes the data is there, but not easy to find. For example, the ABACUS survey for the 2021 fiscal year asked for the percentage of sales from children's/young adult books. If you have many children's categories in your point of sale system, you would need to combine the data for ABACUS reporting in this case. For situations like this, you may want to consider if there's an easy change you could make to save you time next year. For example, you may consolidate your categories and create a few top-level children's categories. Make sure you're mindful of what implications any changes you make to support ABACUS may have on other areas of your business.

The data for the income and expenses section will generally come from your Profit & Loss statement in your accounting software. The subcategories that show up on this report, like Utilities or Supplies, are based on how you have set up the underlying **Chart of Accounts** in your accounting software. We will do a deep dive into the Chart of Accounts in a later class, but for now, it may help if you re-organize your Chart of Accounts to support the three main ABACUS reporting categories: Payroll, Occupancy, and Operations.

Subcategories in your Chart of Accounts are an easy way to track items for ABACUS. You can leave the main category for your accountant on your Chart of Accounts for tax purposes, then create a subaccount underneath it of the portion of the data that ABACUS wants.

Until you have a better understanding of both bookkeeping and tax implications, you may want to use a written map of categories instead of changing your Chart of Accounts. Once you finish this course in its entirety, you could talk to your accountant and/or bookkeeper about any changes you'd like to make going forward.

**REAL-LIFE SCENARIO**

Jill showed her landlord the average occupancy percentage in ABACUS for profitable bookstores and what her own higher percentage was on her ABACUS company report to renegotiate her lease at a lower rate.

## 4.5 USING ABACUS TO CREATE MORE PROFIT

ABACUS is a great tool to use to wring out a little more profit. You can compare yourself to other stores in your sales bracket to see which of your expenses may be a little or a lot above average. Once you know what to concentrate on, you can usually research ways to reduce them.

Reducing expenses generates extra cash, which you can pass through to your bottom line as profit to help you pay down debt or make the store look more attractive to a buyer. Or, you may decide to use the extra money to bump up your owner compensation or purposefully pay higher-than-average wages to attract and retain staff.

When you're emailed your ABACUS company report, it comes with a colorful "Report Card;" however, that report card compares your data to the average of all stores. Because most of the report card indicators are highly correlated with sales, it may be more useful for you to first look at how you are doing compared to stores in your own sales bracket.

You can do this by going onto the ABACUS reporting website and generating your own report card, then comparing yourself to all the stores in your current sales bracket.

## 4.6 USING ABACUS TO INVESTIGATE EXPENSES

You should compare expenses to similar stores through ABACUS, look at expenses where you see considerable variance from your peers, and investigate why.

### Inventory Expense

If you run a new bookstore, inventory is your biggest expense. The IRS has specific rules about how inventory expense must be calculated for retail stores, so this figure is usually calculated by your accountant at the end of your fiscal year and is called **Cost of Goods Sold (COGS)**. COGS differs from **Purchases**, which is the actual money you pay to vendors over the course of the year. We're going to get into much more detail about Cost of Goods Sold and how to calculate it in later classes, but what is important for you to know now is that ABACUS is used by the ABA to negotiate with publishers for better terms, so the survey wants inventory expenses accounted for in specific ways that may differ slightly from what your accountant uses for tax purposes.

For those of you who have gotten a publisher co-op credit, you may have noticed that it looks very similar to an inventory return credit. Many stores lump co-op credits and returns credits together in the same category in their accounting software; however, ABACUS does not want co-op credits included in cost of goods sold. Instead, they want them listed under marketing so those credits offset your actual marketing expenses.

Return freight for books may similarly get lumped in with the postage you pay to ship out web orders. In order to report your inventory expense the way ABACUS prefers, it may not be a case of simply mapping one category to another, but figuring out how to subdivide some of your categories. Subcategories are easy to setup in accounting software, so it's more about getting into the habit of separating out the expenses and knowing why it's important.

Once you are entering COGS the way ABACUS wants, you can easily compare your store to other stores to see if your inventory expense is a higher percentage of sales than the average, which tends to be around 55%. If so, we recommend that you or your buyer take the Professional Booksellers School Inventory Management course, which is dedicated to helping you lower this biggest expense.

## Payroll Expense

The next biggest expense a store usually has is payroll, including owner compensation.

A general rule of thumb is that payroll should be around 25% of sales or less. Depending on where your store is located, though, perhaps rent is high, but you have part-time staff who don't require a living wage. In that case you may want to look at payroll and occupancy together and ensure your total for the two is in line with your peers. A maximum of 35% for both is recommended.

ABACUS also includes some employee productivity ratios that can be very useful. "Total personnel expense per full-time equivalent employee" can tell you whether you are paying your staff more or less than the average bookstore, and "net sales per full-time equivalent employee" can tell you whether your employees are performing better or worse than the average employee. Keep in mind that though this section is called "employee productivity," it includes the owner as an employee, so in smaller stores, this may skew your results. You may have to take a questionable result with a grain of salt, like in the case where you may have a great employee, but a lousy location, or perhaps your inventory is so low that employees can't sell any books - neither of which is the employee's fault.

Owner compensation can be trickier to determine than employee wages, as it can depend on the structure of your business. In the ABACUS survey, they want you to enter a fair wage for the owner's work, even if it's not actually being paid to the owner yet.

**REAL-LIFE SCENARIO**

A bookstore in South Carolina noticed that ABACUS showed her utilities as much higher than other bookstores her size. She investigated why and discovered she had a water leak!

## 4.7 USING ABACUS TO DETERMINE STORE VIABILITY

One of the most useful figures ABACUS gives us for determining long-term sustainability is owner compensation. The average across all stores is 4.4% of sales, and likely, the highest you could sustainably get to would be about 10% of sales. To calculate the sales range you would need to hit for sustainability, take your desired salary at success and divide it by .1 to get the low range and by .044 to get the high range.

For example, if you want to make a salary of $30,000, then your top-line sales need to be in a range of $300,000 to $681,818. The math will give you a broad range, but you can use it as a target.

Some owners also take most of the store's profits as part of their compensation as well, but keep in mind that profit is also needed to pay down store debts, build up cash reserves, and make capital investments such as replacing computers or growing your inventory, space, or your staff so you can grow sales. If you can afford to take some profit as an owner bonus that's great, but you don't want to rely on profit bonuses for your yearly compensation.

Once you have your sales goal, look at your current sales and see how far you have to go and whether you have the resources you need to get there. Useful ABACUS figures to help with this analysis include: sales growth vs. prior year to see if you could be growing faster and net sales per selling square foot. Sales per square foot can vary quite a bit from urban to rural areas, so when analyzing this particular figure, you may need to run a separate report on the ABACUS website.

Sales growth can come from multiple avenues. Your inventory mix and size certainly play a role, as do your systems and procedures to create an outstanding customer experience, but your marketing efforts may be your main growth driver. You should steadily increase your customer base and your core sales year-over-year until sustainability is in sight.

## 4.8 USING ABACUS TO ANALYZE YOUR BUYING

When looking for more profit, it's generally best to start with your biggest expenses. That's likely going to be cost of goods sold (COGS) for most stores. When evaluating how well your buyer is doing (whether that's yourself or an employee), the three ABACUS metrics to pay the most attention to are:

**Cost of Goods Sold** percentage, **Gross Margin** percentage, and **Inventory Turn**. If your buyer is doing a good job with the basic retail skill of buying low and selling high, your COGS and Gross Margin percentages should be on par with your peers or better. "Better" for COGS means lower and "better" for Gross Margin means higher. If they are not, you may have to dig deeper into why.

Perhaps you buy low, but you also offer discounts for customer loyalty programs, teachers, veterans, etc. In that case, you may get the same vendor discounts as your peers, but your COGS percentage will be higher, and your Gross Margin percentage may be lower than your peers who don't discount.

If your COGS percentage is higher than your peers and you don't do a lot of discounting, you may need to add some higher-margin sidelines or move more of your purchases direct to publishers.

Your **Inventory Turn(over)** rate can help you decide if you have the right inventory level and mix. There are a few ways to calculate turns. Using the retail formula, if you have sales of $300,000 per year and your average inventory cost at retail is $100,000, then you have turns of three (3). The average industry turn rate for new bookstores is around three (3). If you're only at a rate of two (2), you may be carrying too much inventory for your space, and doing returns to give you more room to merchandise and face-out could increase your sales. Or, you may have the right amount of inventory, but don't have quite the right mix. You may need to fine-tune your buying criteria or invest in tools like Edelweiss Analytics.

You may also be fine with having a lower than average turn rate; however, if you have cash flow issues, you may want to consider improving your turns.

## BUYER METRICS

| METRIC | BETTER | WORSE | FACTORS |
|---|---|---|---|
| Cost of Goods Sold % | Lower | Higher | Vendor discounts, product mix, freight, restocking fees, markdowns/sales, discounts |
| Gross Margin % | Higher | Lower | |
| Turns | Higher (unless > 6) | Lower (usually) | Inventory levels, return frequency, sales |

Improving turns typically results in better cash flow, as it means moving inventory faster or shrinking inventory via returns, which generate return credits. If you have really high turns of six (6) or more, this can be a sign that you should consider investing in more inventory to grow your sales.

Keep in mind that pop-up stores, events-only stores, bookmobiles, and other models that sell on a pop-up or events basis will (and should) generate higher turns than traditional brick-and-mortar stores. If you operate on one of these store models, it's possible that a turn of six (6) is usual. If your turns are low, consider carrying less inventory and displaying all books face out (or face up) on your tables to increase sales.

## 4.9 ABACUS AS A FINANCIAL DASHBOARD

As you will learn throughout this course, the purpose of a financial dashboard is to bring disparate information into one central location so you can get a big picture view of your store finances and see trends over time.

ABACUS is basically a financial dashboard for both our industry as a whole and for your specific store; however, it only comes out once per year. Many metrics are better tracked on a weekly or monthly basis so you can notice issues and react to them quicker. As you think about the data ABACUS provides you, consider which metrics are most important to your store and may need to be tracked more frequently on the dashboard you create for this course.

## SUMMARY

**Why It Matters**

ABACUS is an annual survey in which bookstores report financial information to the American Booksellers Association (ABA). ABACUS is our industry's best tool for analyzing stores' financial performance. It provides baseline metrics to help you compare your store to industry averages. It benefits independent bookstores, the publishing industry as a whole, and the ABA staff members who work on behalf of independent bookstores lobbying with publishers, legislators, vendors, and others.

**4.1 The Basics**

ABACUS gives us baseline industry metrics, which are useful for both new and existing stores. These baseline metrics help you get a data-based idea on how you are doing. It also helps those considering opening an independent bookstore to make realistic plans and projections and those who already have stores to improve operations and hopefully become more profitable or resilient.

**4.2 How ABACUS Comparisons Help**

Submitting financials to ABACUS helps you to be proactive in paying attention to your financial performance, looking at the different data points, and seeing where you can make a measurable difference. It also helps you understand where your gut instincts are correct or off, set goals, and know where to focus your attention. ABACUS can help you know where you're doing well when you see that you're ahead of industry average in a certain area.

**4.3 Where to Find Data for ABACUS**

You can find the data to help you report to ABACUS from a mix of sources: your Profit & Loss statement or company tax return and reports from your point of sale system, e-commerce website, or event ticketing platform. Creating a map between your data and the ABACUS survey will save you time later.

**4.4 Tips & Tricks for Submitting ABACUS**

The first step to making ABACUS easy is to go through the ABACUS questionnaire step-by-step and think about how to obtain the requested data. The data for the income and expenses section will generally come from your Profit & Loss statement. Subcategories in your Chart of Accounts are an easy way to track items for ABACUS, but before you set this up, ensure you fully understand your Chart of Accounts and have a conversation with your accountant.

**4.5 Using ABACUS to Create More Profit**

You can use ABACUS to compare yourself to other stores in your sales bracket to see which expenses you could reduce. Reducing expenses generates extra cash, which can allow you to pay down debt, bump up your owner compensation, or purposefully pay higher-than-average wages to attract and retain staff.

**4.6 Using ABACUS to Investigate Expenses**

You should compare expenses to similar stores through ABACUS, look at expenses where you see considerable variance from your peers, and investigate why. Cost of Goods Sold (COGS) is likely your biggest expense. You can easily compare your store to other stores to see if your inventory expense is a higher percentage of sales than the average, which tends to be around 55%. The next biggest expense a store usually has is payroll, including owner compensation. A general rule of thumb is that payroll should be around 25% of sales or less.

**4.7 Using ABACUS to Determine Store Viability**

One of the most useful figures ABACUS gives us for determining long-term sustainability is owner compensation. The average across all stores is 4.4% of sales, and likely, the highest you could sustainably get to would be about 10% of sales. To calculate the sales range you would need to hit for sustainability, take your desired salary at success and divide it by .1 to get the low range and by .044 to get the high range.

## 4.8 Using ABACUS to Analyze Your Buying

When evaluating how well your buyer is doing (whether that's yourself or an employee), the three ABACUS metrics to pay the most attention to are: Cost of Goods Sold (COGS) percentage, Gross Margin percentage, and Inventory Turn. If your buyer is doing a good job, your COGS and Gross Margin percentages should be on par with your peers or better. Your Inventory Turn(over) rate can help you decide if you have the right inventory level and mix. Improving turns typically results in better cash flow.

## 4.9 ABACUS as a Financial Dashboard

ABACUS is basically a financial dashboard for both our industry as a whole and for your specific store; however, it only comes out once per year. Many metrics are better tracked on a weekly or monthly basis so you can notice issues and react to them quicker.

### KEY TAKEAWAYS

- ABACUS gives us baseline industry metrics.
- You can use ABACUS to monitor your financial performance, understand where to focus, set goals, and see where you can make a measurable difference.
- Create a map between your data and ABACUS to save time.
- You can use ABACUS to reduce expenses and create more profit.
- ABACUS can help you analyze your buying.

### TEMPLATES & RESOURCES

- **Resource**: 2023 ABACUS Survey Questions
- **Resource**: PK Sindwani's ABACUS Presentation

### KEY TERMS

- ABACUS
- Chart of Accounts
- Cost of Goods Sold
- Gross Margin
- Inventory Turn(over)
- Profit & Loss statement
- Purchases

## REVIEW QUESTIONS

**True or False**:

- When you submit your data to the ABACUS survey, everyone who participated can see the results for your individual store.
- ABACUS is a financial dashboard.
- ABACUS stands for the American Booksellers Association Census.

## ANSWER KEY

- FALSE
- TRUE
- FALSE

## DIG DEEPER

# TAKING ACTION FROM YOUR ABACUS COMPANY REPORT

Most bookstore financial indicators are highly correlated (positively or negatively) with sales volume. Thus, when looking at your own data, the report card at the beginning of your company report (which compares to all companies) may not be as useful as comparing to your current sales bracket in the Company Performance Report. Your Company Performance Report always shows this comparison, but it's usually a couple of columns over, or you can run a revised company report card on the benchmarking site using your sales bracket as the filter to get a nice colorful report card comparing you to other stores in your sales bracket. Depending on which way you look at the data, the report labels are slightly different.

Below are measures we think are most important to review and analyze.

### NET PROFIT MARGIN/NET OPERATING PROFIT BEFORE TAXES AS A PERCENTAGE OF SALES

This is your profit from your Profit & Loss statement before Other Income and Other Expenses and usually shows your profit from inventory-related sales.

**Too Low/Weak or Fair.** Investigate ASAP! Check to see if your cost of goods sold is too high. If so, see the COGS section below. Check all expense categories to see which need better control. If you have a lot of Other Income, check your Net Income (at the end of Other Operating Costs section on your Company Report) to see if it's OK or also low. Perhaps your model depends on a lot of high-profit non-inventory income streams.

**Too High/Strong.** Know why this is so and make sure you are not misreporting. Are you not compensating owners for their work? Do you own your building and are not paying market rent?

### COGS/GROSS MARGIN/GROSS MARGIN AS A PERCENTAGE OF SALES

**COGS Too High/Margin Too Low/Weak or Fair.** If you buy a lot of non-returnable (books and/or sidelines) merchandise, this could indicate poor inventory selection, leading to clearance sales or giveaways that erode margin. If buying returnable, you may need to move more buying and returns direct to publishers for better margins and fewer restocking fees. If you offer customer discounts or have B2B sales, your COGS/Gross Margin will be worse than a store that sells the same amount of merchandise at full retail.

## DIG DEEPER

If you primarily carry books, you could add higher-margin sidelines in an attempt to increase your gross margin or rethink your discounting policies.

**COGS Too Low/Margin Too High/Strong.** If you take used books for trade credit, make sure you report those credits as part of your COGS. Otherwise, a high margin is rarely a problem except that it may not be sustainable as your business grows. Other retailers may start to carry your most profitable products, or other bookstores may open near you, and you may have to reduce your margins to compete.

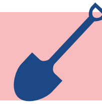
### INVENTORY TURNOVER

Inventory turnover tells you how many sales dollars are generated by each dollar of inventory.

**Too Low/Weak or Fair.** It's possible you have too much inventory for your space. If you're a new brick-and-mortar bookstore with more than $50-75 of inventory per square foot, consider reducing your inventory to that level. Otherwise, you may simply have the wrong mix and need to return quicker so you can buy more of what is selling. If you don't have a brick-and-mortar and see a low turnover rate, take into account the events and pop-ups you've done recently, including attendance/foot traffic, time of event, weather, etc. If everything was great and you still see a low turnover rate, consider doing returns and starting fresh at the next event.

**Too High/Strong.** Above turns of six (6) in a brick-and-mortar store, you are likely losing out on sales by not having sufficient inventory. You should consider increasing inventory, even if you need to increase leverage. If you don't have a brick-and-mortar, your turns may be higher, but if you start seeing turns of ten (10) or higher, you should consider increasing inventory at your next event.

## D I G   D E E P E R



# NEW BOOKSTORE BURNING FINANCIAL QUESTIONS

### QUESTION #1: WHAT SALES LEVEL DO I HAVE TO REACH TO BECOME SUSTAINABLE?

First, you must define what sustainable means to you. Does it mean not putting in your own money each month to sustain the store? Does it mean at least paying yourself *something*? Paying yourself a living wage as a working owner? Or does it mean paying yourself a living wage as a working owner who works no more than 35 hours per week?

Next, track gross margin. **Gross Margin = Net Revenue - COGS** and is usually expressed as a percentage. If you buy all new books from Ingram and don't do any discounting or many returns, your gross margin might be 40%. If you're a used bookstore, your gross margin could be as high as 60%. Really investigate whether your COGS seems accurate. If you do any discounting, you may want to set up a "Sales Discount" account in your Chart of Accounts as a "contra" account to sales (meaning it subtracts from your sales) so you can see the amount of margin you are giving away that you could potentially reclaim with a change of policy.

Third, carefully track all your expenses and classify them as fixed (unrelated to sales volume, such as utilities) or variable (related to sales volume, such as register tape or shopping bags).

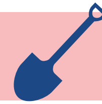
Once you have these three pieces of information, use the breakeven formula:
**Breakeven Sales = Gross Margin % / (Desired Owner Wage + Fixed Expenses)**

Whenever you choose to take on a new fixed expense or set a new desired owner wage goal, you would need to recalculate the formula.

### QUESTION #2: CAN I AFFORD TO PAY MYSELF AS A WORKING OWNER?

This question touches on issues of both profit and cash flow. Typically, but not always, the working owners do not get paid until after the store passes the first breakeven level and stops bleeding cash. The exception is if you got a startup loan and factored in owner salaries from the beginning.

## DIG DEEPER



There are three ways to increase profit: increase sales, reduce expenses, or both. Let's pretend that your store's fixed expenses are $90,000 per year, your gross margin is 45%, and you eventually want to pay yourself $30,000 per year. Currently your sales are at $200,000, which is breakeven. To pay yourself what you want, you'd either need to grow sales by 33% to $266,667, or you'd need to cut expenses by one third. It is highly unlikely you're going to be able to cut enough to achieve profitability, and if you cut muscle instead of fat, you're going to stunt the business.

New stores typically need to focus on increasing sales while keeping an eye out to make sure their expenses aren't completely out of whack (this is where an ABACUS comparison can be useful). One of the best ways a new store can "cut expenses" is to focus on improving margins. In the previous example, gaining just 1% point of margin from 45% to 46% means that now you only have to grow sales by 30% instead of 33%.

However, just because your profit & loss statement shows a profit, it doesn't mean your cash flow will support your desired owner payments. Many stores consciously (or unconsciously) plow any profit back into the store to grow inventory and/or staff to in turn grow sales to try to reach the next breakeven point.

Before you can afford to take cash out of the store, it's best to create a system to proactively measure and manage your inventory levels. You need to decide if you are trying to hold inventory steady or increase it. It's rare for a newer store to want to decrease inventory. You'll need to measure your inventory levels each month and determine action steps to take if your inventory is growing more than you want it to (return old merchandise, hold off on restocks, or reduce next month's frontlist buy).

Alternatively, you can sometimes grow sales even without growing inventory by turning your inventory faster. If you have $50,000 in inventory at retail and it turns twice per year, then you're generating $100,000 in sales. If it turns four times per year, you've increased sales to $200,000. One way to increase turns is to return your duds faster and invest that money in more of what seems to be selling for you. Another way to increase turns is to get more eyes on your inventory – either increase customer traffic to the store, merchandise better, train your staff to be better handsellers, or market your books via social media and email newsletters. Improving turns may not require you to invest more in inventory, but it's not without cost, as your returns freight will increase, and unless your staff have free time, you'll pay more in payroll.

## DIG DEEPER

Once you are reliably profitable and managing your inventory so that your profit stays liquid, then the best way to know if you can afford to pay yourself is to set aside your desired salary in a separate business bank account for three months (where you can get to it in an emergency) and see how well the business does without it. Can you get by without raiding the account? Ideally, you should try this during your lowest sales quarter.

### QUESTION #3: I HAVE A LIMITED AMOUNT OF TIME FOR BUYING, BOOKKEEPING, EMPLOYEE MANAGEMENT, MERCHANDISING, AND MARKETING. HOW BEST SHOULD I SPEND IT? HOW DO I GET THE BIGGEST BANG FOR THE BUCK?

As a new business owner, your goal is to grow sales to viability. Growing sales has several components, including merchandise, marketing, and the customer experience.

To reach viability, most brick-and-mortar bookstores will require employees. Given this, the owner should first work on creating a solid customer experience, documenting standard policies and procedures, capturing the data you need to make future decisions, figuring out how to hire and train staff to implement your vision, and creating oversight systems to make sure procedures are followed, even if your "staff" is just a part-timer who comes once per week. You want to dial in the customer experience before you turn on the marketing spigot. This is why many stores have a "soft" opening before their highly publicized "grand opening."

Next, you want to figure out if marketing is your superpower or if you're better off hiring for it. Marketing help can range from a high-school student who loves Instagram to a 1099 contractor who runs Facebook ads for you. The phrase "always be marketing" is very true. Even after you hit a sustainable sales level, you'll always have some degree of customer churn from those who move, die, or otherwise stop or reduce their patronage. Given this, marketing is not only for your opening, but is a critical expertise that will always be needed by your business.

Once you've got the customer experience down and a marketing plan, you should learn how to improve your margins and inventory turns. Also, it's important for an owner to understand their books and chart of accounts, but not necessarily to do the bookkeeping themselves. However, bookkeeping is one of the more expensive tasks to outsource, so if you find it enjoyable, you may want to keep it on your plate.

## DIG DEEPER

The trick to freeing up owner time is to find a nice arbitrage opportunity where you can replace your time fairly cheaply without losing a lot of quality. For example, it usually doesn't make sense for an owner to be receiving/shelving/returning books. It's tempting to hang onto the front desk role, but you'd be better off using your time to train staff to become better handsellers or figure out how to communicate your buying to them.

### QUESTION #4: CAN I AFFORD AN EMPLOYEE?

Can you afford not to have a team? Business is about creating a team to implement your leadership vision. It is nearly impossible to grow a brick-and-mortar retail store to sustainability without employees unless you are a nonprofit using volunteers or a co-op or worker-owned business where the workload is shared. Some store models might be able to use 1099 contractors, but standard retail uses W2 employees, so learning the skills of hiring, training, firing, managing, and delegating, which we generally are not taught in school, are important.

Your job as the owner is to evaluate whether you can pay a living wage, how much you can afford to pay, and what level of skill you are looking for. Before hiring, you should ideally know the main tasks you plan to delegate, have written procedures and training material, and have a plan for what you will do with your free hours after the employee is trained to produce two to four times the amount of income you are paying the employee. You should also research payroll software, state and federal labor laws, etc. If you can, it's not a bad idea to save up three months of what you'll pay the employee as a buffer so you don't worry about making payroll, but ideally it's better to hire when you're at 80% capacity than at 120% capacity. Training takes time and energy, and if you're already running on empty, you are probably not representing your business to your new employee in a manner that will create a loyal, enthusiastic employee.

ABACUS recommends that all payroll costs, including owner wages, employer taxes, benefits, etc., be between 20-25% of total sales. Adding a new employee is an investment in your business and a way to grow sales. Adding staff might let you expand your hours, attract new customers, take part in offsite sales opportunities, or add needed marketing skills. Investments are rarely guaranteed and usually contain some risk, but wasn't opening a bookstore risky too?

*Chapter 5*

# Event, Promo, & Co-Op Management

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Build an event profit & loss statement.
- Build a tracking system for promos and co-op.

## WHY THIS MATTERS

Events are an integral part of many bookstores' businesses, both from a financial and mission perspective. Looking at your specific event finances will help you improve your accuracy in predicting how much you can make at events and reduce the possibility that costly mistakes like overstaffing, understaffing, or overpaying for a venue happen.

Also, taking advantage of **publisher promotions** and **co-op** is key to maximizing your cash flow and minimizing your **cost of goods sold**. With a good system for tracking and using publisher promotions and co-op, you will get better discounts, increase your cash flow, and decrease your cost of goods sold.

## CHAPTER OUTLINE


**5.1** The Basics
**5.2** Event Finances
  **5.2.1** Building an Event P&L Statement
  **5.2.2** Creating a Year-Over-Year Tracking System
  **5.2.3** Tips & Strategies for Making Events Profitable
**5.3** Publisher Promotions
  **5.3.1** How to Track Publisher Promotions
  **5.3.2** Tips on Managing Publisher Promotions
**5.4** Publisher Co-Op
  **5.4.1** Big Picture Questions About Co-Op
  **5.4.2** Getting Started With Co-Op
  **5.4.3** Types of Co-Op
  **5.4.4** Tracking Co-Op
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Running a Successful Pre-Order Campaign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## 5.1 THE BASICS

Tracking event finances and analyzing that data is an important financial planning tool that will help you choose what kind of events to do more of and which ones to stop doing to ensure your event program remains stable and profitable. Creating **profit & loss statements** for each event also helps you plan and predict financial outcomes for future events and helps you with budgeting.

Taking advantage of **publisher promotions** and **co-op** is key to maximizing your cash flow and minimizing your cost of goods sold. With a good system for tracking and using publisher promotions, you will get better discounts and make higher profits by lowering your COGS. And very likely, you are already doing many things you can use to claim co-op! Co-op is money on the table offered by publishers, and you can use it to ensure you have the funds to keep your inventory fresh.

## 5.2 EVENT FINANCES

When looking at your current or anticipated event program finances, ask yourself these big picture questions to start:

- What are your big picture goals? Are your events a marketing tool or a sales driver?
- Is your events program mission-driven or profit-driven? If mission-driven, you will look at your event program's budget differently than if it is profit-driven. Mission-driven programs or events would generally fall under the marketing budget, whereas profit-driven events would fall under your general store budget or a specific events budget.
- If you had an event program in previous years, did that program make money? Did it make money if you factor in all of your costs? Did it meet other goals, like social media growth or overall sales growth from new customers? What are the potential areas for improvement? What are the financial strengths?
- Is your store financially stable enough to absorb unexpected costs? If an event gets canceled at the last minute, can you afford to refund the bundled tickets and return the books ordered (or absorb them into your normal inventory)? Do you hold event ticket money separately until the event is over to ensure you can refund if necessary? Do your terms with publishers allow you to order large quantities for events without exceeding your credit limit?
- What is your event strategy? How are you making these events happen? What angle are you working? What markets are you diving into?
- Can you afford staffing for events? Events often add hours outside of your regular operating hours, and even if they don't, they may happen offsite, which requires extra or after-hours staffing, which adds to your budget.
- Do you have the finances to invest in the logistics and infrastructure it takes to hold events in-store? Can you invest in equipment like microphones, mic stands, speakers, chairs, etc. to make in-store events as successful as possible? How many events do you need to have to make those investments worthwhile?

Once you've asked yourself the big picture questions about event finances as a whole, the next step is to ask yourself some event-specific questions when building your finances/budget for a specific event:

- What are your goals for the event? Is this a community event that should fall under your marketing budget? Are you hoping to get a big boost in sales all at once?
- What are your must-haves, or needs, for this event? What are your extras, or wants? Do you *need* an offsite venue or would it just be cooler? Do you *need* to provide snacks or can you just have bottles of water in case someone needs one? What are the corners you can cut without sacrificing the goals of the event if you need to?
- How can you prepare for unexpected costs?
- Can you take the loss if the event gets canceled? Do you have an escrow account for tickets that have sold? Make sure you **do not** spend that money, in case of cancellation.
- What can you consolidate?
- Should you shop around for venues, software, equipment, etc.? Are there options available that better fit into your budget? Is there a venue with lower fees and included equipment? Do you need all of the bells and whistles of a full POS for an offsite event? Are there options that fit your budget/mission/goals better? Consider your goals, mission, values, and budget when looking for venues, tech, and hosts. Shopping around could also help you find local businesses to partner with!
- What can you automate? Event grid requests can be done using a template. You could also create a digital form to collect day-of event data that automatically gets dumped into a spreadsheet to save time. Creating systems that require minimal effort to maintain can save you a huge amount of time and effort.
- How does this event fit into your store's event strategy? What were your greatest successes and failures? What areas are you trying to concentrate on? How do those goals fit with your big picture financial goals?
- What type of staffing will your event require? Don't forget that staffing is more than just day-of staffing. Will staff need time to make flyers? Reply to emails? Collect supplies? Even if this is done during store hours, we recommend tracking time spent on events so you can make sure you account for opportunity costs.
- What type of equipment will your event require?

Asking yourself all of these questions will help you build a successful events financial strategy and make decisions about what events are worth it for you and which ones are not.

### 5.2.1 BUILDING AN EVENT P&L STATEMENT

Chapter 11 will be a deep dive into profit & loss statements, but since this chapter covers them in terms of events, here is a brief introduction. A **Profit & Loss Statement**, or P&L, is a financial statement that summarizes your revenue and expenses incurred during a specific period (or in the case of this chapter, a specific event). This statement provides information about how much you made (or didn't make) and breaks all your expenses down so you can analyze each category. A P&L can also be referred to as an "income statement." The statement begins with your total revenue/sales, then lists your **cost of goods sold** and **gross margin**, which is your total sales minus your cost of goods sold. Next comes all your expenses, and for events, **co-op** received is added after that. At the bottom is your **net income**, which is your gross margin minus all your expenses, and thus, how much money you actually made or lost.

Running a profit & loss statement for every event you host is worth the time. Event profit & loss statements look different from a general P&L because they include things that are event specific. You may also find it useful to create a seasonal events P&L to understand seasonal event trends.

The first step in creating an event-specific P&L is figuring out a way to track your event-specific sales. Stores with different models do this differently, but if you have a brick-and-mortar store, you should look up which sales in your POS system are from events versus your normal sales, otherwise your P&L will be off, and so will your reorders from publishers. One way to do this is to run sales of event-specific titles from 1 week prior to the event to 1 week post-event. This allows you to account for the residual sales/excitement surrounding the event, even if the day-of sales are lower. For example, did everyone pre-order, so sales happened before the event day? Did everyone who attended the event come back for the rest of the author's books two days later? Running sales pre- and post-event help you capture this data.

Some stores create a unique SKU or promo code that is linked to the event in their POS system so they can pull event sales. In some POS systems, you can create an event category and move the inventory for the event into that category, then run a report that pulls sales based on the category. Any of those methods are valid, but make sure that you use the same method every time. Data tracking is so much easier if you're consistent!

You will track book sales, ticket sales (if the ticket is not just the cost of the book), café sales if applicable, and sideline sales if relevant for the event, like a craft event that sells craft kits or supplies. You will also track cost of goods sold for the event, which would include only costs of event-specific inventory. Add up all of your revenue/sales categories, then subtract your cost of goods sold, to get your gross margin for the event.

# EXAMPLE EVENT
# PROFIT & LOSS STATEMENT

| [Your Bookstore]<br>Event Profit & Loss Statement<br>[Time Period Covered] | | | |
|---|---|---|---|
| **Revenue** | | | |
| | % of Total Revenue | Enter your own $ amounts in blue boxes | |
| **Net Revenue/Sales** | **100%** | **$1,500** | |
| Event book sales | 66.67% | $1,000 | |
| Ticket sales (Not including price of book) | | $0 | |
| Cafe | 0.00% | $0 | |
| Sidelines | 33.33% | $500 | |
| **Cost of Goods Sold (Combined)** | **52.67%** | **$790** | |
| **Gross Margin** | **47.33%** | **$710** | |
| | | | |
| **Expenses** | | | |
| Payroll used for event planning | 3.00% | $45 | |
| Payroll used for Day-Of event help | 5.00% | $75 | |
| **Total Payroll** | **8.00%** | **$120** | |
| Venue | 0.00% | $0 | |
| Chairs/AV/Event Equipment | 0.00% | $0 | |
| permits, if needed | 0.00% | $0 | |
| **Total Occupancy** | **0.00%** | **$0** | |
| Social Media | 1.33% | $20 | |
| Tech/Software | 0.00% | $0 | |
| Honorarium for Speaker | 0.00% | $0 | |
| Marketing | 0.00% | $0 | |
| Printed Materials | 2.00% | $30 | *Things like posters, etc.. |
| Materials for event use | 0.00% | $0 | *Things like craft supplies |
| Travel | 0.00% | $0 | |
| Refreshments | 3.33% | $50 | |
| Decor | 0.00% | $0 | |
| Security | 0.00% | $0 | |
| Returns | 0.00% | $0 | |
| **Total Operations** | **6.67%** | **$100** | |
| **Total Expenses** | **14.67%** | **$220** | |
| **Net Income from event/Operating profits from eve** | **32.67%** | **$490** | |
| Co-op, other sources of cost sharing from Publisher | | $50 | |
| **Total Co-Op** | | **$50** | |
| Other costs | | **$0** | |
| **Net Income** | **36.00%** | **$540** | |

Some stores are hesitant to track event expenses, as it does take additional time; however, it is important to do so to ensure your events are meeting your financial goals. Here are a few expenses included in the example Event Profit & Loss Statement on the previous page you should ensure you account for.

## Payroll for Event Planning

Even if staff are doing the planning on the sales floor or if you plan the event yourself, planning an event takes time, which costs money. If you or your staff weren't planning this event, that time would have been allocated to something like selling/merchandising that actively makes money for your store. Event planning can be stressful for you and/or your staff, and there is a cost to stressed staff, so keeping solid documentation of the hours used for event planning can help you know the true financial and human costs of the event.

## Chairs/AV Equipment, Etc.

This is a category often skipped by stores that own equipment, but the wear and tear on those things is an expense. You will have to replace broken chairs or get new speakers when they get stomped by a 6-year-old. You should factor those costs into your calculations before they become emergency expenses. You can calculate this by taking the full cost of the item/equipment divided by the number of events you generally host over the course of three years. If that comes out to $0.50/chair, then when you put out 20 chairs, it costs $10.

## Honorarium for Speaker

Not every author or speaker will expect payment, but this is a line item that is often not discussed until deals have already been finalized, and it is too late to back out. This should not be a hidden expense, so make sure you have clarified whether this is part of your equation before finalizing the decision to host an event. As a general rule, if it is a publisher-sponsored tour or an author event specifically to sell books (like a book launch or author signing), you won't need to worry about this, but if you approach an author directly to do a presentation or panel, there is a much higher chance they will expect an honorarium.

## Printed Materials

This includes signage for local businesses, bag stuffers, etc. Sometimes these costs will be close to nothing, but they can add up fast, so know what you spend.

## Materials for Event Use

This includes anything used during the event. If you host a Sip and Paint evening, the cost of the canvases, paints, brushes, etc. should all be included in this line item. If it is an author signing, these costs might just be sharpies and a couple of bottles of water.

## Returns

This is one of those line items you don't want to think about, but it must be accounted for. Sometimes, publishers will cover this cost for you (it doesn't hurt to ask them if they will

cover this when you're planning), but you should otherwise double-check how much you'll pay for the books to be returned, especially in the event of a last minute cancellation.

### Co-Op

Although this isn't an expense, co-op is a good line item to add to the bottom of your event P&L, as it is often a solid way to offset some of the costs of hosting a successful event.

If your expenses and sales are tracked well, you should have a solid idea of your profit for each event. It's good to have individual P&Ls for every event as well as a master spreadsheet with less detail listing your event finance numbers as a whole to calculate year-over-year growth seasonally.

## 5.2.2 CREATING A YEAR-OVER-YEAR TRACKING SYSTEM

You should run a combined events P&L for all events at least once a year, but we also suggest tracking your **Year-Over-Year (YOY)** profits for events at least once per quarter. Since YOY tracking is going to account for seasonal fluctuations more than most tracking, this will allow you to identify overall trends, like events in May are rough because everyone is so overwhelmed, as well as soft areas, like whether your event profits are trending lower than in previous years.

The simplest way to do this is with a spreadsheet. Take your individual event P&L statements based on date, then enter those numbers into the spreadsheet for the year. When you're ready to do the comparison, it's easy to compare based on total year-to-date or any other metric you wish to use. It's good to look at this data quarterly, however, you can check by month, by week, and/or by number of events. For example, you can look at your first 15 events of last year compared to your first 15 events of this year. When doing these comparisons, it's important to note factors like weather, traffic, competing events in town, and other things that could have affected your events.

For any metric you use, the formula is always the same:

**YOY = (This Year's Number - Last Year's Number) / Last Year's Number**

## 5.2.3 TIPS & STRATEGIES FOR MAKING EVENTS PROFITABLE

Here are some tips and strategies you can employ to help make your events as profitable as possible.

- Events that cost money where you don't make sales should go under your marketing budget.
- Know if your staff is excited about events. Enthusiasm means better sales. Residual sales and long term customers are wins, but you need event sales to justify the program, unless your goal is mission or marketing based.
- Find a profitable lane and get known for it with both customers and publishers. For example, Southern author lunches, boozy book fairs, store book clubs, etc.
- Keep the in-house publicist in the loop, even if they didn't set the event up.

- Keep/update a record of your greatest hits, and use it for your publicity kit!
- Order books from the publisher at least 4-6 weeks out and track the order. If possible, have the order arrive in time to get damage replacements. You do not want to order event titles through a distributor with a lower margin.
- Plan for the worst. Use panels in case one author doesn't show, escrow funds, align your customer refund policies to venue refund policies if possible, and pre-arrange call tags or request them afterward if the author canceled if you can.
- Take lots of photos and share them and customer kudos with the rep/publicist.
- You may not make money on every event. This is where your events mission comes into play. If you know WHY you're doing events, it will drive whether making money is what's important to you. Even if you don't intend to profit off an event, you will still need to know how much that event is costing you, unless you have infinite money to lose.
- Keep money from event tickets/presales in escrow until after the event as a contingency fund. Move it to a separate bank account so you don't spend that money just in case.
- Consider things outside of your control when analyzing past events. Was the weather bad? Did the author cancel at the last minute?
- Data is power! If you have the capacity, record all of it. Finding trends in success can be made easier by tracking things like weather, attendance, time of day/day of the week, etc. Which display
- did you use for each event? Do you get better attendance/sales from events that were spotlighted from a specific place in the store?

## 5.3 PUBLISHER PROMOTIONS

**Promos**, or promotions, are deals that publishers offer that typically get you extra points on your discount, but also sometimes include things like swag or signed copies. Many times, there is a minimum order you need to reach to qualify for the promo. The big publishing houses (and a lot of the smaller ones too!) usually have regular offers, at least seasonally, and sometimes more often. Most have either a permanent backlist offer or time-limited offers issued on a regular schedule. These offers also usually have a pub date requirement that may be six months before or just the day before the promo was released. For example, Hachette has a perpetual backlist promo of +3% if you order 25 or more units published six months ago or before (code: BKLST3). Everyone should use that promo!

Financially, promos are a tremendous help. Of course, higher discounts mean higher profits and lower cost of goods sold. Publisher promotions have a direct impact on your bottom line, and it's basically free money, so you should take advantage as often as you can.

That being said, it may not make sense for you to take every single promo offered, for example, if the minimum order is a case of books you don't think you could sell. You should evaluate each offer that comes through and use trial and error to figure out what works best for you.

### 5.3.1 HOW TO TRACK PUBLISHER PROMOTIONS

Promos can be tricky to track. If you already have accounts with publishers, you can get bombarded with promo e-mails. It's important to ensure these e-mails don't get buried. If you don't have a system already, you should create something that tracks which promos are available and which you've used. This can be done in Trello, Airtable, Google Docs/Sheets, Excel, and others, so use what works best for you. The most important thing is that your promo tracking is done all in one place so you don't have to go back and forth searching different places for the information. The American Booksellers Association Book Buyer's Handbook on Bookweb is supposed to include promo information, but it isn't always updated, so make sure you check before using the information. If you're a member of the New Atlantic Independent Booksellers Association (NAIBA), they have an e-mail that goes out each week listing publisher promos. Check with your regional association to see if that information is available to you.

Every time you go to place an order, make it part of your process to check your tracking system for open promos before you submit. Another tactic is to e-mail the order to your sales representative and ask them to apply any appropriate promos before you submit.

In your accounting software, promos can be tracked as a **contra account** under cost of goods sold, meaning money is deposited into what is normally an expense account.

If you enter invoices individually, promos can also show as credits to the invoice. One reason to track promos under COGS is because the promo decreases the amount you pay for the inventory ordered under it.

### 5.3.2 TIPS ON MANAGING PUBLISHER PROMOTIONS

Here are some tips you can use to help you successfully manage **publisher promotions**.

- Look for promos in winter before Winter Institute, in late spring/early summer, in early fall before the regional shows, and in late fall around Indies First.
- Get in the habit of building orders in advance using seasonal holiday backlist promos. For example, if you sell a St. Patrick's Day book on March 16, put the re-order on a Winter Backlist promo order for the same publisher for the next year.
- Put the promo codes used on your order in your POS system or in Edelweiss.
- If you're unsure about what promos might be available, submit your order through your sales representative and ask them to apply anything the order is eligible for.
- You can also ask your sales representative to tell you if you're close to hitting a minimum for a promo so you can add to the order if needed.
- It's important for your receivers to know that an order was supposed to have a promo! Make sure you have a system for communicating with your receivers so they can check to ensure the promo was applied when receiving the order.
- Promo codes sometimes work on event orders, and sales representatives may apply them automatically for you.

## 5.4 PUBLISHER CO-OP

**Co-Op** means "cooperative advertising," and it's when publishers offer money or credit in exchange for you featuring their books in your marketing. Like promos, co-op has a direct impact on your bottom line. It's *almost* free money (you do need to spend some time on it), and it's easily a $10,000 annual value without requiring any upfront monetary investment.

To qualify for co-op, usually you must have a direct account with the publisher, a returnable account on terms (not prepaid/credit card), and a brick-and-mortar store. Stores without a brick-and-mortar may or may not qualify, depending on the publisher's rules for co-op. It does typically include new stores, who can claim co-op their first year, but if you're a new store that missed the deadline, you may need to have had a publisher account for at least one year, then sign up before the end of the first quarter of the next year to qualify. Gift accounts, non-returnable, and prepaid accounts do not qualify for co-op. Make sure to pay attention to sign-up dates, as those typically come around annually, and if you miss the cutoff, you may not be eligible to claim for the year.

Co-op is a reward for doing things you're likely already doing: making displays, sending newsletters, and hosting authors. It's a bit finicky, but it's totally worth it, because it can be big money. There are services out there you can use to track co-op for you, but they will take a significant percentage, usually around 40% of what you claim. That may be worth it to you! But you can get more money if you or someone on your staff tracks and submits claims.

Co-op is like creating an events program - the best way is to start small and build, especially if the order requirement causes you to buy more copies than usual of a title, because credits usually come after the inventory bills are due. It takes effort and organization to get started, but taking advantage of co-op can help you build relationships and even score bigger events.

### 5.4.1 BIG PICTURE QUESTIONS ABOUT CO-OP

Here are some big picture questions to ask yourself about co-op.

- Is your store eligible for co-op, or could you become eligible?
- Are you already claiming co-op? If so, do you have a plan/strategy to maximize what you're claiming?
- Are you tracking co-op? If so, are you tracking it separately?
- What is your overall co-op strategy?
- Do you want to use a service or do it yourself?

## 5.4.2 GETTING STARTED WITH CO-OP

If you'd like to get started with co-op, here is a basic checklist you can follow.

- Gather your co-op contacts.
- Ask your sales representatives if you qualify for co-op.
- Research co-op services, publisher co-op policies, available pool, and lists of imprints under divisions. Send a group e-mail to your sales representatives asking for co-op policies and update your internal document with the information.
- If you have an event scheduled, ask the publicist if event co-op is available.
- If you have a newsletter, submit a claim with HarperCollins or Sourcebooks for a title you featured in the last three months.
- Collect documentation of all your promotions (links, photos, etc.).
- Create a tracking system (use our sample spreadsheet linked in **Templates & Resources**).
- Meet with your co-op service or internal staff to discuss processes, timelines, and expectations.
- Create a plan for how you will spend pool co-op and how you will max out newsletter co-op for the year.

## 5.4.3 TYPES OF CO-OP

There are four main types of co-op: pool, newsletter, display/exempt, and author events. Let's get into what each of these are and how to use them.

### Pool

The first type of co-op is called "pool." This type of co-op is based on how much money you spend with a publisher. Some publishers calculate this based on the last fiscal year, and others based on the current fiscal year. Usually, it's about 2-4% of your retail spend. Some publishers have multiple pools, for example, one for adult and one for children's or one for directly published titles and one for distributed titles. Some of the pools are automatically credited based on your spend if you sign up, and some are not.

The automatic pools may have a tiered sales threshold or require you to give up newsletter co-op, and that is usually issued quarterly. It may also require a yearly survey or some other re-up form. Non-Automatic pools usually require pre-approval, then you have to submit an invoice or claim to get the credit. All of the Big 5 publishers have pools, and some of the smaller houses do as well.

The biggest thing with pools is to know whether they're automatic or if you're expected to submit something, and that you understand your pool calculation choices, as the way pools are calculated can differ. Direct is usually best, but make sure to ask.

### Newsletter

With newsletter co-op, the store chooses the titles you promote in your store's direct newsletter. This co-op does NOT work with Shelf Awareness, Indie Next newsletters, etc. - only with newsletters that come directly

from you. Sometimes, in order to claim this co-op, you have to order 5-6 copies of the title you're promoting. The publisher may also require a cover photo and/or a 50-word blurb about the title. Most publishers limit these to frontlist titles and require that you feature the title within three months of the publication date (HarperCollins is an exception to this). All of the publishers have a standard reimbursement rate for newsletter co-op, which can vary from $20-$80/title depending on the publisher. Make sure you add your sales representatives to your newsletter so they can see that you're featuring titles and that you archive your newsletter somewhere online so you can send a link to it with your claim. Publishers that offer newsletter co-op include: HarperCollins, Sourcebooks, and Hachette/Workman.

### Display/Exempt

Display/Exempt co-op means the publisher chooses the titles, and you get a credit if you order a certain number of copies (for example, $25 if you order six copies). You can often split the order between purchase orders as long as the total required quantity is ordered before the release date. Your sales representative should also know about this, because typically they will need to submit for you, although sometimes the system may do it automatically if you order the right number of copies. Some publishers also require that you feature the titles on a display at the front of the store and/or that you feature them in your newsletter. This is the only co-op outside of pool that Penguin Random House offers.

### Author Events

You can also get author event co-op. In some cases, this requires pre-approval, but in all cases, the event must be set up through an in-house publicist in order to claim co-op. Distribution clients may not qualify or may have their own rules/procedures, so check that before you submit a claim. Typically, this is either a set amount or based on your event order. It also usually requires proof of the event: pre-event marketing, event pictures, etc., that you send in. The event must occur in order to claim, even if the author/publisher is the one who cancels. If the event doesn't happen for ANY reason, you don't get to claim the co-op. This co-op is usually meant to cover advertising costs, not food or venue rental.

## 5.4.4 TRACKING CO-OP

Now that you've learned the different types of co-op, let's learn how to track it. First, you need to make sure that you sign up or renew each fiscal year, typically before the end of the first quarter. You should request the pool amounts and any policy changes for the new year from your sales representative, and you should also request and document the policies for each publisher. You'll want to sign up for the automatic pool if you're qualified or request your non-automatic pool amount if you don't qualify. Take a look at your last two months of newsletters and at the current one you have planned to see if anything might qualify for co-op. If it does, submit those claims. You'll also want to start a claim tracking spreadsheet noting title, pub

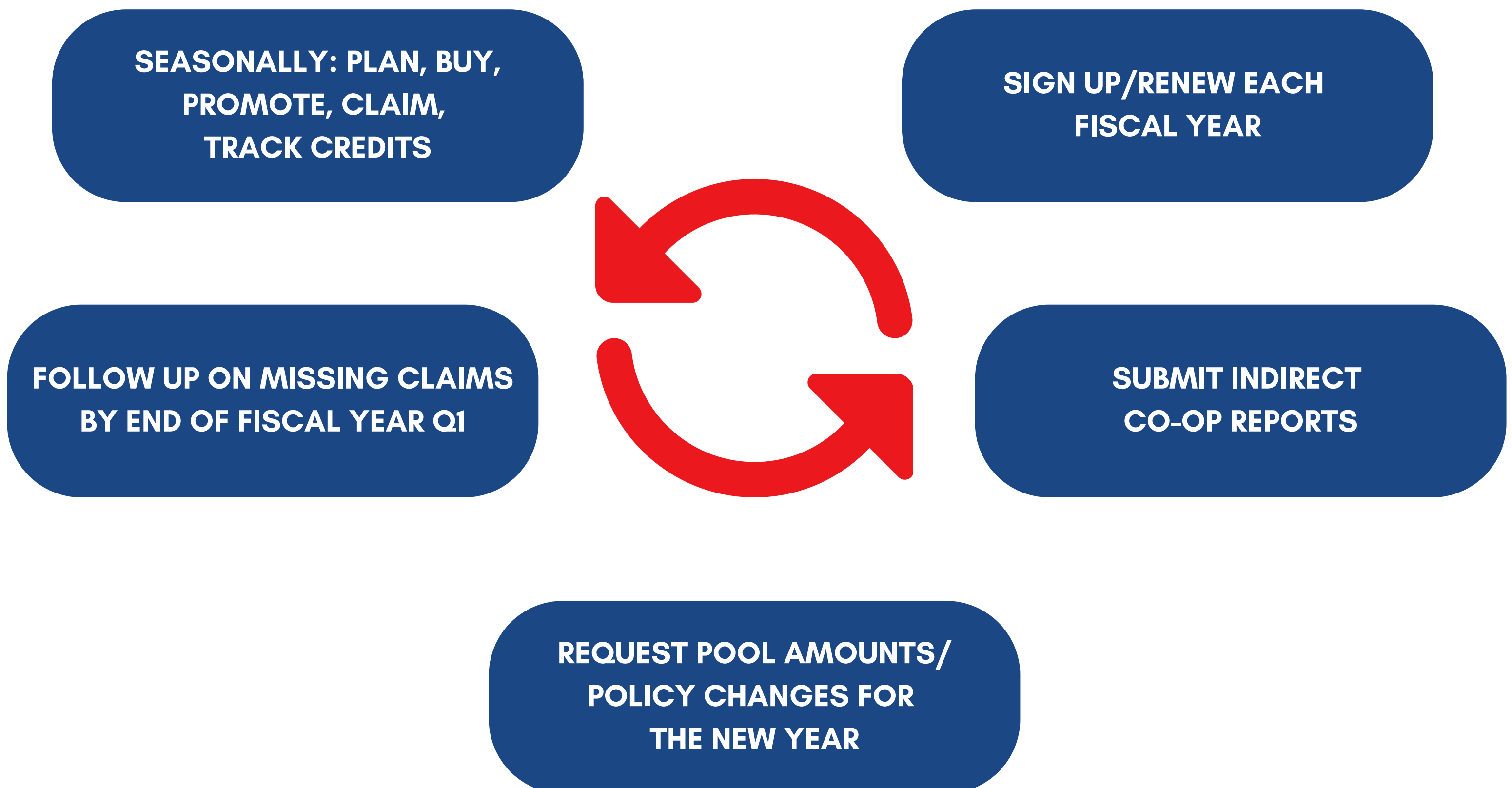
date, claim date, claim amount, and date the claim was received. You can see an example tracking spreadsheet in **Templates & Resources**. You'll also want to create a monthly reminder to submit your newsletter and author event co-op.

Seasonally, you'll want to plan out your co-op, buy accordingly, promote the titles needed to claim the co-op, actually claim the co-op, then track your credits. Plan out your newsletter co-op and note eligible author events you'll want to submit claims for. Talk to your sales representatives about pre-approvals and unfilled claims that are older than four months.

At the end of the year, you should submit your indirect co-op reports if you ordered titles from Ingram that you promoted for a publisher. You should also follow up on missing claims by end of the first quarter of your **fiscal year**.

In your accounting system, co-op credits are typically tracked under either a marketing or cost of goods sold subaccount and are separated from returns credits (one is marketing, one is returns). As you learned in the last chapter, ABACUS/ABA likes this tracked under marketing so the credits offset your marketing costs.

## YEARLY CO-OP WORKFLOW



# SUMMARY

**Why It Matters**

Looking at your specific event finances will help you improve your accuracy in predicting how much you can make at events and reduce the possibility that costly mistakes like overstaffing, understaffing, or overpaying for a venue happen.

Taking advantage of publisher promotions and co-op is key to maximizing your cash flow and minimizing your cost of goods sold. With a good system for tracking and using publisher promotions and co-op, you will have better cash flow and make higher profits by lowering your COGS.

**5.1 The Basics**

Creating profit & loss statements for each event helps you plan and predict financial outcomes for future events and helps you with budgeting. Very likely, you are already doing many things you can use to claim co-op. Co-op is money on the table offered by publishers, and you can use it to ensure you have the funds to keep your inventory fresh.

**5.2 Event Finances**

There are big picture, overall questions as well as event-specific questions to ask yourself about your event finances. View this section in the chapter for the list of questions.

**5.2.1 Building an Event Profit & Loss Statement**

A **Profit & Loss Statement**, or P&L, is a financial statement that summarizes your revenue and expenses incurred during a specific period (or event).

First, figure out how to track event-specific sales. You will track book sales, ticket sales (if the ticket is not just the cost of the book), café sales if applicable, and sideline sales if relevant for the event. You will also track cost of goods sold for the event, which would include only costs of event-specific inventory. Add up all of your revenue/sales categories, then subtract your cost of goods sold, to get your gross margin for the event.

For expenses, make sure you track: payroll for the event (including owner time), chairs/AV/equipment costs, speaker honorariums, printed materials, materials for event use, and returns. Also make sure to track co-op for the event to offset your costs.

### 5.2.2 Creating a Year-Over-Year Tracking System

Create a year-over-year tracking system with a spreadsheet. Take individual event P&L statements based on date, then enter those numbers into the spreadsheet for the year. When you're ready, compare based on total year-to-date or any other metric. It's good to look at this data quarterly; however, you can check by month, by week, and/or by number of events. When doing comparisons, it's important to note factors like weather, traffic, competing events in town, and other things that could have affected your events.

For any metric you use, the formula is always the same:

**YOY = (This Year's Number - Last Year's Number) / Last Year's Number**

### 5.2.3 Tips & Strategies for Making Events Profitable

View this section in the chapter for the list of tips to help make your events as profitable as possible.

## 5.3 Publisher Promotions

**Promos**, or promotions, are deals that publishers offer that typically get you extra points on your discount, but may also include things like swag or signed copies. Higher discounts mean higher profits and lower cost of goods sold. Publisher promos have a direct impact on your bottom line, so take advantage as often as you can.

### 5.3.1 How to Track Publisher Promotions

Create something that tracks which promos are available and which you've used. Promo tracking should be done all in one place. Every time you go to place an order, make it part of your process to check your tracking system for open promos before you submit. Another tactic is to e-mail the order to your sales representative and ask them to apply any promos before you submit.

In your accounting software, promos can be tracked as a contra account under cost of goods sold. Promos can also show as credits to the invoice in your system.

### 5.3.2 Tips on Managing Publisher Promotions

View this section in the chapter for the list of tips to help you successfully manage publisher promotions.

### 5.4 Publisher Co-Op

**Co-Op** means “cooperative advertising,” and it’s when publishers offer money or credit in exchange for you featuring their books in your marketing. Like promos, co-op has a direct impact on your bottom line. To qualify for co-op, usually you must have a direct account with the publisher, a returnable account on terms (not prepaid/credit card), and a brick-and-mortar store. Stores without a brick-and-mortar may or may not qualify, depending on the publisher’s rules for co-op.

Co-op is a reward for doing things you’re likely already doing: making displays, sending newsletters, and hosting authors. The best way to start with co-op is to start small and build. It takes effort and organization to get started, but taking advantage of co-op can help you build relationships and even score bigger events.

#### 5.4.1 Big Picture Questions Co-Op

There are big picture, overall questions to ask yourself about co-op. View this section in the chapter for the list of questions.

#### 5.4.2 Getting Started With Co-Op

There are some basic things you can do to get started with co-op:

- Gather your co-op contacts.
- Ask your sales representatives if you qualify.
- If you have an event scheduled, ask the publicist if event co-op is available.
- If you have a newsletter, submit a claim for a title you featured in the last three months.
- Collect documentation of all your promotions (links, photos, etc.).
- Create a tracking system.
- Meet with a co-op service or internal staff to discuss processes, timelines, and expectations.
- Create a plan for how you will spend pool co-op and how you will max out newsletter co-op for the year.

#### 5.4.3 Types of Co-Op

**Pool**: Based on how much money you spend with a publisher; may or may not be automatic. Know your pool calculation choices.

**Newsletter**: Store chooses the titles you promote in your store’s direct newsletter. May need to order 5-6 copies of the title, write a blurb, and/or feature the title within three months of publication.

**Display/Exempt**: Publisher chooses the titles, and you get a credit if you order a certain number of copies. May require you to feature the titles in a display or in your newsletter.

**Author Events**: Event must be set up through an in-house publicist. Either a set amount or based on your order. Requires proof of marketing for the event. Cannot claim if event doesn't happen.

#### 5.4.4 Tracking Co-Op

Start a claim tracking spreadsheet noting pub date, claim date, claim amount, and date the claim was received. Create a monthly reminder to submit your newsletter and author event co-op.

Seasonally, plan out your co-op, buy accordingly, promote the titles needed to claim the co-op, actually claim the co-op, then track your credits. Plan out your newsletter co-op and note eligible author events you'll want to submit claims for.

At the end of the year, submit indirect co-op reports if you ordered titles from Ingram that you promoted for a publisher, and follow up on missing claims by end of the first quarter of your fiscal year.

### KEY TAKEAWAYS

- Creating event P&L statements helps you plan and predict financial outcomes for future events and helps you with budgeting.
- A year-over-year tracking system will help you make comparisons to improve your event profitability.
- Co-op is money on the table for things you're likely already doing.
- Publisher promos give you higher discounts, which means higher profits and lower cost of goods sold.

### TEMPLATES & RESOURCES

- **Template**: Event P&L Excel Template
- **Template**: Year-Over-Year Analysis Excel Template
- **Template**: Promo Tracking Spreadsheet Template
- **Template**: Co-Op Claim Tracking Spreadsheet Template

## KEY TERMS

- Co-Op
- Cost of Goods Sold
- Fiscal Year
- Gross Margin
- Net Income
- Profit & Loss Statement
- Publisher Promotions

## REVIEW QUESTIONS

**True or False**:

- Expenses to be included in your Event P&L are: payroll, equipment, printed materials, speaker honorarium, event materials, returns, and co-op.
- The main types of co-op are pool, newsletter, author events, displays, and CCM.
- Orders with promos must be submitted through your sales rep.

## ANSWER KEY

- FALSE
- FALSE
- FALSE

## DIG DEEPER

### RUNNING A SUCCESSFUL PREORDER CAMPAIGN

Preorder campaigns are a great way to maximize cash flow. You can use them specifically for events, where customers order the book ahead of time, and for popular authors in your store. Here's some advice on running a successful preorder campaign and tracking finances for it:

- Choose books that your particular customers will want to buy. Don't just go with the big books publishers are promoting, as they may not be the same as what your customers want.
- If there's a book that you know will be big with your customers, you can approach the publisher/publicist and say you want to run a preorder campaign for it. Publishers are happy to send swag if they have it or at least bookplates to help you successfully promote one of their books.
- Make a schedule for social media posts, newsletter, and marketing. You can use Trello, Airtable, Google Sheets, Excel, or another tool you like. Create a list for each month, then create an entry for every event, newsletter, marketing campaign, etc. You can also use labels and checklists to make sure everything needed for planning is right at your fingertips.
- Have a cutoff date for the campaign.
- Have customers pay upfront. This gives you cash flow now and ensures that the copies you order are paid for. Make sure you set this money aside in escrow so you have enough to pay the invoice when it comes due.
- Don't run preorder campaigns more than three months in advance, as pub dates can change.

As far as sales for preorder campaigns, you should track these the same way you track special orders. If you run preorder sales through your POS system, it will track the sales for you, and you can run a report at any time to see how the campaign is going. If you don't run these through your POS so as not to track sales too soon, you can create a spreadsheet or an Airtable table that will automatically add up the number of copies sold and the total sales (not including tax) so you can keep track throughout the campaign. Having a spreadsheet or tracking in your POS system also ensures you have the data for reporting when the book is released.

## DIG DEEPER

Keep in mind that the sales for preorders don't actually count until the book is released, even if you're accepting the money upfront. In your bookkeeping, if you're on a cash basis, you would record the revenue when you accept the money, however, if you're on accrual basis, the revenue should not hit your books until the customer receives the order, which is when the sale actually happens. If you do any reporting to the New York Times or to Bookweb, make sure you don't report preorder sales until release week!

*Chapter 6*

# Staff Financial Management

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Understand the varying types of wages and benefits you can offer to employees.
- Understand when to use **1099** vs **W2** employees.
- Understand when and how to pay different types of payroll taxes.
- Determine how much payroll your store can afford to invest.

## WHY THIS MATTERS

You need to be able to make decisions about pay and benefits and discuss these things with your payroll processor and with your employees. Many bookstore owners are dedicated to the idea of paying living wages in their communities, but need to balance that against their stores' profitability and sustainability. You also need to be able to answer your employees' questions about their checks and their taxes.

Employee financial management has legal implications, and the money you spend on payroll is an investment, so it's important to ensure the return on that investment is healthy and you are investing intelligently. Keeping close watch on your payroll investment is one of the most important things you can do to keep your business financially healthy.

## CHAPTER OUTLINE

**6.1** The Basics
**6.2** Wages & Benefits
  **6.2.1** Employee Classification
  **6.2.2** Types of Wages & Benefits
  **6.2.3** Payroll Frequency
  **6.2.4** Time Tracking
**6.3** Taxes & Compliance
  **6.3.1** Payroll Taxes
  **6.3.2** Payroll Tax Remittance
  **6.3.3** Employer Contributions
  **6.3.4** Employee Contributions
**6.4** Payroll & Profitability
  **6.4.1** How Much Can You Afford to Invest?
  **6.4.2** Determining Wages & Salaries
  **6.4.3** Paying Yourself As An Owner
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Collecting & Storing Employee Data

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## 6.1 THE BASICS

When we can pay companies to handle most parts of payroll, why do you need to know about payroll taxes, employee classifications, and compliance? Even though we have the benefit of technology and do not need to calculate payroll taxes manually anymore, you *do* need to be able to make decisions about pay and benefits and discuss these things with your payroll processor and with your employees.

Employee financial management also has legal implications. You must pay your employee correctly depending on their **W2** or **1099** status, and you are required to store data correctly. If you don't give a required break, an employee could file a lawsuit against you; if you don't remit your payroll taxes correctly, you could receive a tax notice or a lien against your business.

Some bookstore owners are their own, sole employee; other bookstore owners have hired more employees to help them, either as actual employees or as contractors. Whatever your situation, this chapter will help you navigate the financial aspects of staffing the store.

## 6.2 WAGES & BENEFITS

When managing payroll, it's important to understand employee classification, the types of wages and benefits you can offer, how often you should run payroll, and how employees should track their time.

### 6.2.1 EMPLOYEE CLASSIFICATION

Employee classifications identify employee requirements set by the **Fair Labor Standards Act (FLSA)** and determine the benefits they receive. You may have heard the terms "full-time" and "part-time" before, but there are even more employee classifications that involve jobs that offer varying compensation, duration, and work hours.

#### Employee vs Independent Contractor

**Employees (W2)** are usually classified according to the hours worked and the responsibilities of the job. All employees are eligible to pay payroll taxes and receive worker's compensation, unemployment compensation, and benefits if they work over a certain amount of hours. Generally, employees fall into two categories: exempt and non-exempt. **Exempt employees** are not entitled to overtime pay, as they are exempt from the Fair Labor Standards Act's (FLSA) overtime regulations. Non-exempt employees are just that - not exempt from FLSA regulations, therefore, they must be paid overtime.

Exempt employees must earn the minimum weekly amount set by FLSA, which changes by the year. In 2023, the amount was $684 per week. Typically, exempt employees are in a salaried, managerial position.

**Non-exempt employees** are required to be paid minimum wage and overtime (they are usually paid by the hour). These are usually hourly employees who are directly supervised by a manager who controls the workflow.

**Independent Contractors (1099)** are non-employee workers who typically perform specialized work and are retained for a specific period of time or project. This means that 1099 contractors can't perform tasks that need to be supervised or directed. As a client, you can't set their hours or tell them how a task should be accomplished. You give general guidance and a deadline, and they do the task in whatever way they see fit. As a client, you're concerned about the result of the work, but not the means by which it's accomplished. Independent contractors' pay information is summarized annually on a **1099 form**. The criteria for independent contractors is:

- The worker is not under the control of the employer for the performance of work.
- The work must not be within the usual course of the employer's business. An example of this would be a social media manager or a website designer.

Independent contractors are not considered employees of the organization, which means these workers are not covered by the laws for minimum wage and overtime, payroll taxes, workers' compensation, unemployment compensation, or employment discrimination.

## 6.2.2 TYPES OF WAGES & BENEFITS

There are regular hourly wages and salaries, then a few types of wages and benefits outside of regular employee wages, including bonus pay and overtime pay. For benefits, there are retirement plans, paid time off, health benefits, and other benefits such as family leave.

### Bonuses and Overtime

An **employee bonus** is pay awarded in addition to the employee's regular salary or hourly wage. In most cases, employees earn bonus pay as an award for excellent work or as an end-of-year reward. Other types of bonuses include sign-on bonuses or sales milestones bonuses.

Non-exempt employees must be paid overtime for any hours they work over 40 hours per week. Overtime is at minimum time and a half the employee's usual hourly rate. You can calculate this by taking the usual hourly rate and multiplying it by 1.5.

Example: $15/hour x 1.5 = $22.50/hour x (the # of hours over 40 worked)

### Retirement Plans

**Retirement plans** as a benefit are not mandated by law in many states, but the number of states with mandated retirement plans is growing. Seventeen states that we're aware of have passed laws regarding a mandated retirement program:

- California
- Colorado
- Connecticut
- Illinois
- Maine
- Maryland
- New Jersey
- New York
- Oregon
- Virginia
- Hawaii
- New Mexico

- Washington
- Vermont
- Massachusetts
- Delaware
- Nevada

If your store operates in one of these states, you should check with your state department of labor about how to administer this benefit. Generally, if an employer does not already offer a retirement plan, they sign up with the state's plan as required. These usually do not require employers to match employees' contributions, but the plans do tend to boost retirement savings anyway, because they are often set up for auto-enrollment, and employees must opt-out of them rather than opt-in.

Even if a retirement plan is not mandated in your state, bookstore employees - and sometimes owners - are often barely scraping by, and it's pretty easy for bookstores to set up a retirement plan that will benefit all of you greatly in the long run, helping you retain your employees and working together with them to contribute to their better future. It's a feel-good partnership: employees set aside money out of their own paychecks, and as the employer, you can opt to match those contributions up to a certain level, helping them build their retirement nest egg.

If you are an owner of your business, say as a shareholder in an S-Corp, or a sole proprietor, you can participate too. There are two types of plans, a **401(K)** and a **SIMPLE IRA**. The rules are very different for these, but the principles are the same.

In either case, you should do further research on what works best for you and your business. There are many companies who can administer these plans and other benefits for you, or you can administer it yourself, setting up a plan directly with a fund company such as Calvert or Schwab.

The beauty of a SIMPLE IRA plan for a store owner is that owners can have a SIMPLE account for the business as well as a traditional, **individual IRA** or **Roth IRA** for themselves, and owners can contribute to both of these, giving them a much higher maximum allowed contribution each year.

Any reputable payroll system will be set up to handle a retirement plan benefit. You should be able to enter the set amount or percentage of each paycheck that your employee wishes to contribute to the plan, and in a separate line, enter the percentage of your employer match. These amounts will be tracked through the year and reported on the W2 for each employee. Since they are usually pre-tax deductions, these actually reduce the amount of taxable income for the employee, while simultaneously boosting their savings.

## Paid Time Off

Paid Time Off (PTO) is not required by federal law, however, it can go a long way in showing how much you appreciate your employees. The average PTO for a small business is 10 days. PTO is less common with hourly workplaces. It's usual to offer at least 2 paid weeks off per year for salaried employees, like full-time managers.

You could offer both full-time and part-time employees PTO at a rate of two-hundredths of an hour (.02) for each hour worked for sick leave and four-hundredths of an hour (.04) for personal leave and vacation. For a full time employee working 40 hours a week for 50 weeks a year, that adds up to 40 hours per year of paid sick leave and another 80 hours per year of paid vacation and personal time. Again, any reputable payroll system has the capability of tracking this for you, so that's a feature to look for when setting up your payroll processing.

## Health Insurance/Other Health Benefits

In this society where healthcare costs can bankrupt anyone, we should do anything we can to protect ourselves and our employees from that catastrophe. Health insurance or other health benefits are a way we can do this.

According to the **Affordable Care Act**, also known as ACA, only applicable large employers — or employers with at least 50 full-time employees — are subject to the employer mandate to provide health insurance coverage for employees. Although most stores are not that big, offering some kind of health benefit can help you retain the employees you've worked so hard to train. Hopefully, it will also help you and your employees stay healthy and reduce everyone's stress, which can help the business run more smoothly.

There are different ways of offering health benefits. The ABA's partnership with LIG Solutions allows ABA members to gain access to LIG's extensive knowledge of the health insurance market, which will help members navigate a wide array of insurance options. You can find out more about this at the ABA's website: https://www.bookweb.org.

Some stores offer accident plans from companies such as AFLAC.

There is a new option available in some areas for employers to offer primary care for their employees and their dependents and household members at an amazingly low monthly fee per employee. One example of this is called NICE healthcare. In some higher density population areas, you can actually get house calls from real medical providers from NICE. In other areas, the coverage is remote only for now; but believe it or not, you can even get physical therapy treatment remotely. Companies like NICE focus on primary care, mental health care, prescription drug benefits (many common drugs are free through the plan), and physical therapy - things that are important, but sometimes hard to access.

Another way of handling health benefits is simply to offer some support for your employees' health insurance premiums, if they are getting their own health insurance outside of your business. If you go this route, be sure to check with your accountant about how those expenses need to be coded in your books and handled on your employees' W2s. Store owners who are employees can have their own health coverage as a business expense paid by the store, and in that case, the amount paid for that coverage is included in a separate box on the W2. Most benefits for

employees, however, are not included on their W2s and are not taxable income, nor will they make payroll taxes higher.

Even if you can't offer a traditional group health plan to your employees, you have options. Basically, any type of health benefit where you reimburse your employees for certain types of expenses they incur are called a **health reimbursement arrangement**, or HRA. An HRA is an IRS-approved, employer-funded health benefit used to reimburse employees, tax-free, for their healthcare expenses, including health insurance premiums, out-of-pocket medical expenses, or a combination of the two. You can reimburse employees for all kinds of expenses, up to a certain amount per month, including things like acupuncture, over-the-counter remedies, and massage. You can reimburse your employees for many things their regular insurance probably doesn't cover, and this does not increase your payroll taxes or your employee's income. You can find more information on health reimbursement arrangements at the Additional Resources link in the **Templates & Resources** section.

### Other Benefits

Besides what is listed above, there are a couple of other benefits worth considering. The first is family or parental leave. Whether it is mandatory to offer parental or family leave to your employees depends on the size of your company and the state you operate in, so you'll need to look up how it applies to your business. There is too much labor law information to cover fully in this chapter, so please refer to the Additional Resources link in the **Templates & Resources** section for more information.

Secondly, if you're a caring and creative employer, there are many benefits you can provide to your employees that will help them feel valued and also help stretch their paycheck without increasing your payroll taxes. These include meal allowances, employee discounts, birthday gift cards, and others.

## 6.2.3 PAYROLL FREQUENCY

If you're in charge of your store finances, you probably make the decision on payroll frequency, or how often employees get paid. The most typical frequencies are semi-monthly or bi-weekly. **Semi-monthly** is when you pay your employees twice a month on specific dates, for example, if the pay period goes from the 1st through the 15th of the month with a paycheck coming on the 20th, then again from the 16th to the last day of the month with a paycheck coming on the 5th. This semi-monthly schedule results in 24 paychecks in a year.

**Bi-weekly** is paying your employees every two weeks, usually on a Friday. This results in 26 paychecks per year, and assuming the schedule stays the same, bi-weekly payroll results in paychecks that are more or less the same throughout the year, since the pay period is the same number of days each time. There is more variability with semi-monthly, since the number of days in the month differs.

Each state has different laws about payroll frequency, and some industries pay weekly

and some monthly, so check what your state requires, and if you don't already have a payroll schedule established, or are thinking about modifying your current one, talk it over with your bookkeeper or accountant to determine what will work best for you. Some payroll services charge you per payroll, so changing to a more frequent schedule could be more expensive. If you are running payroll yourself, for instance, using Quickbooks Online Payroll or Homebase or something else, you can make the decision on your own after consulting state laws.

Keep in mind that whatever you choose, it's going to be a pain to change once you've gotten it established, so make sure you're happy with it from the start! From your own working life, you might have a good idea about what payroll frequency you think is preferable. If you decide you'd like to change, we recommend changing at the start of a new fiscal year.

### 6.2.4 TIME TRACKING

You must have a system for tracking your employees' hours worked so when it is time to run payroll, you'll know what to enter. It should be accurate and easy to use, as well as difficult to fudge. There are a couple of ways to do this.

If you're not yet ready to commit to an electronic solution, set up a paper timesheet for your pay periods and keep them on a clipboard where employees can access them easily. Employees enter the date, start time, and departure time, then add it up at the end of the pay period. You will probably want to double check their math and pay attention to make sure they are entering times whenever they arrive, take breaks, and leave. It's easy to fudge if they enter times later on, when they forget about having been late or having been too busy to take a lunch break.

One example of an online-based time tracking system is Homebase, where employees can clock in on a store computer or from their own phone. It also has a lot of handy features, such as employee scheduling and new employee self-on-boarding, where employees can submit their own **W-4** and **I-9** and direct deposit information, not to mention payroll and human resources capabilities. There are more examples of time tracking resources listed at the Additional Resources link in the **Templates & Resources** section.

## 6.3 TAXES & COMPLIANCE

Taxes can be a big subject; there are a lot of regulations and requirements. Even if you use a separate payroll company, it's important to note that employers are responsible for making sure that employees are paid on time and for making sure that the payroll company is paying payroll taxes and submitting forms on time and correctly.

Human Resources compliance is the work of ensuring your employment practices conform to federal, state, and local laws. This work requires learning which laws apply to your organization and understanding what they require you to do.

### 6.3.1 PAYROLL TAXES

Payroll taxes break down into two categories: employer contributions and employee contributions. On the employer side is state and federal unemployment taxes. Both the employer and the employee pay equally for Medicare and Social Security taxes, and employees have to pay state and federal taxes, which you withhold from their paychecks and remit for them throughout the year. Fortunately, if you have a paid payroll service, once you set up your payroll settings, these will be handled automatically. However, you do have to update your state unemployment tax rates on an annual basis.

### 6.3.2 PAYROLL TAX REMITTANCE

Employers must file a variety of tax returns related to employment taxes. A payroll company is a great resource to submit taxes on your business's behalf, but it is your responsibility to make sure the information you provide them is accurate, including the remittance schedule and account information. It is normally part of any payroll company onboarding process to obtain all your federal and state account numbers as well as your bank account info. You can view how to register for your specific state tax agencies at the Additional Resources link in the **Templates & Resources** section.

We recommend monitoring your EFTPS.gov (Electronic Federal Tax Payment System) account to make sure your payroll provider is doing it correctly; you're still liable for those tax remittances even if your payroll company is doing them on your behalf.

Common federal tax forms include:

- **Form 940**, which is an employer's annual **Federal Unemployment Tax (FUTA)** tax return.
- **Form 941**, which is an employer's quarterly tax return reporting withholding and the employer's share of **Federal Insurance Contributions Act (FICA)**, social security, and Medicare.
- **Form 944** for small employers eligible to pay employment taxes annually rather than depositing them according to a schedule.

When you receive these forms, it's your responsibility to give this information to your payroll company. The information found on the forms will include your unemployment tax rate, how often you have to file payroll taxes, and your account number. For example, **FICA**, **FUTA**, and **State Unemployment Tax (SUTA)** are remitted according to the schedule assigned on the 941 or 944 form. It's different for every business depending on how much you pay in payroll and the kind of business you are.

For employees, there are two main federal forms you'll need: the **W-4** and the **I-9**. The **W-4** gives you all the personal information you need for the employee and lets you know how their tax withholding should be handled for payroll. The **I-9** documents that the employee is eligible to work in the United States. Keep these on file; some payroll platforms let you store them electronically. If you keep physical forms, be sure they are kept in a secure, locked place. Sensitive personal info will be on them that you need to safeguard.

## 6.3.3 EMPLOYER CONTRIBUTIONS

Employer contributions refers to money an employer pays into a compensation package for their employees or to taxes employers pay to fund social programs. The following are types of employer contributions.

### Federal Unemployment Tax (FUTA)

If you spend $1,500 per quarter on wages, you are required to pay FUTA which is 6% for the first $7,000 of an employee's wages per year.

**REAL-LIFE SCENARIO**

An employee is paid $17/hour and they work 30 hours per pay period. They are being paid $510 per pay period in gross wages. The employer will pay 6%, which is $30.60, until the employee reaches $7,000 in gross wages, which will take 14 pay periods. Thus, as an employer, you will pay $30.60 per pay period for 14 pay periods per year for this employee.

### State Unemployment Tax (SUTA)

Depending on the state, SUTA is anywhere from 2-5% of the employee's wages.

### Federal Insurance Contributions Act (FICA), Social Security, & Medicare

Social Security is 6.2% of gross compensation up to the Social Security wage base limit of $147,000. Medicare is 1.45% of the employee's gross compensation and has no wage-based limit.

It's possible that you have other state-specific taxes, such as paid family leave, so be sure to check your state laws.

## 6.3.4 EMPLOYEE CONTRIBUTIONS

Employee contributions are payments made by employees into a compensation package. This money is typically withheld by the employer. The following are types of employee contributions.

### Federal Insurance Contributions Act (FICA), Social Security, & Medicare

FICA is shared between the employer and the employee, so the employee contribution is the same as the employer.

Social Security is 6.2% of gross compensation up to the Social Security wage base limit of $147,000. Medicare is 1.45% of the employee's gross compensation and has no wage-based limit.

### State Income Tax (SIT) & Federal Income Tax (FIT)

Depending on their income bracket, the employee is required to pay a percentage of

their taxable income to income tax. The information provided by your employee on their W-4 form will determine how much is withheld from their paycheck for these taxes, and you will then remit those withholdings to the state and federal government on a regular basis as required.

As with employer contributions, other state-specific taxes may apply.

## 6.4 PAYROLL & PROFITABILITY

It's important to view payroll as an investment, as having staff allows you as the owner or manager to focus on things that can increase profitability. In this section is information on how much you should try to invest in payroll, how you can begin to determine wages and salaries, and paying yourself as a store owner.

### 6.4.1 HOW MUCH CAN YOU AFFORD TO INVEST?

**ABACUS**, the survey covered in Chapter Four, recommends that payroll, including owner wages, employer taxes, benefits, etc. should be between 20-25% of **Net Revenue**. For a quick example, if your net revenue is around $100,000, you should aim for a payroll investment between $20,000-25,000.

Your job as an owner or manager is to evaluate what you can afford to invest and what level of skill you are looking for. There are many factors involved in evaluating job candidates and being a good employer that are beyond the scope of this financial course, but that are covered in the Store & Operations Management course.

When you're ready to bring in more help, whether it's regular W2 employees or 1099 contractors, make sure you know exactly how much money you can invest in new employees, including the cost of your time to train them. We can't control very much in our business, but we do have total control over how many employees we hire and how many hours per week they work.

Hiring employees is truly an investment in your business and a way to grow sales. Adding staff might let you expand your hours, attract new customers, take part in offsite sales opportunities, or add needed marketing skills. If adding a staff member takes you over that ideal figure of 20-25% for a while, don't despair. Just monitor the situation and watch to see if your extra capacity helps your sales grow accordingly, as it should.

### 6.4.2 DETERMINING WAGES & SALARIES

Determining wages and salaries is location specific and can vary hugely depending on whether you are in rural Iowa or metro New York City. When you are trying to determine what hourly wage at which to start your new employees, look at job postings for similar positions in your area. If you have other business-owning friends, ask them about their pay rates. And avail yourself of the myriad of websites with this sort of data, such as livingwage.mit.edu, which will tell you what a living wage is in your area.

Offering a living wage is something to always consider, along with what will make a promising hire thinking about continuing in the job for the long term. Do you only hire college students who will be moving on in a year? Do you hire parents who can work mornings and the middle of the day but need to leave by 2:30PM and have to call in when their child is home sick from school? Do you hire retired teachers who are ready for something less stressful than being in the classroom and are reliable and knowledgeable? The wage expectations for each of these folks may be different.

If you hire someone you want to keep and who is interested in staying, you're going to have to make their wages and benefits competitive with other positions elsewhere they may consider taking instead. Or, perhaps employees will be willing to work for less if the flexibility you offer for unpaid time off or starting or leaving early or late depending on the school schedule makes it a more attractive workplace than something more rigid. If you're the manager or owner, don't be afraid to have those conversations with your employees. The easier you make it for staff to communicate with you about wage and benefit issues, the more information you'll have for making decisions.

Another way to look at determining salaries is by implementing business wide salary bands, or standardized wages. This means each role in the bookstore gets paid the same. For example, every bookseller is paid the same, event staff is paid the same, managers are paid the same, etc. Standardizing wages can be more equitable and result in lower turnover, which in turn lowers payroll costs.

### 6.4.3 PAYING YOURSELF AS AN OWNER

To determine whether your store is profitable, and in the long run, sustainable, you need to include owner compensation in your store expenses. Some owners have the luxury of having income from other sources and don't need to pay themselves a wage, and for others, the bookstore absolutely has to pay them, along with providing benefits such as healthcare. The New Bookstore Burning Questions section under Dig Deeper in Chapter Four, Working With ABACUS, addresses in detail how owners can determine whether or not their store is ready to pay them. Take a close look at that section if you are not yet getting paid by your store but would like to be paid at some point.

There are a couple of ways for owners to be compensated depending on the underlying structure of your business. Sole proprietors and members of an LLC take **owner draws**. You should check with your accountant about how to handle your owner compensation.

## SUMMARY

**Why It Matters**

You need to be able to make decisions about pay and benefits and discuss these things with your payroll processor and with your employees. You also need to be able to answer your employees' questions about their checks and their taxes. Employee financial management has legal implications, and the money you spend on payroll is an investment, so it's important to ensure the return on that investment is healthy and you are investing intelligently.

**6.1 The Basics**

Staff financial management has legal implications. You must pay your employee correctly depending on their W2 or 1099 status, and you are required to store data correctly. Some bookstore owners are their own, sole employee; other bookstore owners have hired more employees to help them, either as actual employees or as contractors. Whatever your situation, this chapter will help you navigate the financial aspects of staffing the store.

**6.2.1 Employee Classification**

**Employees (W2)** are usually classified according to the hours worked and the responsibilities of the job. All employees are eligible to pay payroll taxes and receive worker's compensation, unemployment compensation, and benefits if they work over a certain amount of hours. Generally, employees fall into two categories: **exempt** and **non-exempt**.

**Independent Contractors (1099)** are non-employee workers who typically perform specialized work and are retained for a specific period of time or project.

**6.2.2 Types of Wages & Benefits**

There are regular hourly wages and salaries, then a few types of wages and benefits outside of regular employee wages, including bonus pay and overtime pay. For benefits, there are retirement plans, paid time off, health benefits, and other benefits such as family leave.

An **employee bonus** is pay awarded in addition to the employee's regular salary or hourly wage. **Retirement plans** as a benefit are not mandated by law in many states, but the number of states with mandated retirement plans is growing. **Paid Time Off (PTO)** is not required by federal law, however, it can go a long way in showing how much you appreciate your employees. The average PTO for a small business is 10 days.

According to the **Affordable Care Act**, also known as ACA, only applicable large employers — or employers with at least 50 full-time employees — are subject to the employer mandate to provide health insurance coverage for employees. Although most stores are not that big, offering some kind of health benefit can help you retain the employees you've worked so hard to train.

### 6.2.3 Payroll Frequency

**Semi-monthly** is when you pay your employees twice a month on specific dates. This results in 24 paychecks per year. **Bi-weekly** is paying your employees every two weeks, usually on a Friday. This results in 26 paychecks per year. Each state has different laws about payroll frequency, so check your state laws.

### 6.2.4 Time Tracking

You must have a system for tracking your employees' hours worked so when it is time to run payroll, you'll know what to enter. It should be accurate and easy to use, as well as difficult to fudge.

### 6.3.1 Payroll Taxes

Payroll taxes include employer contributions and employee contributions. On the employer side is state and federal unemployment taxes. Both the employer and the employee pay equally for Medicare and Social Security taxes, and employees have to pay state and federal taxes, which you withhold from their paychecks and remit for them throughout the year. If you have a paid payroll service, once you set up your payroll settings, these will be handled automatically. However, you do have to update your state unemployment tax rates on an annual basis.

### 6.3.2 Payroll Tax Remittance

Employers must file a variety of tax returns related to employment taxes. A payroll company is a great resource to submit taxes on your business's behalf, but it is your responsibility to make sure the information you provide them is accurate, including the remittance schedule and account information. Common federal tax forms include:

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- **Form 944** for small employers eligible to pay employment taxes annually rather than depositing them according to a schedule.

### 6.4.1 How Much Can You Afford to Invest?

**ABACUS**, the survey covered in Chapter Four, recommends that payroll, including owner wages, employer taxes, benefits, etc. should be between 20-25% of **Net Revenue**. If adding a staff member takes you over that ideal figure of 20-25% for a while, don't despair. Just monitor the situation and watch to see if your extra capacity helps your sales grow accordingly, as it should.

### 6.4.2 Determining Wages & Salaries

When you are trying to determine what hourly wage at which to start your new employees, look at job postings for similar positions in your area. If you have other business-owning friends, ask them about their pay rates. And avail yourself of the myriad of websites with this sort of data, such as livingwage.mit.edu, which will tell you what a living wage is in your area.

Another way to look at determining salaries is by implementing business wide salary bands, or standardized wages. This means each role in the bookstore gets paid the same. Standardizing wages can be more equitable and result in lower turnover, which in turn lowers payroll costs.

### 6.4.3 Paying Yourself As An Owner

To determine whether your store is profitable and sustainable, you need to include owner compensation in your store expenses. Some owners have income from other sources and don't need to pay themselves a wage, and for others, the bookstore has to pay them, along with providing benefits such as healthcare. The New Bookstore Burning Questions section under Dig Deeper in Chapter Four addresses in detail how owners can determine whether or not their store is ready to pay them. Take a close look at that section if you are not yet getting paid by your store but would like to be paid at some point.

## KEY TAKEAWAYS

- Staff financial management has serious legal implications.
- Employers must file a variety of tax returns, including Forms 940, 941, and 944.
- W2 Employees are eligible to pay payroll taxes and receive worker's compensation, unemployment compensation, and benefits; whereas 1099 Independent Contractors are non-employees who are not eligible for the above.
- ABACUS recommends that payroll, including owner wages, employer taxes, benefits, etc. should be between 20-25% of net revenue.

## TEMPLATES & RESOURCES

- **Resource**: Additional Staff Financial Management Resources

## KEY TERMS

- 401(K)
- ABACUS
- Affordable Care Act (ACA)
- Bi-Weekly
- Employee (W2)
- Employee Bonus
- Exempt
- Fair Labor Standards Act (FLSA)
- Federal Income Tax (FIT)
- Federal Insurance Contributions Act (FICA)
- Form 940, 941, 944
- Health Reimbursement Arrangement (HRA)
- I-9
- Independent Contractor (1099)
- Individual IRA
- Net Revenue
- Non-Exempt
- Owner Draw
- Retirement Plan
- Roth IRA
- Semi-Monthly
- SIMPLE IRA
- State Income Tax (SIT)
- State Unemployment Tax (SUTA)
- W-2, W-4

## REVIEW QUESTIONS

**Multiple Choice:**
What should your percentage of payroll costs be of your net revenue if you want to be in line with the average store according to ABACUS?

A. 15-20%
B. 20-25%
C. 25-30%

**Short Answer:** What is 1 benefit that doesn't increase your payroll taxes that you do or want to offer to your employees?

## ANSWER KEY

- B
- All correct: health reimbursement arrangement (HRA), meal allowance, primary care through a company such as NICE, employee discount

DIG DEEPER

## COLLECTING AND STORING EMPLOYEE DATA

**I-9 and W-4 files**: You need to keep a record of all employee forms, applications, and any accompanying ID documents for three years after hire or one year following termination.

**Background Checks**: Pre-Employment testing results and background check documents must be kept for one year following employment termination. This includes credit checks, criminal history, driving records, consent forms, and any other form of background check.

**Employment Offers and Contracts**: All employment offers and contracts must be kept for one year following employment termination (although your state may have a different requirement). This includes recruitment and hiring records, job applications, resumes, advertisements about job openings, screening tools, interview notes, and records about hiring decisions.

**Medical Records**: You must retain an employee's medical records for three years following termination. This includes all Family Medical Leave Records, payroll and identifying employee data, occupation, rate of pay, dates taken, hours of leave, copies of notices, documents describing benefits or policies, premium payments, and any disputes.

**Payroll Records**: You need to keep a record of all payroll information for three years. This includes an employee's name, address, social security number, gender, date of birth, occupation, job classification, daily schedules, pay rate, weekly compensation, amounts and dates of payments, daily and weekly hours, overtime hours and pay, annuity and pension payments, benefits, deductions and additions, and pay period dates. You also need to keep a written explanation of variance in pay between genders for two years following termination.

**Employee Tax Records**: You need to keep a record of all tax documentation for a period of four years from the date tax was due or paid. This includes your EIN, together with a record of all payments, tips, in-kind wages, personal information, undeliverable W-2s, dates of employment, PTO, income tax withholding allowance certificates, dates, and amounts of tax deposits, returns filed, and fringe benefits.

## DIG DEEPER

**Health & Safety Records**: Finally, you need to keep a record of all health and safety records for a period of five years after termination. This includes job-related injury records such as logs and summaries of work-related injuries and illnesses. What's more, if one of your employees is exposed to a toxic substance, you must keep a record of all medical exams and safety data sheets for 30 years after termination.

*Chapter 7*

# Accounting Basics

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Speak to your accountant in their own language.
- Develop an accounting task schedule.

## WHY THIS MATTERS

Accounting is important for making business decisions and legal/tax obligations and is a key part of business plans, growth projections, and loan applications. This information helps to communicate and establish credibility with lenders and helps ensure accurate reporting to the IRS. In short, accounting is important for three major reasons:

1. It allows you to evaluate your store's performance, allocate your budget, and compare data across time.
2. It ensures legal compliance and proper reporting to the IRS and that liabilities such as sales tax, income tax, and payroll tax and withholdings, to name a few, are appropriately addressed.
3. It helps you create future projections and analyze trends to keep your operations profitable.

## CHAPTER OUTLINE

**7.1** The Basics
**7.2** Why is Accounting Intimidating?
**7.3** Who Can Help?
  **7.3.1** Accountant vs CPA
**7.4** Accounting Workflow
**7.5** Cash vs Accrual vs Modified Cash Accounting
**7.6** How to Calculate Cost of Goods Sold (COGS)
  **7.6.1** Average vs Specific Cost
**7.7** Accounting Software
**7.8** Who Does Your Bookkeeping?
**7.9** Backups & Document Retention Systems
**7.10** Getting Into a Financial Rhythm
**7.11** Meeting With Your Tax Professional
**7.12** Introduction to Classic Financial Statements
**7.13** Initial Accounting Decisions
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Debits & Credits and Double Entry Accounting

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## 7.1 THE BASICS

**Accounting** is a language that provides information about the financial health of your business. You learn the language by learning to track daily business operations (payroll, gift card sales, invoices) in your accounting software. If those daily operating records are done properly, you'll then have the financial information you need for reports you need to prepare for outsiders (the IRS, shareholders, banks, the public, creditors, etc.) and information for the business's managers to plan for the future (through financial plans, budgets, analyses, etc.) and/or make adjustments to reflect changing conditions.

Accounting is basically just tracking where your money is going. It's important to record your financial transactions so you can generate an overall picture of your store's financial health and so you can analyze those transactions to better understand your financial situation. Up-to-date records of your business transactions also help you compare historical data to current data so you can assess your performance over time.

## 7.2 WHY IS ACCOUNTING INTIMIDATING?

Accounting is intimidating and confusing. Accounting also has unfamiliar jargon/terminology that is sometimes difficult to understand. And the fear of math and getting your numbers wrong is very real, because if you get the numbers wrong, there could be legal and/or tax consequences for those mistakes. What if the IRS comes knocking and something is incorrect? That is really scary!

Accounting also requires specific software, and it can be intimidating to learn something new. It's also a big time commitment, especially if you do all your own bookkeeping.

With accounting, you're also serving two masters - your own business and the IRS - and sometimes those two things conflict. And let's face it, if you're not a numbers person, accounting can be boring.

It's important to remember that you don't realize it, but you use accounting every day in your personal life. When you buy a cup of coffee, for example, you exchange money, via cash, debit, or credit, in exchange for your beverage. The coffee shop receives the cash and provides you with a yummy drink. That is accounting.

## 7.3 WHO CAN HELP?

There are several types of finance professionals you can hire based on your needs.

### Bookkeeper

**Bookkeepers** are professionally trained on using accounting software and can help with financial recordkeeping. Bookkeepers are responsible for providing accurate, up-to-date financial reports and information. Most often, their reports go to owners and managers to help them make decisions. Essentially, a bookkeeper keeps your official financial records. You can be your own bookkeeper, train an employee, or hire a **1099** contractor.

### Tax Professional

A **tax professional** prepares, calculates, and files income tax returns on behalf of individuals and businesses. There are several different types of tax preparers, with some having credentials issued by third-party organizations while others are non-credentialed. This person can be an **accountant**, a **Certified Public Accountant (CPA)**, or an **Enrolled Agent**. CPAs and Enrolled Agents can also represent you during an IRS audit.

Essentially, tax professionals help clients file their taxes and ensure the accuracy of tax forms. They prepare their clients to be able to pay any needed fees and review financial records. They also calculate tax returns, and manage communication between clients and tax authorities. It's possible to just use something like TurboTax for this; however, we highly suggest staying away from that, as small businesses are often complicated, and tax professionals can ensure your filings are accurate and that you're getting all you can back from the IRS.

### Business Advisor

A **business advisor** helps you make business financial decisions, interpret your financial data, etc. This could be a mentor, coach, accountant, or a Chief Financial Officer. They are typically responsible for planning and executing business strategies to improve efficiency in operations and financial management of businesses. They prepare budgets, advise on projects and marketing, and perform risk analysis.

### Payroll Company

Payroll companies are tools businesses can utilize to assist in paying employees and remitting payroll taxes. This arrangement is often beneficial for employers to save time. Payroll companies may also help with human resources and employee benefits. Although employers are ultimately responsible for paying employees on time and remitting payroll taxes and forms on time and correctly, hiring a payroll company can help with this process.

## 7.3.1 ACCOUNTANT VS CPA

One thing to note when working with financial professionals is that accountants and **certified public accountants (CPAs)** aren't necessarily the same. While it may seem that people use these terms interchangeably, all CPAs are accountants, but not all accountants are CPAs.

**Accountants**

- Have at least a Bachelor's degree in accounting. They are educated on the subject, but not necessarily professionally certified.
- Cannot represent you in an IRS audit.
- Do not necessarily have requirements for continuing education.
- Qualified to manage day-to-day financial activity, such as reconciling accounts, analyzing financial statements, and preparing budgets.
- No governing body that requires them to stick to certain ethics (no oversight).

**Certified Public Accountants (CPAs)**

- Licensed by a professional governing body.
- Required to undergo continuing education to maintain their license.
- Held to more stringent standards than unlicensed accountants, and expected to abide by the code of conduct of the Association of International Certified Professional Accountants.
- Held to a fiduciary standard, which means they must put their clients' interests above all else.
- Can prepare audited financial statements, as required by the SEC for public companies.
- If selling your business, the buyer may require an external audit by a CPA.
- Can represent you in an IRS audit (Enrolled Agents can also represent you in an audit).

Professional oversight and an extra certification are the key differences between an accountant and a CPA. Because of the extra standards, a CPA will cost you more than an unlicensed accountant. Small businesses don't necessarily need a CPA. Fun fact: Only about 50% of accountants in the US are actively licensed CPAs.

## 7.4 ACCOUNTING WORKFLOW

Let's walk through the workflow of what actually happens in accounting when you make a financial transaction, which can include depositing cash, writing a check/paying a bill, taking out a loan, etc.

**A financial transaction is made.**
Once made, you enter that transaction into your accounting register for the affected financial account. This means you record the money flowing into or out of your bank account.

**The transaction is linked to a category.**
Next, you need to link the transaction to a category from your **Chart of Accounts**, such as inventory for a vendor payment or utilities for an electric bill payment. Then you're done! Congratulations, you have done Double Entry accounting!

Chapter 8: Bookkeeping for Booksellers will go into great detail about how to categorize your transactions in your Chart of Accounts. You can succeed at double entry accounting even if you never learn the difference between debits and credits. In fact, modern accounting software generally hides the behind-the-scenes details of debits and credits, so they are not something you have to use every day. The good thing is that if you enter something incorrectly (like as a debit when it's supposed to be a credit or vice versa), checking the balance on that account/category will immediately tell you that the numbers are wrong, and you can just switch them.

If you'd like to dive deeper into debits and credits, see the Dig Deeper section at the end of this chapter.

## 7.5 CASH VS ACCRUAL VS MODIFIED CASH ACCOUNTING

An accounting decision the IRS asks you to make with your first business tax return is whether you will use cash basis accounting or accrual. The difference between the two is timing. In **cash accounting**, you record **revenue** and **expenses** when you pay or receive money. With **accrual accounting**, you make a record when you receive a bill or send an invoice regardless of when it actually gets paid.

The term "cash" in cash accounting means payment, not literal cash. Thus, in cash accounting you usually record expenses paid by credit card when your card is charged, not when you actually pay your monthly credit card bill.

Cash accounting usually makes sense to people, as it's just like keeping a check register or looking at your online bank statement. In cash accounting, you aren't required to keep track of accounts receivable and payable in your accounting records because you don't owe tax on any sales until you receive payment for it and you aren't allowed to deduct any expenses until you actually pay them.

Accrual accounting requires more work and may seem a little more mystifying, but it actually gives you a better financial picture of your business's cash flow as it helps remind you about those customers who owe you money and about big bills you may have coming due soon. The purpose of accrual is to try to record income in the period in which it was earned and expenses in the period in which they were spent, regardless of when the money exchanges hands.

For example, do you ever extend terms to schools and deliver books to them with just a purchase order number as a promise of future payment? In accrual accounting, you would record that sale as income in the month you delivered the books, regardless of when the school actually paid you.

Accrual accounting also tends to smooth out the ups and down of your monthly profit and loss reports by taking expenses you may pay annually, like your liability insurance, and allocating a portion of that bill to each month's expenses, rather than have the whole amount show up in the month you were invoiced for it.

The IRS requires all inventory based businesses, such as bookstores, to use the accrual method when calculating inventory expense which is then referred to as **Cost of Goods Sold**.

However, if your business is under $25 million in sales, you can use cash accounting for everything else. This hybrid model is called **Modified Cash Accounting** and is what a lot of smaller bookstores use. Under this model, you record transactions related to long-term **assets** and inventory under the accrual method but use cash accounting for short-term assets and expenses. Over time as your business grows you may find that you adopt more and more elements of accrual

accounting and may eventually want to switch entirely, which requires you to file **Form 3115** with the IRS and could affect your tax owed for the year.

Keep in mind that if you're using Modified Cash Accounting, you may have to change back and forth between Cash and Accrual modes when you run various reports in your accounting software. Make sure you discuss this with your accountant.

## 7.6 HOW TO CALCULATE COST OF GOODS SOLD (COGS)

**Cost of Goods Sold (COGS)** refers to the cost of the inventory you sold during a specific period of time regardless of when you actually paid for the inventory. Another term for COGS is Cost of Sales. The two mean exactly the same thing. So how does one calculate the cost of only the inventory you sold during a period?

The official formula for retail businesses is that **COGS = Starting Inventory + Net Purchases - Ending Inventory**.

The formula above is from the **Schedule C** tax form used for a **sole proprietorship**. It has a few extra lines that would apply if you were a publisher or manufacturer who is actually producing the product but usually don't apply to straight retailers. However, it might if you actually make some of your own goods (like how some stores make candles).

It's really important that you and your tax advisor are on the same page about how you are calculating COGS, what data/reports you need to provide them, etc.

For tax purposes, COGS is a specific number, but a lot of times when you hear the term being used it's shorthand for a related figure: Cost of Goods Sold as a percentage of sales. Once you've calculated your COGS for a period, you simply divide it by your sales for the same period to get a percentage. For example, your accountant tells you that your COGS for the year was $50,000. If your sales for the year were $100,000, then your COGS percentage is 50%. But what if sales at full retail were $100,000 but you gave everyone a 10% discount and only took in $90,000 of income? In that case your COGS percentage would increase to 55.55%.

### 7.6.1 AVERAGE VS SPECIFIC COST

Traditionally, all the pieces of the COGS formula: starting inventory, ending inventory, and purchases, are calculated at cost. When calculating your starting and ending inventory costs, you can either use **specific cost** or **average cost**, but just like everything else tax-related, once you pick a method, you can't just change it on a whim.

Modern point of sale systems make the specific cost method possible. Under this method, you receive against your invoices and your POS tracks the cost of each individual item so when you run your starting and ending inventory reports, you get the cost of just the particular books remaining in inventory.

Before modern POS systems, the specific cost system required too much time, so average cost is also a legal method. With the average cost method, you estimate.

You would track the amounts spent on inventory and the quantity of books bought and sold, then calculate an average cost per book. You would then use the average cost to calculate your cost of goods sold.

Even though you are legally only required to calculate COGS at the end of your tax year, you should have discussions related to COGS at the beginning of the tax year so you make sure you are keeping all the required records.

If you have a good receiving system and remember to run your reports on time, then getting your starting and ending inventory at cost is pretty straightforward. **Net purchases**, though, is where smaller businesses tend to run into issues. This is because you are supposed to track all the invoices and return credits received during the period, not just the ones you paid. The book industry generates a LOT of invoices, and if you're a small one-person shop, you may not have the bandwidth to enter each individual one into your accounting software.

If you only order from one vendor or you prepay for all your inventory on a credit card, then tracking your purchases will be much easier than if you have a myriad of vendor accounts all with different terms. Hopefully, you got some good tips on how to manage the flood of invoices in Chapter 3: Vendor, Debt, & Tax Management.

Depending on your POS and how well you receive, you may be able to generate purchases and returns reports from within it. This is probably a good conversation for everyone to have with their tax advisor as soon as possible to make sure you are on the same page about how to calculate net purchases.

Given how complicated using the official formula for COGS is, many bookstores are tempted to simply use the calculated COGS presented by their POS system. However, you really need to discuss the pros and cons of this with your accountant, as the government may require you to have all three pieces of information (starting inventory, net purchases, and ending inventory), not just the already calculated figure.

## 7.7 ACCOUNTING SOFTWARE

Technically, accounting software is not absolutely required. You could get by with Excel if need be. However, we do not recommend presenting your tax professional with a box of receipts and paper statements. The amount they would charge you to sort through and categorize it all would be ruinous.

Free online software like Wave and Xero was designed for service businesses like coaches and consultants that do a lot of invoicing. You may be able to hack it to support a bookstore, but in general it is not recommended for retail, inventory based businesses.

If you have no previous bookkeeping experience, you usually need some help getting your books set up. If you've already found an accountant or a bookkeeper, then ask what software programs they are comfortable with and recommend. They may even be able to get you a deal on pricing. Most bookstores use Quickbooks Desktop, Quickbooks Online, or Sage. If you've ever

used Quicken to track your own personal expenses, then Quickbooks will feel very similar.

It is currently possible to stay on QuickBooks Desktop if you've been using it, but it looks like all entry-level bookkeeping software for new clients is moving into the cloud, and thus will incur a monthly fee in perpetuity.

## 7.8 WHO DOES YOUR BOOKKEEPING?

Startup owners usually either do all the bookkeeping or none of it, depending on your previous experience and the size of your business. Or if your business is a partnership, perhaps only one partner is responsible for the financial side.

However, we recommend that even if you don't enjoy bookkeeping or have the time to do it regularly, you at least take time to learn how to do it. There's a common acronym GIGO, which stands for Garbage In, Garbage Out. If your bookkeeping is not done correctly, your resulting financial reports are not going to be very reliable.

Even if you love bookkeeping, as your business starts to grow, owners should typically begin outsourcing some or all of the bookkeeping. You could train a **W2** employee to become a bookkeeper or you can hire an experienced bookkeeper as a **1099** contractor. Depending on your needs, a 1099 contractor may come into your business to work or work online. However you outsource, remember that you also need to design an oversight system to catch both simple mistakes as well as intentional embezzlement or fraud. Accountants usually refer to this oversight as financial controls, and they can be a great resource for you. Chapter 2: Daily Store Finance discussed some simple financial controls to implement.

## 7.9 BACKUPS & DOCUMENT RETENTION SYSTEMS

The next thing you need to consider in your accounting system is a backup system and document retention policy.

If you use online software, it is backed up automatically. But if you use Quickbooks Desktop or Excel, it's best to create a system to back it up to the cloud.

You should discuss federal and state document retention requirements with your accountant. The IRS requirements usually range from three to seven years, but records related to property may be much longer, and your state may have additional requirements.

If you accept credit cards, check with your merchant provider to see if and how long you need to retain copies of signed receipts and other documentation. Customers may have up to six months to dispute a transaction, so you need to keep the documentation until that window closes.

Some records you'll need in perpetuity, such as those documenting your business structure. In the case of an LLC, you need articles of organization and an operating agreement, which you have to present anytime you switch banks. If you ever want to apply for certification as a minority or woman-owned business, they usually ask for other startup

related documents, like proof of where your startup funds came from. You'll also want easy access to important business documents like your previous tax filings, your lease, loan documents, insurance policies, etc.

In this day and age, we recommend digitizing and organizing documents by year if possible. If you're not storing your digitized documents online, they also need to be backed up.

Even if you have current online access to documents like bank statements and payroll reports, you should get into the habit of downloading these each year then backing them up to your own cloud storage in case you switch vendors and lose access. Plus, banks only give you easy access to a few years worth of statements; after that, they charge you a record search fee. And after seven years, the records may be gone for good.

## 7.10 GETTING INTO A FINANCIAL RHYTHM

It will make accounting easier for you if you start to develop a rhythm for your store and create some checklists so nothing falls through the cracks. Each week, you or your staff will be doing the day-to-day financial tasks discussed in Chapter 2: Daily Store Finance of making bank deposits, reconciling credit card and website remittances, and placing change orders. In Chapter 8: Bookkeeping for Booksellers, you'll learn about keeping up with bookkeeping data entry. A senior staffer such as the owner, general manager, or Chief Financial Officer should monitor sales and cash flow, which will be discussed in Chapter 9: Cash Flow Deep Dive.

On a monthly basis, whoever is responsible for bookkeeping will finish up data entry, reconcile statements, close your books, and prepare monthly financial reports. Your bookkeeper may also pay bills, or you may reserve that right as the owner or manager. Your store may also need to remit monthly sales tax and payroll tax payments. You as the owner or manager should set time on your calendar to review your monthly financial reports, which should include a **profit & loss statement**, which we will deep dive into in Chapter 11.

On a quarterly basis, some owners may need to make estimated tax payments. Those stores with employees will need to file quarterly payroll forms and may need to make quarterly unemployment tax payments. Depending on your business, quarterly financial reports are often more meaningful than monthly ones, so put extra time to review these on your calendar at the end of each quarter.

We highly recommend meeting with your tax advisor at least twice a year. If you have a separate business coach or advisor, biannual meetings may also be useful there. If your tax filings are on a calendar year basis, then you'll usually meet with your tax advisor in the spring to discuss your upcoming tax filing and expectations for the next calendar year.

Prior to meeting your tax advisor, you may have already met with your business coach to create a plan and set those expectations for the next fiscal year. You may also want to

have a meeting with your tax advisor in late summer or early fall to check in about how sales are comparing to expectation and to discuss recent or prospective changes to the tax code and any odd bookkeeping question you may have. It may seem counterintuitive, but having a banner quarter is a strong sign that you should talk to your tax adviser sooner rather than later. The tax code is full of income-related brackets and cliffs that can jump your tax bill up an enormous amount, but with enough advance warning, a good tax advisor can help you navigate them. Whereas, having a weak quarter could be the trigger to call your business coach ASAP.

On an annual basis, you must produce year-end reports that include Cost of Goods Sold and file income tax in all applicable jurisdictions: federal, state if required, and possibly city. Your city or county may also require you to file a **business property tax** return and/or renew a business license. If you have employees you'll need to submit W2s and other annual payroll forms. 1099s may be required for contractors, landlords, accountants, and other services you pay by check or bank draft. If you are required to provide worker's comp insurance, you'll have an annual audit at some point in the year.

Many stores create annual budgets and sales projections, which you'll learn about in Chapter 12: Creating & Analyzing Your Budget. You should download yearly payroll provider reports and clean out any old company records you are no longer required to retain. Depending on how you calculate Cost of Goods Sold, you may be required to do an annual physical inventory, but it's a recommended practice even if not legally required. If you have company vehicles or drive your personal vehicle for business tasks other than commuting, you need to document the mileage of each vehicle at the start and end of your accounting year.

## 7.11 MEETING WITH YOUR TAX PROFESSIONAL

Your tax advisor usually makes more per hour than you do, so it pays to prepare well for your meetings so you get the best value out of them.

Before you e-mail your advisor a question, make sure you know whether they bill you for those or not.

You may find it useful to keep an open document of running questions and schedule a meeting when one of those questions turns urgent, or if you get an IRS notice, see a lot of variance up or down from the previous year, either in business income or in total family income, or if it's been at least six months since you last met.

Prior to the meeting, run your financial reports and send those to your advisor along with your questions as your "agenda." Or if you use online accounting software, you may be able to give your advisor access to your account.

We have included a sample agenda checklist in the **Templates & Resources** section.

## 7.12 INTRODUCTION TO CLASSIC FINANCIAL STATEMENTS

Publicly traded companies and those in regulated industries have to comply with GAAP (generally accepted accounting principles), but many large private businesses voluntarily comply as well. GAAP requires that companies produce three classic financial statements on a quarterly basis: a **Profit & Loss Statement**, a **Balance Sheet**, and a **Cash Flow Statement**.

We will deep dive into each of these in later chapters, but here's a brief introduction to each.

### Profit & Loss Statement

The **Profit & Loss Statement**, called a P&L for short, may also be called an Income Statement or Statement of Operations. It summarizes all the transactions in your Income, Expense, and Other Income/Expense categories from your Chart of Accounts over the reporting period. Theoretically, it shows whether your business is making a profit or losing money, but as you'll see in Chapter 11: Profit & Loss Deep Dive, there are nuances related to owner's pay and your business structure.

### Balance Sheet

The **Balance Sheet**, also called the Statement of Financial Position, summarizes the value of your Asset, Liability, and Equity categories in your Chart of Accounts as of a specific date. It shows what a business owns and owes. It's called a "balance sheet" because your total **assets** should exactly match, or be in balance with, the combined total of your **liabilities** and **equity**.

You may be familiar with the term equity from owning a house. Equity is the amount you'd realize after selling all your business assets and paying off all your business liabilities. With your house, your initial equity is your down payment, but if the market value of your house increases, your equity could grow. It can also shrink if you let your house fall into disrepair or your neighborhood goes to pot. The equity listed on your company balance sheet is an estimated amount. Whether you'd receive that amount or more from selling your business depends on too many factors to go into during this course, but usually the higher the equity, the better.

### Cash Flow Statement

Lastly is the **Cash Flow Statement**. Under GAAP, the first two reports are run on an accrual basis, and the Cash Flow Statement fills in the gaps to show how cash is entering and leaving a company. Cash is the lifeblood of a business. Many retail stores don't make their profits for the year until the fourth quarter. However, if you run out of cash to pay your rent and staff in July, potential fourth quarter profits don't really matter.

Even though most bookstores are not required to follow GAAP, these statements are important financial tools, and understanding them will increase your financial self-confidence as a business owner.

## 7.13 INITIAL ACCOUNTING DECISIONS

There are some initial accounting decisions you should have made when your store was founded; however, sometimes things slip through the cracks, or you may have needed to make some early decisions without full knowledge and now want to rethink them. The following are decisions every store needs to make regarding accounting and finances.

### Business Bank Accounts

Every business should have a separate business bank account. This is legally required if you have a DBA or have created your business as a separate entity (an LLC, partnership, or corporation) but is strongly recommended even for sole proprietorships.

The benefit of a separate account is to more easily separate your business and personal transactions for tax prep, to look more professional or legitimate (which can be important for pop-ups, bookmobiles, etc.), and to help establish business credit.

Depending on your model, you may use Square for your credit card processing, but most banks also offer what are called merchant accounts and are happy to set that up for you as a bundle with your business checking account. Having an official business checking account may in fact be a requirement for traditional merchant processors.

When shopping for banks, business owners are typically most concerned about convenience, fees, and minimum balance requirements. But during the pandemic, it became clear that relationships are just as important. The banks that got the best reviews during that period tended to be regional banks, who were more helpful to their small business customers than the big national banks. For more advice on building relationships with your bank, see the Dig Deeper section of Chapter 3: Vendor, Debt, & Tax Management.

Credit unions often have lower fees and minimums than banks, but they are geared toward personal banking and may not offer business accounts or only offer limited business services. Online banks may be a good place to keep a business savings account but are not recommended for your main business checking account if you're going to accept cash from customers.

Out of convenience, many owners open their business bank account at the same bank where they have their personal accounts. But just like with insurance, internet services, and your merchant account, it may be worth your while to shop around every so often for a better fit.

### Hiring a Tax Advisor/Accountant

Ideally, you want to start working with an accountant or tax advisor before you open your doors as they can help you decide on your business structure, explain tax implications of different choices you have (like whether to classify your startup capital as an investment or a loan to the business), and help

you find other advisors. Theoretically, you could do all your business tax filings yourself, but business accounting is usually intimidating enough that most owners want professional help with it.

Many business owners only meet with their accountant once a year for tax prep, but if you can find someone who can help you learn what you don't already know and is good at answering questions clearly, it's probably worth your time and money to meet with them more often, especially in the early days of your business or any time you're contemplating significant changes. And even if nothing changes in your business, the tax code can change wildly from year to year and can be hard for lay people to interpret.

The best way to find a good accountant is through other references. If you're in a big city with other bookstores, ask who they use. If you're the only bookstore in town, talk to other retail stores and to restaurants, since they also have to calculate cost of goods. Accountants may specialize just like anyone else and finding one with a roster of small business retail clients similar in size and scope to your store means they will already be familiar with common issues.

Also think about your current level of need and whether that is changing. As your business grows, you may need more services, such as bookkeeping help or financial planning. Or perhaps you want the safety net of a larger firm, rather than a single person who might get sick or retire. Or perhaps you started out with a CPA because of their extra credentials but now you can get by with a less expensive person.

Even once you find a reputable tax advisor, keep in mind that they depend on the accuracy of *your* records, and they can still make mistakes. It's your responsibility to oversee what they prepare, ask questions about anything you don't understand, and make sure nothing obvious seems off.

## Your Fiscal Year

Your business **fiscal year** is set by the first business tax return you file, so many people use the calendar year without realizing they may have had other options.

A sole proprietor reports their business income or loss on their owner's tax return, which is almost always the calendar year. A partnership or LLC must generally use the same tax year as the majority of its owners. An S corporation or a personal service corporation must generally use a calendar year. A C corporation that starts after January 1 can choose any 12-month period they want for their fiscal year or use the calendar year.

After you've filed your initial business tax return, you can only change your fiscal year with the IRS's permission by filing **Form 1128**, and you can typically only do this once every ten years. To change your fiscal year, you typically have to provide a business rationale other than avoiding tax.

For seasonal businesses, it makes sense that their accounting period should include the entire season. For a business like a ski resort, the calendar year would break the winter

skiing season into two fiscal years and require them to do inventory and other fiscal year end tasks right in the middle of their busiest time of year.

For other businesses, it may make business sense to change your fiscal year if associated expenses would fall in a different fiscal year than the income they produce. This is the main reason retail stores use a different year. If merchandise is non-returnable and must be put on sale to be cleared out, you may need time after the holiday season to run those sales. In this case, you'd want your fiscal year to end after those sales so your advertising and markdown expenses offset your non-markdown sales in the same fiscal year.

Some counties require businesses to pay business property tax based on their fiscal year-end inventory levels. Given this, you may want your fiscal year to end during a time of low inventory levels. However, that is not a valid "business reason" in the eyes of the IRS to change your fiscal year.

## SUMMARY

**Why It Matters**

**Accounting** is important for three major reasons:

1. It allows you to evaluate your store's performance, allocate your budget, and compare data across time.
2. It ensures legal compliance and proper reporting to the IRS and that liabilities such as sales tax, income tax, and payroll tax and withholdings, to name a few, are appropriately addressed.
3. It helps you create future projections and analyze trends to keep your operations profitable.

**7.1 The Basics**

Accounting is a language that provides information about the financial health of your business. You learn the language by learning to track daily business operations (payroll, gift card sales, invoices) in your accounting software. Accounting is basically just tracking where your money is going. It's important to record your financial transactions so you can generate an overall picture of your store's financial health and so you can analyze those transactions to better understand your financial situation.

**7.2 Why is Accounting Intimidating?**

Accounting has unfamiliar jargon/terminology that is sometimes difficult to understand. The fear of math and getting your numbers wrong is very real, because if you get the numbers wrong, there could be legal and/or tax consequences for those mistakes. With accounting, you're also serving two masters – your own business and the IRS – and sometimes those two things conflict. And let's face it, if you're not a numbers person, accounting can be boring.

### 7.3 Who Can Help

**Bookkeepers** are professionally trained on using accounting software and can help with financial recordkeeping. Bookkeepers are responsible for providing accurate, up-to-date financial reports and information.

**Tax professionals** prepare, calculate, and file income tax returns on behalf of individuals and businesses. They can be accountants, **Certified Public Accountants (CPAs)**, or **Enrolled Agents**. CPAs and Enrolled Agents can also represent you during an IRS audit.

**Business advisors** help you make business financial decisions, interpret your financial data, etc. This could be a mentor, coach, accountant, or a Chief Financial Officer. They are typically responsible for planning and executing business strategies to improve efficiency in operations and financial management of businesses.

**Payroll companies** are tools businesses can utilize to assist in paying employees and remitting payroll taxes. This arrangement is often beneficial for employers to save time.

#### 7.3.1 Accountant vs CPA

Accountants have at least a Bachelor's degree in accounting. They are educated on the subject, but not necessarily professionally certified, nor do they necessarily have requirements for continuing education. There is also no governing body that requires them to stick to certain ethics (no oversight), and they cannot represent you in an audit.

Certified Public Accountants (CPAs) are licensed by a professional governing body and are required to undergo continuing education to maintain their license. They are held to more stringent standards than unlicensed accountants and are expected to abide by the code of conduct of the Association of International Certified Professional Accountants. They can represent you in an audit.

### 7.4 Accounting Workflow

A financial transaction is made. Once made, you record the money flowing into or out of your bank account. Then, the transaction is linked to a category from your Chart of Accounts. Then you're done!

### 7.5 Cash vs Accrual vs Modified Cash Accounting

In **cash accounting**, you record revenue and expenses when you pay or receive money. With **accrual accounting**, you make a record when you receive a bill or send an invoice regardless of when it actually gets paid. In **modified cash accounting**, you record transactions related to long-term assets and inventory under the accrual method but use cash accounting for short-term assets and expenses.

## 7.6 How to Calculate Cost of Goods Sold (COGS)

The official formula for retail businesses is:

**COGS = Starting Inventory + Net Purchases - Ending Inventory**

### 7.6.1 Average vs Specific Cost

Under the specific method, you receive against your invoices and your point of sale system tracks the cost of each individual item so when you run your starting and ending inventory reports, you get the cost of just the particular books remaining in inventory. Before modern POS systems, the specific cost system required too much time, so average cost is also a legal method. With the average cost method, you estimate.

## 7.7 Accounting Software

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## 7.8 Who Does Your Bookkeeping?

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## 7.9 Backups & Document Retention Systems

If you use online software, it is backed up automatically. But if you use Quickbooks Desktop or Excel, it's best to create a system to back it up to the cloud. You should discuss federal and state document retention requirements with your accountant. The IRS requirements usually range from three to seven years, but records related to property may be much longer, and your state may have additional requirements.

## 7.10 Getting Into a Financial Rhythm

It will make accounting easier for you if you start to develop a rhythm for your store and create some checklists so nothing falls through the cracks. We've provided an accounting calendar in the **Templates & Resources** section to help you develop a good rhythm.

## 7.11 Meeting With Your Tax Professional

You may find it useful to keep an open document of running questions and schedule a meeting when one of those questions turns urgent, or if you get an IRS notice, see a lot of variance up or down from the previous year, either in business income or in total family income, or if it's been at least six months since you last met.

Prior to the meeting, run your financial reports and send those to your advisor along with your questions as your "agenda." Or if you use online accounting software, you may be able to give your advisor access to your account.

We have included a sample agenda checklist in the **Templates & Resources** section.

## 7.12 Introduction to Classic Financial Statements

The **Profit & Loss Statement**, called a P&L for short, may also be called an Income Statement or Statement of Operations. It summarizes all the transactions in your Income, Expense, and Other Income/Expense categories from your Chart of Accounts over the reporting period.

The **Balance Sheet**, also called the Statement of Financial Position, summarizes the value of your Asset, Liability, and Equity categories in your Chart of Accounts as of a specific date.

The **Cash Flow Statement** fills in the gaps to show how cash is entering and leaving a company.

## 7.13 Initial Accounting Decisions

Every business should open a separate business bank account, hire a tax advisor/accountant, and determine your **fiscal year**.

## KEY TAKEAWAYS

- Accounting is basically just tracking where your money is going.
- The accounting workflow is simply recording a financial transaction then linking that transaction to a category within your Chart of Accounts.
- In cash accounting, you record financial transactions when money changes hands; whereas in accrual accounting, your record transactions when they happen regardless of when money changes hands. Modified cash accounting is a mix of the two.
- COGS = Starting Inventory + Net Purchases – Ending Inventory
- The Profit & Loss Statement, Balance Sheet, and Cash Flow Statement are the three classic financial statements every business should use.

## TEMPLATES & RESOURCES

- **Resource**: Accounting Calendar
- **Resource**: Sample Tax Advisor Meeting Agenda

## KEY TERMS

- 1099
- Accountant
- Accounting
- Accrual Accounting
- Assets
- Average Cost
- Balance Sheet
- Bookkeeper
- Business Advisor
- Business Property Tax
- Cash Accounting
- Cash Flow Statement
- Certified Public Accountant (CPA)
- Chart of Accounts
- Cost of Goods Sold (COGS)
- Enrolled Agent
- Expenses
- Fiscal Year
- Form 1128
- Form 3115
- Liabilities
- Modified Cash Accounting
- Net Purchases
- Profit & Loss Statement
- Income/Revenue
- Schedule C
- Sole Proprietorship
- Specific Cost
- Tax Professional
- W2

## REVIEW QUESTIONS

**True or False:**

- The only person who can speak to the IRS on your behalf is a CPA (certified public accountant).
- The COGS formula is: COGS = Starting Inventory + Net Purchases + Ending Inventory.
- The accounting workflow is recording a financial transaction then linking that transaction to a category within your Chart of Accounts.

## ANSWER KEY

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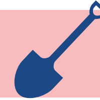
- F
- T

DIG DEEPER 

## DEBITS & CREDITS AND DOUBLE ENTRY ACCOUNTING

### WHAT IS DOUBLE ENTRY ACCOUNTING?

Your bookkeeping accounts are a database just like your point of sale system. You're tracking items (in this case, financial transactions) over time and storing information about those items. Accounts can be real live bank accounts or "virtual accounts" like Accounts Payable and Accounts Receivable. Single Entry accounting is a simple and straightforward method: you only record income and expenses, and each transaction is a single entry in your records. Double Entry accounting, then, means there are two entries for each transaction.

Let's begin with a brief history lesson: Double Entry accounting was officially developed in the mercantile period of Europe to help rationalize commercial transactions and make trade more efficient. The concept of double-entry bookkeeping, however, dates back to the Romans and early Medieval Middle Eastern civilizations, where simplified versions of the method can be found. Some thinkers have argued that double entry accounting was a key technology responsible for the birth of capitalism.

The modern double entry system started to become widely used in the 13th and 14th centuries by Italian merchants. The first known documentation of the double entry system was recorded in 1494 by Luca Pacioli, who is widely known today as the "Father of Accounting" because of the book he published that year detailing the concepts of the double entry accounting method.

Today, Double Entry Accounting is the main accounting system used by most modern accounting software, as it tells the full story of what is happening with your money.

It's called "double entry" because every transaction you make involves both a debit and a credit - as one account increases, another must decrease, and the sum of every debit and its corresponding credit must equal zero.

Just like in your POS where you track author and title and can search on either one, in your accounting system, you want to track both the transaction and its category. For example, when you purchase office supplies, you would record the money coming out of your bank account AND record the purchase in your "Office Supplies" category.

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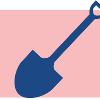


Categories come from your Chart of Accounts, which we'll go into in detail in Chapter 8: Bookkeeping for Booksellers. While single entry only tracks revenue and expenses, double entry also tracks equity, assets like inventory, and liabilities like accounts payable. You'll learn all about these categories as we move through this course, but for now, it's important to understand that while the double entry system may seem like more work, it paints a more complete picture of how money is moving through your business.

## ACCRUAL DOUBLE ENTRY SYSTEM

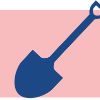
Accrual accounting requires the double entry system that is supported by Quickbooks and other accounting software. In this system, every transaction balances out to zero, with one account being debited and another being credited the same amount. You debit the account that value is flowing into and credit the account that value is flowing out of (usually your bank account).

Let's walk through how that works with inventory. Under the accrual system, if you are on terms with a publisher, you would enter inventory invoices as you receive them, debiting your Inventory asset account and crediting Accounts Payable. When you buy inventory, value flows into the inventory asset account, which means it gets entered in the debit column on the left. That means the other account has to get credited to balance it out.

### DOUBLE ENTRY ACCOUNTING

**Example:** $100 invoice for inventory received, then paid. $50 of the inventory sold by the end of the month.

| ACCOUNT | DEBIT | CREDIT |
|---|---|---|
| Inventory | $100 | |
| Accounts Payable | | $100 |
| Accounts Payable | $100 | |
| Bank Account | | $100 |
| Cost of Goods Sold | $50 | |
| Inventory | | $50 |

## DIG DEEPER 

When you pay the invoice, you would debit Accounts Payable and credit your bank account, since money is leaving the bank. But asset accounts like inventory aren't an expense, so how do you get to deduct inventory as an expense from your income? That's where Cost of Goods Sold comes in. You have to calculate the cost of only the inventory you sold during the period, and then you debit Cost of Goods Sold, which is an expense account, and credit Inventory, which is an asset account.

The double entry accounting system is based on the accounting equation:
Assets = Liabilities + Equity

If you look at this equation, it's a bit easier to understand debits and credits. Debits increase your asset accounts, which means they have to decrease your liabilities and equity accounts, because they're on opposite sides of the equation. Credits increase your liabilities and equity, therefore they must decrease your assets, again because they're on opposite sides. Similarly, debits increase your expense accounts, which means they decrease your revenue accounts, and credits decrease expenses and increase revenue, again because revenue and expenses are opposites.

Here's a nifty chart to help you remember when to debit or credit an account.

| ACCOUNT | INCREASE | DECREASE |
|---|---|---|
| Assets | Debit | Credit |
| Liabilities | Credit | Debit |
| Equity | Credit | Debit |
| Expenses | Debit | Credit |
| Revenue | Credit | Debit |

*Chapter 8*

# Bookkeeping for Booksellers

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Customize your Chart of Accounts to meet your reporting needs.

## WHY THIS MATTERS

**Bookkeeping** is a critical piece of managing and understanding your business. It helps tell the story of the financial health and longer term viability of the company.

The result of doing bookkeeping activities is to be able to review the information that has been recorded to make business decisions and understand how the company is performing from a financial perspective. Keeping up on bookkeeping activities, especially the ins and outs of your cash accounts, can help prevent theft or embezzlement.

Ultimately, financial recordkeeping is necessary for filing with state and federal tax authorities. Being organized and easily finding information for the various tax returns a business files saves time and money and reduces stress.

## CHAPTER OUTLINE

**8.1** The Basics
**8.2** Setting Up Your Chart of Accounts
**8.3** Types of Accounts
**8.3.1** Income
**8.3.2** Expenses
**8.3.3** Other Income/Expense
**8.3.4** Assets
**8.3.5** Liabilities
**8.3.6** Equity
**8.4** Serving Three Masters
**8.5** Using Subaccounts
**8.6** Categorizing Transactions
**8.7** Tax Related Coding Issues
**8.8** Pros & Cons of Accounting Software
**8.9** Closing the Books
**8.10** Monthly Reporting
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper:** General Journal Entries

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## 8.1 THE BASICS

**Bookkeeping** is the process of recording a business's financial transactions. It is the way to track business activity in an organized manner. It used to be done on paper, but these days most businesses use software to help with bookkeeping, which could be a generic program like Excel or Notion or specialized accounting software like Quickbooks or Sage. Bookmanager point of sale software even has accounting built into it.

Whatever system you use to record your store's financial transactions, it is important to be consistent when entering information into your bookkeeping system. As with any database, Garbage In = Garbage Out.

## 8.2 SETTING UP YOUR CHART OF ACCOUNTS

The accounts you use to track business activities in your accounting software are commonly referred to as your **Chart of Accounts**. When you look at your chart of accounts in your accounting software, it is a flat hierarchical structure similar to an outline. **Subaccounts** get slightly indented, showing what parent account they belong to. This makes sense because the purpose of the Chart of Accounts is to group similar types of transactions together.

Traditionally, each account was also given an account number, such as 2000 for Accounts Payable, 2100 for Payroll Liabilities, and 2200 for Sales Tax Payable, but modern bookkeeping software may not require this or may have a setting toggled to hide the numbers. Traditional account numbers leave a gap for subaccounts so you can create 99 Payroll Liability subaccounts if necessary.

Most software comes preloaded with chart of account templates depending on whether you are an inventory or service type of business. Or perhaps you had an accountant or bookkeeper set yours up for you. If not, it's time for you to create one!

What's important to know is that your chart of accounts can be a living, breathing document that changes with your business needs; however, it is important to plan out your changes so you can decide whether you can just make the change going forward or if you'll need to clean up old data.

If you're not a public company, your chart of accounts is not going to be seen by anyone but you and your accountant, so feel free to make it work for you. Note that including symbols like $ may break things when you try to link your accounting software to your payroll company's software. Also, once successfully linked, if you change the name of a linked account because your budget changed, you may have to go back through the linking process again.

## 8.3 TYPES OF ACCOUNTS

The five main categories of accounts are: **Income**, **Expenses**, **Assets**, **Liabilities**, and **Equity**. Within those broad categories, most companies break things down further to help explain how the company is doing from a financial perspective.

### 8.3.1 INCOME

Your primary income accounts are related to sales. Typically, you will have subaccounts for books, sidelines, greeting cards, café, used books – big categories of sales you want to budget for and monitor trends. These subaccounts should each have a corresponding **Cost of Goods Sold** subaccount under Expenses.

You may also want to break some or all of those categories down even further – in store sales, online sales, school sales, business-to-business sales, etc. Another way to subdivide sales is resale, mail order, or exempt for easier sales tax reporting.

### 8.3.2 EXPENSES

Expenses are numerous, and breaking them into subcategories will help you report to outside entities like tax authorities and the ABA ABACUS survey.

As mentioned in the income section above, you will need to have Cost of Goods Sold expense accounts related to the income accounts you set up. It is YOUR chart of accounts, and you should make it as detailed and helpful as possible. Ease of information retrieval can be a big time saver!

After figuring out the level of detail you need for COGS accounts, consider the other big expense categories for your store. One suggestion is to use expense subcategories for the ABACUS survey – payroll, occupancy, and operations. It is also helpful to set up accounts to make it easier for tax reporting.

### 8.3.3 OTHER INCOME/EXPENSE

Other Income and Expense are the last type of accounts that are typically part of your **Profit & Loss statement**, but are in the "other" category because they are not tied to sales of inventory (and the corresponding cost of goods sold) or to the day-to-day operations of your store. Here are some examples.

**Other Income** could be affiliate income, like Bookshop.org or Libro.fm. For both of these examples, books were sold to your customers, but they were not in your inventory. Hence, "other" income. Maybe your store rents out space to third parties, collects fees for consignment services, sells tickets for events, or offers publishing services. Perhaps you received a grant from Binc or an SBA EIDL grant. Or you may have earned interest income from a savings account. All of these types of revenue are considered "other" income.

**Other Expenses** include interest expense on loans or credit card balances if not paid in full each month. If you rent space for an event, that would be an "other" expense. Depreciation of fixed assets can also go in other expenses, though this past ABACUS listed it as a standard expense, so you can see that the dividing line between regular and other expenses can be a bit subjective. Theoretically, "other" expenses are unrelated to the day-to-day bookstore sales activities.

Your chart of accounts can be a great management tool. Keep in mind all the detail

you enter is available for all sorts of management reports, including financial statements like the balance sheet and income statement, but also the ability to look into specific activities and see just where the money went or how a certain line of business is performing.

## 8.3.4 ASSETS

**Asset** accounts usually show up on a **Balance Sheet** report. Assets are things that have current or future economic benefit to a company. They are typically things the company owns. Here are some common types of assets for a retail bookstore.

### Cash

These include your business checking accounts, petty cash, cash drawers, and balances from money software like Square, PayPal, Venmo, etc.

### Inventory

Inventory is a key asset account. We suggest breaking inventory down into multiple accounts based on what you have in your store. For example, you may have an account for books and one for sidelines. If you also have a café, you will want food & beverage inventory accounts. Used Books or Remainders may be part of what you offer your customers, and it might make sense to break out the balances in those accounts separate from other book inventory.

### Accounts Receivable

This is money you're owed from customers. Small retail stores do not usually extend credit to customers, but a common exception is when you start to work with school systems who expect books to be delivered first and issue payment several weeks later.

### Prepaid Expenses

If you are on the **accrual method** of accounting covered in the previous chapter, you may record annual licenses or dues paid early in the year as **Prepaid Expenses**, then record a portion of the big bill each month as an expense rather than all of it at one time. That way, you don't have huge swings in expenses.

### Deposits

These are typically a rent deposit or other payments you made for an expense farther out in the future.

### Fixed Assets

**Fixed Assets** are things like bookcases, computers, POS Software, and tenant improvements. Vehicles, like bookmobiles, and buildings are also categorized as fixed assets. These are large expenditures for items that have a lifespan beyond the year you purchase them.

Besides these main types of assets, your store may have trademarks or start up costs, which are also assets of the company.

## 8.3.5 LIABILITIES

**Liabilities** are things a business owes to other people or entities. Here are some common liabilities for a bookstore.

### Accounts Payable

These are monies owed to your vendors for inventory and other purchases where you were given terms, or a certain time to pay the bill. You will want to closely monitor accounts payable and know your credit limits. It's also important to keep your vendors happy so they will continue to extend credit.

### Credit Card Balances

Balances due on any company credit cards are also liabilities.

### Outstanding Gift Cards

These are a liability when issued to a customer. When customers use gift cards to buy items in your store, the balance decreases. You will want to pay attention to what your POS says the outstanding balance is and make sure that is what is in your accounting software. It's also important to know your state laws as to whether gift cards expire at some point or not, as that will affect your bookkeeping procedures.

### Loans

Bank loans or owner loans to the business are common examples.

### Taxes Payable

Sales tax payable and payroll taxes payable are owed to governmental entities who have the power to shut your business down, so stay on top of those.

### Prepaid Orders/Subscription Boxes

Prepaid special orders, preorders, and subscription boxes are also liabilities, as you collect money upfront for something you will deliver later. Another example of this is selling event tickets ahead of time where monies are collected for events in the future. Until the book arrives in your store and is rung thru, the monies collected are considered short-term liabilities.

## 8.3.6 EQUITY

**Equity** accounts are probably the most complex types of accounts because how they are set up depends on the business or tax structure of the bookstore. S Corporation equity accounts may include Capital Stock - funds owners/founders put in to start the business - a distribution account for cash owners are allowed to withdraw, and retained earnings - cumulative net income of the business. A single-member LLC that files its business taxes as part of the owner's personal tax return, may have equity accounts for owner's capital, subdivided into investments and draws, and a member's equity account, which is the equivalent of a retained earnings account. If you are a sole proprietor, yours might be called owner's equity; if a partnership, partner's equity. Ask your tax advisors how to set up and record entries to equity accounts.

## 8.4 SERVING THREE MASTERS

The chart of accounts is the foundation underlying the reports you can get out of your accounting software. Where it becomes complicated is that you have varying reporting needs for three different masters: you as the business owner or manager, the IRS, and the industry via ABACUS. These masters often come into conflict and are also subject to annual changes.

As a business owner or manager, you may need a lot of different data out of your accounting software, whether for internal business decisions or for state and local reporting. For business decision-making, you may want to track income and expenses for separate income streams, such as school sales vs in-store sales. Or if your state has sales tax, you may need additional categorization for that reporting.

How you pay income tax on your business earnings will depend on your corporate structure. Your business may have to file its own separate return, or the earnings may pass through to the owners and be reported solely on their returns. And, of course, each of those IRS forms is slightly different from the rest. Your accountant may take responsibility for mapping your chart of accounts to the required IRS tax forms for your business, or perhaps they require you to give them the data via an organizer that is already broken down into the required government categories.

## 8.5 USING SUBACCOUNTS

Subaccounts tend to get added to your chart of accounts over time as you discover that you want reports with more granularity. For example, maybe you're trying to decide if your author event programming is worth continuing, and you want to calculate the true profit and loss from the events program, but all your event supplies are lumped in under a "supplies" category. You decide to create a subcategory called "Supplies: Event" going forward so you can attribute those expenses to that particular income stream. In Quickbooks Desktop, you could use Classes instead of subcategories to do the same tracking and keep your chart of accounts looking a little cleaner.

One subaccount we recommend everyone have is for **co-op**. The industry is divided as to whether this subaccount should go under Advertising Expense or Cost of Goods, but no matter the parent, it's helpful to have the subaccount so you can easily track the amount of co-op you claim.

## 8.6 CATEGORIZING TRANSACTIONS

Your reporting is only going to be as good as your coding. **Coding** is bookkeeping speak for categorization. Whether an employee manually enters all your credit card receipts or you have your accounts linked to import them automatically, it's important to make sure your bookkeeping data entry is being done in a timely and consistent manner. The longer you wait to review a transaction, the less you are going to remember about it and the more inconsistent your data will be. You'll see a

receipt for paper and put it under Office Expense without remembering that it was special red construction paper for an event craft and should be in Event Supplies instead.

Also, remember that you can split a transaction into multiple categories, so if you're tracking departments separately, you can split a single invoice for books and sidelines and put the appropriate amount into book inventory and the rest into sideline inventory.

As the owner, you may not do your own bookkeeping, so consider what documentation, training, and oversight you have in place to make sure your transactions are coded properly and consistently.

## 8.7 TAX RELATED CODING ISSUES

Most legal business expenses are considered tax deductible; however, there are a few that get treated differently under current tax law. For example, the rules for buying meals and entertainment keep going back and forth as to what is fully deductible, partially deductible, or nondeductible. In cases like this, it's important to speak to your accountant about what qualifies for each related category in your chart of accounts or if you need to add a new subcategory.

In general, there are tax implications for anything you purchase directly for an employee (meals, uniforms, gifts) because it may have to be reported as income on their W2s.

When in doubt, create an "Ask Accountant" category and initially code any transactions to it that you have questions about until you can get a definitive answer.

Another big coding decision is whether an equipment purchase should be considered an asset to be depreciated over time or an expense to be deducted that year. Startup costs are required to be depreciated, but if you wait to invest in a point of sale system until Year Two, you have more options. $2500 is a commonly cited threshold for depreciating assets, but small businesses currently have a lot of leeway due to Section 179 and the Safe Harbor for De Minimus Amounts to set their own thresholds. In our point of sale example, you could either deduct the entire expense in the tax year you purchased it using Section 179, or you could depreciate it over the expected life of the system. These are individual decisions you should discuss with your tax advisor.

Another coding decision is when a third party like Square, Paypal, or your merchant processor nets their fees out of their deposit to you. Technically, you should show the gross amount as income and the fees as an expense. Now that these companies have to send you 1099-K forms, you want your topline income to match or this could potentially trigger an audit. This may require you to set Square up as a separate account in your accounting system and reconcile it like a bank account each month.

## 8.8 PROS & CONS OF ACCOUNTING SOFTWARE

The main benefit of accounting software over Excel is that most support quite a bit of automation. The first level of automation is memorized or templated transactions. For example, Quickbooks can "memorize" monthly bills that are always the same amount. Your accountant may also set up some general journal transactions as monthly memorized transactions.

The next level of automation is integrations with other software. Most accounting software will link with major banks and credit cards to auto-import your transactions. They may also link with payroll companies to automatically log everything related to payroll, including benefits. With an online software like Quickbooks Online, this may be very seamless, but even with Quickbooks Desktop, you can import a payroll file. In Chapter 3: Vendor, Debt, & Tax Management, it was mentioned that accounting software also integrates with Batch and Autoentry.com to import publisher invoices.

Your point of sale system may also have an accounting module (either built-in or as an added expense) that will export your receiving and daily sales to your accounting software.

Another pro is that accounting software has built in warnings when you are about to make a common mistake, such as a typo in the year or trying to credit and debit the same account.

Typically, the user interface provides dashboards, pre-built reports, and other helpful guidance as well.

The main con to accounting software, besides the cost, is that it's a new thing to learn, and sometimes it just doesn't do what you want.

## 8.9 CLOSING THE BOOKS

Tax advisors get really busy in March and April, and bookkeepers get stressed out the last week of the month and the first week of the new month when they are working on "closing the books" on the previous month. What this means is they are trying to get all the transactions for the month entered so they have complete data to run accurate monthly reports. In the olden days, this may have meant waiting on a credit card statement to arrive in the mail so you could run a reconciliation. Today, it's usually much faster to close the books since most financial records can be accessed online.

It's helpful to create a checklist of all the accounts that need to be reconciled, general journal entries to run, things to double-check, etc. before you can run final monthly reports. The bigger your store, the bigger a deal it can be if the reports are off or need to be re-run and redistributed. We have provided a "Closing the Books Checklist" in the Templates & Resources section to help.

If you have a bookkeeper, they may be responsible for most of the end-of-month checklist; however it's important for the owner to be involved at least at the oversight level.

Once you've gone through your checklist and everything is complete, the last step is to set a closing date in your software. This prevents you from accidentally entering a new transaction for that period and changing the data. This is helpful for preventing accidental typos, but what do you do when a week after you've closed your books you get a vendor statement listing a credit dated the previous month? We recommend simply changing the date when you enter it to be a date at the beginning of the current open period.

Because it may take you some time to run through your checklist or wait on outstanding items, closing last month's books usually happens about a week or two into the next month. Closing your books for the year, though, may take a bit longer. Often stores run a physical inventory at the end of a fiscal year and need to incorporate those results into their records. Or you may want to wait a month to get all your publisher statements and reconcile them.

Returns that have posted in your point of sale system but have not yet been credited by the publisher are a hassle and need to be adjusted at year-end since publishers have been known to take up to three or four months to credit returns.

Another thing to keep in mind is any owner retirement matches made out of your business bank accounts in the first quarter that count for the previous calendar year. You may want to call this account "Previous Year Owner IRA Match" to highlight this to your accountant so it doesn't accidentally get deducted twice.

## 8.10 MONTHLY REPORTING

Once your books are closed, you can confidently run and analyze monthly reports. Make sure you've actually blocked off time on your calendar for analysis. The main reason to create and run these reports is to help you make business decisions, so you need some distraction free time to analyze them.

Again, it's helpful to create a list of the standard reports you'd like to see each month, whether it's your bookkeeper producing them or you running them yourself. Each business may have different reporting needs, but these are some standard ones to consider:

- What reports do you need to see to file your monthly sales tax? Is this simply a Profit & Loss statement, or do you need a POS report as well?
- Do you want to look at monthly reports only, or do you also want comparison reports that show you the same month in the previous year? Or maybe it would be more useful to look at a rolling 12-month period that ends on the month you just closed and may even include a comparison to the same 12 months of the previous years. These comparison and rolling reports can help you spot trends over time.
- If you budget, you may want to run a budget variance report showing whether you are keeping to your budget or not.
- An Accounts Payable Aging Report can show whether you are overdue, and a Vendor Balance Summary report can show whether you are close to hitting your credit limit.

- If you work with schools or otherwise offer terms to customers, you should keep an eye on your Outstanding Accounts Receivable by Customer and send dunning emails as needed.
- The Balance Sheet gives you a snapshot of your cash, inventory, and payables.

## SUMMARY

**Why It Matters**

**Bookkeeping** is a critical piece of managing and understanding your business. It helps tell the story of the financial health and longer term viability of the company. The result of doing bookkeeping activities is to be able to review the information that has been recorded to make business decisions and understand how the company is performing from a financial perspective.

**8.1 The Basics**

**Bookkeeping** is the process of recording a business's financial transactions. It is the way to track business activity in an organized manner. Whatever system you use to record your store's financial transactions, it is important to be consistent when entering information into your bookkeeping system. As with any database, Garbage In = Garbage Out.

**8.2 Setting Up Your Chart of Accounts**

The accounts you use to track business activities in your accounting software are commonly referred to as your **Chart of Accounts**. When you look at your chart of accounts in your accounting software, it is a flat hierarchical structure similar to an outline. It's important to know that your chart of accounts is a living, breathing document that changes with your business needs; however, it is important to plan out your changes so you can decide whether you can just make the change going forward or if you'll need to clean up old data.

**8.3 Types of Accounts**

The five main categories of accounts are: Income, Expenses, Assets, Liabilities, and Equity.

**8.3.1 Income**

Your primary **income** accounts are related to sales. Typically, you will have subaccounts for big categories of sales you want to budget for and monitor trends. These **subaccounts** should each have a corresponding **Cost of Goods Sold** subaccount under Expenses.

### 8.3.2 Expenses

You will need to have Cost of Goods Sold expense accounts related to the income accounts you set up. After figuring out the level of detail you need for COGS accounts, consider the other big expense categories for your store. One suggestion is to use expense subcategories for the ABACUS survey - payroll, occupancy, and operations. It is also helpful to set up accounts to make it easier for tax reporting.

### 8.3.3 Other Income/Expense

Other Income and Expense are the last type of accounts that are typically part of your **Profit & Loss statement**, but are in the "other" category because they are not tied to sales of inventory (and the corresponding cost of goods sold) or to the day-to-day operations of your store.

### 8.3.4 Assets

**Asset** accounts usually show up on a Balance Sheet report. Assets are things that have current or future economic benefit to a company. They are typically things the company owns. Examples include cash, inventory, accounts receivable, prepaid expenses, deposits, and fixed assets.

### 8.3.5 Liabilities

**Liabilities** are things a business owes to other people or entities. Examples include accounts payable, credit card balances, outstanding gift cards, loans, taxes payable, and prepaid orders/subscription boxes.

### 8.3.6 Equity

**Equity** accounts are probably the most complex types of accounts because how they are set up depends on the business or tax structure of the bookstore. Ask your tax advisors how to set up and record entries to equity accounts.

## 8.4 Serving Three Masters

The chart of accounts is the foundation underlying the reports you can get out of your accounting software. Where it becomes complicated is that you have varying reporting needs for three different masters: you as the business owner or manager, the IRS, and the industry via ABACUS. These masters often come into conflict and are also subject to annual changes.

## 8.5 Using Subaccounts

Subaccounts tend to get added to your chart of accounts over time as you discover that you want reports with more granularity.

**8.6 Categorizing Transactions**

Your reporting is only going to be as good as your coding. **Coding** is bookkeeping speak for categorization. It's important to make sure your bookkeeping data entry is being done in a timely and consistent manner. The longer you wait to review a transaction, the less you are going to remember about it and the more inconsistent your data will be. And remember that you can split transactions!

**8.7 Tax Related Coding Issues**

There are tax implications for anything you purchase directly for an employee (meals, uniforms, gifts) because it may have to be reported as income on their W2s. Another big coding decision is whether an equipment purchase should be considered an asset to be depreciated over time or an expense to be deducted that year. Another coding decision is when a third party like Square, Paypal, or your merchant processor nets their fees out of their deposit to you. Technically, you should show the gross amount as income and the fees as an expense. Now that these companies have to send you 1099-K forms, you want your topline income to match or this could potentially trigger an audit. When in doubt, create an "Ask Accountant" category where you can code transactions you have questions about until you can get them answered.

**8.8 Pros & Cons of Accounting Software**

The main benefit of accounting software is that most support quite a bit of automation. The main con besides the cost is that it's a new thing to learn, and sometimes it just doesn't do what you want.

**8.9 Closing the Books**

It's helpful to create a checklist of all the accounts that need to be reconciled, general journal entries to run, things to double-check, etc. before you can run final monthly reports. We have provided a "Closing the Books Checklist" in the Templates & Resources section to help.

**8.10 Monthly Reporting**

Each business may have different reporting needs, but these are some standard ones to consider:

- Reports for monthly sales tax
- Profit & Loss statement
- Comparison reports
- Budget Variance Report
- Accounts Payable Aging Report
- Outstanding Accounts Receivable by Customer
- Balance Sheet

## KEY TAKEAWAYS

- Bookkeeping is the process of recording a business's financial transactions. It is the way to track business activity in an organized manner.
- The accounts you use to track business activities in your accounting software are commonly referred to as your Chart of Accounts.
- The five main categories of accounts are: Income, Expenses, Assets, Liabilities, and Equity.
- The chart of accounts is the foundation underlying the reports you can get out of your accounting software.
- Your reporting is only as good as your coding.
- Create a checklist for closing the books and monthly reports.

## TEMPLATES & RESOURCES

- **Resource**: ABA Standard Chart of Accounts
- **Resource**: ABACUS Survey Definitions
- **Resource**: Schedule C
- **Example**: Fiction Addiction's Chart of Accounts
- **Example**: Well-Read Moose's Chart of Accounts
- **Example**: Melissa's Financial Reports Checklist
- **Example**: Melissa's Monthly Closing Checklist
- **Video**: How to Map Taxes in Quickbooks Desktop

## KEY TERMS

- Accrual Method
- Assets
- Balance Sheet
- Bookkeeping
- Chart of Accounts
- Coding
- Co-op
- Cost of Goods Sold (COGS)
- Equity
- Expenses
- Fixed Assets
- Income
- Liabilities
- Prepaid Expenses
- Profit & Loss Statement
- Other Expenses
- Other Income
- Subaccounts

## REVIEW QUESTIONS

**True or False:**

- Inventory is a liability.
- Your chart of accounts can include more categories than the tax form you file for your business.

**Multiple Choice:** Your chart of accounts is used for:

A. Tax Prep

B. Report Generation

C. ABACUS

D. All of the Above

## ANSWER KEY

- F
- T
- D

## DIG DEEPER

## GENERAL JOURNAL ENTRIES

Depending on your accounting software, there may be several different ways to enter transactions.

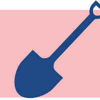
Using the general journal tends to be where non-bookkeepers get the most confused. Typically, you would work with your accountant or bookkeeper to set up any monthly journal entries that you'll need to use. The general journal can be intimidating for inexperienced bookkeepers, as it's where the double-entry system is on naked display with just a column on the left labeled debit and one on the right labeled credit. The Deeper Dive section of Chapter 7 taught you that debit refers to money flowing into an account and credit to money flowing out of an account. This terminology seems backward to normal, non-accountants because it's the opposite of bank terms you're more familiar with, such as debit cards.

If your transaction involves a vendor, such as paying a publisher or your internet bill, you typically would not use the general journal. Most accounting software has a "pay bills" function for those use cases.

Instead, the general journal is most often used like a bank transfer to reassign money between two existing accounts. For example, you may run a monthly general entry for COGS that debits Cost of Goods sold subaccounts and credits Inventory accounts.

| ACCOUNT | DEBIT | CREDIT |
| --- | --- | --- |
| Cost of Goods Sold: New Books | $12,943.91 | |
| Inventory: New Books | | $12,943.91 |

## DIG DEEPER



Another example is with postage expense. The ABA sometimes asks us to report New Book Return Freight separate from shipping expense on customer orders. If you use shipping software such as PirateShip for both types of postage, your accounting software may automatically code all these charges as customer freight. In that case, at the end of the month, you can look at a report in your shipping software and add up how much was actually freight on vendor returns. Once you have that total, you could do a general journal entry to debit return freight and credit customer freight.

| ACCOUNT | DEBIT | CREDIT |
|---|---|---|
| Operations: Freight Out | | $139.34 |
| Operations: Returns Freight | $139.34 | |

Other examples of times you may do general journal entries are when you have assets to depreciate or if you're on the accrual system and need to do monthly allocations of prepaid yearly expenses.

*Chapter 9*

# Cash Flow Deep Dive

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Understand the difference between cash, profit, and sales.
- Create strategies to manage your cash flow.
- Understand how to read an official cash flow statement.

## WHY THIS MATTERS

**Cash flow** is crucial information because it shows you how much money is coming in and going out of your business and whether you have enough cash on hand to pay your bills. Having a handle on the amount, timing, and uncertainty of cash flows is essential to evaluating your store's financial performance. Ultimately, scrambling to keep up with poor cash flow can lead to a death spiral for a business. Additionally, even if a lack of cash flow doesn't endanger your business, it may still limit its ability to grow.

Regularly monitoring and analyzing cash flow is an essential aspect of planning and budgeting. Anticipating high inflows of cash may indicate your ability to grow. Budgeting for planned outflows of cash helps you determine exactly how much you can spend month-to-month.

## CHAPTER OUTLINE

**9.1** The Basics
**9.2** How to Calculate Cash Flow
**9.3** How to Calculate Break Even Rate
**9.4** How to Calculate Burn Rate
**9.5** Cash Flow vs Profit
**9.6** Why Sales May Not Directly Convert to Cash
**9.7** Cash Flow is About Timing
**9.8** Using Budget to Improve Cash Flow
**9.9** Strategies for Managing Cash Flow
**9.10** How to Read a Cash Flow Statement
**9.11** What To Do About a Cash Flow Deficit
**9.12** Getting Ahead of Cash Flow Issues
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper:** How to Project Cash Flow

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## 9.1 THE BASICS

The term **cash flow** refers to the net amount of cash or cash equivalents flowing into and out of your business. When you receive cash, it's an inflow; when you spend money, it's an outflow.

According to a 2019 Intuit survey, 61% of small businesses worldwide experience cash flow problems. Due to these cash flow problems, almost one-third of those polled are unable to pay their debts, creditors, vendors, or employees. Even if a company appears to be doing well, and even if it's showing profits, poor cash flow can still cause it to fail.

Understanding cash flow helps you determine whether or not you can pay your bills on time. Failure to keep up with bills can lead to late fees, penalties, and strained relationships with vendors. Ultimately, scrambling to keep up with poor cash flow can lead to a death spiral for a business. Additionally, even if a lack of cash flow doesn't endanger your business, it may still limit its ability to grow.

Therefore, regularly monitoring and analyzing cash flow is an essential aspect of planning and budgeting for your store. Anticipating high inflows of cash may indicate your ability to grow. Budgeting for planned outflows of cash helps you determine exactly how much you can spend month-to-month.

## 9.2 HOW TO CALCULATE CASH FLOW

The cash flow calculation is extremely simple:

**(Beginning Cash + Cash In) - Cash Out = Ending Cash**

Think about your bank account. You have a balance at the beginning of the month that carries over from the previous month. That is your "beginning cash." Then, you accept payments throughout the month, which is your "cash in." If you add your beginning cash to your cash in, that gives you the total cash you've had for the month. Then, you subtract everything you spent money on, which is your "cash out." The number left over is both your "ending cash" AND your "beginning cash" for the next month.

## 9.3 HOW TO CALCULATE BREAK EVEN RATE

Assuming **Cost of Goods Sold** is your main expense, you would use the simple formula below to calculate the total sales you need to "**break even**," or not lose money.

**Break Even = Fixed Costs / Gross Margin**

You'll learn more in Chapter 11: Profit & Loss Deep Dive, but **Gross Margin** is your **Net Revenue** (or total sales) minus your cost of goods sold, and that is the money your business runs on. To get the number you need to make to break even, you divide your fixed costs by your gross margin.

When you use this formula, make sure to include owner's pay in your fixed costs. Depending on your business structure, owner's pay may not show up under payroll, so it can be easy to forget to include it.

Typically, you calculate your break even rate annually, using your yearly fixed costs, then divide by 12 to get your monthly break even sales figure.

If you have a lot of variable expenses, meaning expenses that are dependent on sales, then your break even analysis will be a bit more complicated. Here, you would need to project (or use your annual budget to determine) how much you'll spend on variable expenses over the course of the year, then divide by 12 to get the average, and add it to your fixed monthly expenses to get a true break even number.

## 9.4 HOW TO CALCULATE BURN RATE

If you're not breaking even, then you're losing money and will burn through your cash, which is pretty common for startups. If you find yourself burning through cash, you'll want to calculate your **burn rate**, or the amount of cash you pay out each month divided by the amount of revenue you bring in. The revenue number to use is usually the Net Income (bottom line) amount on your **Profit & Loss Statement** adjusted for owner's pay if appropriate. You then divide that figure into the amount of cash reserves you have to see how many months you can continue to operate as is, without increasing revenue, cutting expenses, or finding other sources of income. That period is commonly called your **runway**.

**Net Income / Cash Reserves = Burn Rate**

Net Income is the bottom line from your Profit & Loss Statement. Cash reserves is the total amount of money you currently have in the bank, savings, register, petty cash, etc. Your burn rate shows how quickly you're burning through cash and long you can operate.

The calculation above gives you a burn rate percentage. If your Net Income is -$2000, and you have $10,000 cash, you're burning cash at a 20% rate. If you flip that and divide cash by net income, you'll see you can operate for 5 months.

## 9.5 CASH FLOW VS PROFIT

Your cash flow and your **profit** are not necessarily the same thing, which is why your Profit & Loss Statement and your **Cash Flow Statement** will look different and show different numbers. Your cash flow is the real-time money flowing in and out of your business, whereas your profit is what is left of your revenue after all your expenses are taken out.

Cash flow is different from profit because of several reasons. First, not all of your sales directly convert into cash (which is covered in the next section). Also, if you use the accrual accounting method (vs the cash method), it means you record the money you're still owed as revenue when you make the sale, not when you get paid, so the money shows on reports sooner than you intake the cash.

Imagine a kid opening a lemonade stand. They plan to charge 50 cents per cup. If they sell 100 cups, they will make $50 of revenue. If each cup costs 13 cents to make, expenses are $13. **Profit = Revenue - Expenses**, which is $37 in this case ($50-$13). The cash inflow is $50, but the profit is the money left once expenses are paid, which is $37.

Cash flow is about timing – it refers to *when* a business needs money. If our kids need to pay the grocery store $5 for lemons today, but they won't have it until they make $50 on the weekend, they'll need to ask their parents for a loan to get them through, then pay it back once they make the money.

Because cash flow and profit are different numbers, a business can show a profit and still struggle to cover its expenses. Conversely, just because a company can pay all its bills doesn't mean it's profitable. If you have lots of money in the bank, but you still spend more than you make, you will show negative profits even though you're flush with cash.

Profit only exists on paper. It's one way of looking at business revenue, but it tells you nothing about whether the business has enough money to cover expenses. They say "cash is king" because you survive or fail based on whether you actually have the cash to pay what you need to, when you need to.

## 9.6 WHY SALES MAY NOT DIRECTLY CONVERT TO CASH

In the last section, it was stated that not all sales convert directly into cash. There are several reasons for this.

**Customers preorder books**, giving you an inflow of cash that can't be called sales until the customer actually gets the book.

**You send invoices** for books, which is the opposite of above. In this case, a customer pays later for a sale you've already made.

**You offer discounts**. In this case, when you make a sale, you don't receive the full cash amount of the sale. For example, if you make a $100 sale, but you offer a 10% discount, you would only receive a $90 inflow of cash.

**You offer store credit**. This means you made a sale, but received no cash, or received less cash than the total sale.

**You offer gift cards**. This means you receive an inflow of cash upfront when selling the gift card, but when a customer redeems the gift card, that sale doesn't produce any cash.

**You accept credit cards**. A credit card sale does not result in the same inflow of cash as that same transaction would with cash as the tender because your credit card processor takes a fee from each transaction. This applies to all non-cash tender types, such as PayPal, Venmo, and IndieCommerce.

**You remit sales tax**. If your state requires you to charge and remit sales tax, then that percentage of the transaction is a temporary inflow of cash, but it's a liability that you must eventually remit to the government.

**You depreciate assets**. For example, if you purchase a computer, you pay cash for it upfront, so that cash comes out of your bank account. However, if you depreciate assets, the total cost of the computer would be depreciated each year until it's "useful life" is over. In other words, for reporting and asset purposes, you're actually spending that money over several years even though all the cash already came out of your bank account. This applies to equipment, furniture, fixtures, and any other **assets** that you keep for more than one year. You'll learn more about assets in Chapter 10: Balance Sheet Deep Dive.

## 9.7 CASH FLOW IS ABOUT TIMING

Effective cash flow management strategies come down to timing. You may be successful over a month or a year, but not over a particular day or week. Even if you earned more money than you spent, you still have a cash flow issue if your bills are due at the beginning of the month, but you won't actually have money in the bank until the middle of the month.

Timing is about *when* you actually receive money relative to when the money needs to be spent. This is just as important as how much money you have at the end of the month. If your bills don't match up with your income, you're more likely to miss payments or run into other issues.

As you learned in Chapter 2: Daily Store Finance, monitoring your available cash (bank balance minus payments in transit) on a regular basis can provide you with the information you need to attend to this timing issue.

You may find it helpful to time paying your bills according to when you're likely to have money in your account versus paying all your bills once per month, perhaps with weekly payments to vendors to spread out your outflows. If you can better match up your income to your expenses, you'll save money on fees and won't have to worry as much about whether you'll have enough money to pay bills.

## 9.8 USING BUDGET TO IMPROVE CASH FLOW

Chapter 12: Creating and Analyzing Your Budget will cover budgeting in depth; however, it's important to understand now that budgeting is a crucial component of cash flow management.

A **budget** lets you estimate upcoming income and expenses, and it enables you to monitor and more clearly comprehend whether your business generates enough income to cover its costs. In other words, you will be ready to anticipate future inflows and outflows of cash and set goals for business growth if you use a budget. There are, of course, ups and downs in the retail industry, and if your store is located in a seasonal tourist destination, some months can be five times as busy as others.

Because your balance of revenue and expenses is unpredictable, budgeting is a continuous process rather than an isolated exercise. You should review and update your budget every month, every quarter, or whenever there are significant changes to your business, like large expenditures. This will help you stay on track to achieve your goals. It's also great practice for maintaining your financial records year-over-year.

In review, a budget will help with:

- Estimating income & expenses
- Monitoring whether income can cover costs
- Setting goals for business growth
- Cutting costs to avoid overspending
- Preparing for busy seasons and slow months
- Maintaining financial records

## 9.9 STRATEGIES FOR MANAGING CASH FLOW

Now that you understand how cash flow works, here are some actionable strategies you can implement for cash flow management.

- **Returns to publishers for credit**. Whether you do returns every month or a few times a year, they are great for increasing cash flow. While returns can be a release valve on your Accounts Payable since you can apply the credits toward outstanding bills, you should never rely on them to stay current on your account.
- **Gift cards and preorders**. These are quick and immediate inflows of cash, so promoting gift cards and preorders is a great way to increase cash flow.
- **Sales and promotions**. Sales, promos, and discounts are another way to help with cash flow. Keep in mind that the purpose of these is to turn over your inventory quickly and receive some inflows of cash, but any discount is money out of your pocket, so use them wisely.
- **Subscriptions/First Editions Clubs**. Many stores have implemented subscription boxes and store memberships, which can give you an influx of predictable monthly (or quarterly, or yearly) cash.
- **High Value Customers**. These are the regular customers you can depend on for loyalty and sales. Make sure you nurture these relationships through VIP, frequent buyer programs, loyalty promos, and targeted marketing.
- **Newsletter/Social Media**. Virtual platforms are excellent ways to leverage your following, your branding, and your inventory into cash. Well placed posts and messages can lead to sales that otherwise wouldn't happen.
- **Bookshop.org**. Bookshop is a free way to earn money. You may receive a smaller percentage of each sale; however, having a Bookshop account allows customers to find your store who may not have otherwise. Using Bookshop means you also save on shipping, inventory, and labor. Bookshop also distributes "pool payments" each January and July, which is a free inflow of cash that could come exactly when you need it.

- **Negotiating Terms**. Negotiating terms with your vendors can be an effective way to manage your cash flow without additional expenses. If you have a great history of paying your bills, talk to your credit reps and ask for a bigger discount, or ask for longer payment windows if you need help with cash through slower seasons. It's also beneficial to become familiar with business-to-business programs. These will give you a hefty discount on large orders for books sold to corporate or nonprofit institutions who intend to give them away. Some of them are up to an extra 10% off your regular discount.
- **Asking for incoming order holds if you're in a pinch**. This means you won't receive inventory, but it also forestalls the bills on those shipments. Keep an eye on your upcoming orders being shipped so you know about future outflows of cash.
- **Paying early**. Check if any of your suppliers offer early pay or credit card payment discounts. Ingram is one vendor whose terms include a 10% discount on bills paid before the 10th of each month. That may not seem like much, but it adds up. Some vendors will also offer a discount if you pay by credit card, but be careful, because you don't want to fall behind on credit card bills either.
- **Communicating with credit representatives**. Err on the side of communicating too much. They can't wave a magic wand and make your bills disappear, but they can help in times of hardship.
- **Have an emergency plan.** Who knows what might happen that could result in a worst-case scenario? A clear, well thought out back-up plan can provide you with peace of mind and a source of reserve cash in case you need it one day.
- **Obtain a line of credit while you're doing well.** Apply when you don't need it so it's there when you do need it.
- **Reduce/eliminate expenses.** If your income goes down, your expenses should also go down. Look closely at the relationship between your total expenses and total income. Your expenses should not be growing if your income is flat or down. If your income is down and your payroll is high, it's important to catch that as soon as possible, as payroll is likely one of your biggest expenses. It's important to consider the contributing causes of this.
- **Stay on top of Accounts Receivable.** Your Accounts Receivable report with Future Due gives you an idea of money you can expect to see in your account in the near future. It is important to keep up with your invoices. This is money that's owed to you, so make sure you collect on it. This includes **co-op** that is owed to you.
- **Manage Accounts Payable well.** Know when your bills are due and set up a schedule to pay them (ideally more than once a month). You must be sure to pay your bills, otherwise you will go onto a credit hold with publishers and be unable to receive new books from them. Also, your power could get turned off, or you may experience assessed late fees or reduced credit limits.

## 9.10 HOW TO READ A CASH FLOW STATEMENT

There are many ways to monitor, track, and report on cash. Internally, you may keep a spreadsheet that shows beginning cash, ending cash, and cash inflows and outflows. There is no one way to do this internal tracking and reporting, but consistency can help you compare yourself to a week, a month, or a year ago. Most internal cash flow reporting for you and/or your management team will look similar to a personal checkbook or bank account. Hopefully, you start out the month with some money in the bank, which would be your **Beginning Cash**. Throughout the month, money flows in mostly from sales, but also potentially from loans, grants, miscellaneous income, etc. This is your **Cash In** or positive cash flow. Money also flows out to pay bills, including inventory purchases and other expenses, and this is your **Cash Out** or negative cash flow. At the end of the month, the amount of cash left, which is your **Ending Cash**, is brought forward to the next month, and you start over. Remember our formula for calculating cash flow:

(**Beginning Cash** + **Cash In**) - **Cash Out** = **Ending Cash**

This internal reporting can help you understand your cash volume, which is super important.

There is also formal cash flow reporting commonly referred to as a **Cash Flow Statement** or formally referred to as a Statement of Cash Flows. A properly Generally Accepted Accounting Principles, or GAAP, prepared Statement of Cash Flows provides the reader, often a bank, vendor, investor, or lender, a clear cut way to understand your business's cash flows in a concrete way that is comparable to other businesses because it uses a consistent format. This is especially useful when a business is on an accrual basis and net income may not tell your full "cash" story. The Cash Flow Statement is divided into three sections: **Operating Activities**, **Investing Activities**, and **Financing Activities**.

### Operating Activities

Operating Activities are things like your regular expenses, inventory purchased or sold, accounts receivable and payable, preorder sales, and gift cards. These could be cash in or cash out, depending on the transaction. This section most closely ties to a business's net income, often reformatted and consolidated to conform to broad categories defined as "Cash Received from customers" and "Cash Paid to supplies and employees." Interest income, interest expense, and income taxes are generally stated separately so the reviewer can easily calculate financial ratios that help them evaluate the business.

### Investing Activities

Investing Activities are purchases of things that are considered investments, generally assets. Typically, these are equipment, furniture, fixtures, and leasehold

improvements. They can also include intangible assets like the domain name, website, or goodwill of another business. The net activity is generally always negative, because if you categorize something here, it means you have spent a bunch of money on it, so it's Cash Out. Since this section includes assets sold as well, there is a rare chance that the net amount could be positive, but that would be the exception.

## Financing Activities

Financing Activities are things like lending and equity activity. For example, cash you received from a loan would show up in this section as positive; whereas payments on the loan would be negative. Equity activity includes things like sale of shares or owner/member contributions, for example, the owner(s) putting their own money into the business. Equity activity can also include owner/member draws or dividends paid. All of these are broken out between cash in and cash out for the period covered.

## Total Change in Cash

The last lines of a Cash Flow Statement are **Net Change in Cash**, which is all of your Cash In minus all of your Cash Out. At the bottom, the statement will recap your Beginning Cash and Ending Cash. This goes back to our cash flow formula:

(Beginning Cash + Cash In) - Cash Out = Ending Cash

Your Ending Cash is what you end the period with (month, year, etc.), and this will carry over to be the Beginning Cash for the next period.

Whether you're preparing a cash flow report in formal GAAP format or informally, the reporting should provide you and potentially other reviewers with information to understand the cash health of the business. Consistently monitoring and tracking your cash is ultimately more important than the method you use to report your cash flow.

### Cash Flow Statement Example

Check out the Cash Flow Statement on the next page for a good example of a GAAP-prepared statement.

# EXAMPLE CASH FLOW STATEMENT

**Healthy Micro Bookstore - 400 square feet of selling space**
**Statement of Cash Flows**
**For the Year Ended 12/31/22**

| | |
|---|---|
| Operating Activities | |
| Cash received from customers | $ 160,000.00 |
| Cash paid to suppliers and employees | $ (155,000.00) |
| Interest received | $ 100.00 |
| Interest paid | $ (471.00) |
| Income taxes paid | $ (500.00) |
| Net Cash from (used for) Operating Activities | $ 4,129.00 |
| Investing Activities | |
| Proceeds from sale of equipment | $ 50.00 |
| Purchase of equipment and leasehold improvements | $ (2,000.00) |
| Purchase of intangible assets | $ - |
| Net Cash used for Investing Activities | $ (1,950.00) |
| Financing Activities | |
| Proceeds from Notes Payable | $ - |
| Principal Payments on Notes Payable | $ (3,147.00) |
| Dividends Paid (Owner's Draw) | $ (1,000.00) |
| Net Cash used from (used for) Financing Activities | $ (4,147.00) |
| Net Change in Cash | $ (1,968.00) |
| Cash, Beginning of Year | $ 14,968.00 |
| Cash, End of Year | $ 13,000.00 |

## 9.11 WHAT TO DO ABOUT A CASH FLOW DEFICIT

In the event of a cash flow deficit, these are some of your options you can consider using.

- Withdraw money from your business savings account.
- Apply for a loan or a line of credit for the business. Your credit line will have a credit limit, which is the most money you can borrow at one time. However, you don't have to borrow money immediately when you open a credit line, so apply for one when you're doing well so it's there for when you're not doing so well.
- Collect on your outstanding invoices/accounts receivable.
- Sell off assets that may not add value to your business.
- Talk to your credit representatives about alternate payment schedules and credit holds.
- Ask friends and family for money. Perhaps lending from them may provide quicker resolution than traditional lending from a bank.
- Create a crowdfunding campaign, or run a marketing campaign encouraging customers to purchase gift cards.
- Explore balance transfer options with credit cards, or open a bank loan with a lower interest rate and use it to pay off high interest credit cards.

Some stores have also used merchant cash advances. You may be able to quickly borrow money with a merchant cash advance, like a Square or Quickbooks "loan," which is actually just a cash advance on your sales, but it can also be a costly option that leaves some small business owners stuck in debt for much longer than they anticipated.

With a merchant cash advance, you'll usually receive an upfront amount of money in exchange for a percentage of your future credit card and debit card sales. The total amount you'll repay is determined when you receive your cash advance, which means that early repayments won't save you money because your total cost is determined upfront.

Generally, you'll have to make daily or weekly repayments, and there may be a minimum you must repay each month, which means even if you don't have the sales volume, you'll still have to pay it.

It can be easy to qualify for a merchant cash advance and quickly get money to help you pay for an emergency expense, which makes merchant cash advances tempting. However, repaying the money with a percentage of your sales can make it difficult to maintain positive cash flow. Merchant cash advances are also an expensive way to borrow money and should generally be a last resort.

Always consult with a professional accountant before making major financial decisions that could impact the future of your business or your personal finances.

## 9.12 GETTING AHEAD OF CASH FLOW ISSUES

You've learned how to manage your cash flow and about what to do if you have a cash deficit. Now, it's important to learn how to be proactive to stay on top of and ahead of your cash flow.

- **Know when you'll break even**. The question, "When do I start to turn a profit?" is at the front of every small business owner's mind. Rather than wonder, set a realistic goal for when you want to break even. This will help you to focus your efforts and provide a numerical benchmark for projecting your cash flow in the near future. Use the break even formula mentioned earlier in this chapter to determine your break even number.
- **Cash flow management should come before profits**. This may seem counterintuitive; however, if you aren't managing your cash flow, you'll run into problems that a profitable quarter might not be able to fix. Learn to manage your cash well so you can be ready for whatever success comes your way.
- **Consider having separate bank accounts to set aside money for future large cash outflows**. If you know you're going to pay sales tax, or need to make quarterly payroll tax payments, or have large vendor invoices (like from school, business-to-business, or event orders), consider placing that money into a separate bank account so you have the cash when you need it.
- **Secure credit early**. As mentioned more than once in this chapter, you don't need to use a line of credit immediately, and it's the best way to be prepared for the unexpected. Too often, small business owners wait until they need it to secure a line of credit. You should apply for a line of credit when you're doing well so that it's there when you aren't doing so well.
- **Use accounting software**. Even if you run a small operation and you think a simple spreadsheet will suffice, it won't. Most accounting software available today allows you to both hone in on the details and look at the big picture of your finances. There are plenty of other advantages these programs offer, but above all, using a dedicated system to manage your cash flow will keep you organized and on top of your finances.
- **If you have employees, use a payroll service**. It's tempting to think you can do payroll all on your own. However, many small business owners have found that having the professionals take care of payroll saves them an enormous amount of time, helps streamline their cash flow, and is fully worth the cost.
- **Use a budget**. You'll learn all about budgeting in Chapter 12, but for cash flow, it's important to compare what you actually spent to the budgeted amount. Watching this every month will allow you to notice when you overspend in a particular category. This can be easy if you use accounting software as long as you have a budget and enter it into your software.

- **Prioritize and schedule out bill payments**. Spread your bills out so you're not paying all of your bills at the same time. You don't have to pay everything at once; in fact, you shouldn't. This is not to say you should be delinquent on any payment; rather, to keep sufficient cash on hand, consider dividing your bills into three categories: 1) bills you *must* pay immediately, 2) bills that are important to pay, but you may have a grace period, so you don't need to pay right away, and 3) bills where payment is flexible. Dividing your bills this way will help ensure you have the cash to pay your bills when you need it. This works in any size business from a single employee store to multi-location stores.
- **Have a financial plan**. Another key aspect of proper cash flow management is having a solid financial plan in place. This means understanding your business's expenses and income, setting realistic budget targets, and tracking your progress against those targets. Your cash flow projections are also a part of your financial plan. See the Dig Deeper section of this chapter to learn more about projecting cash flow.
- **Be proactive**. This means monitoring the economy (including local, state, and national) and keeping an eye on key indicators such as interest rates, inflation, and consumer spending. Anticipating what will come can help you plan better and prepare alternate financing sources if needed.
- **Use a high-interest savings account**. To maximize your cash flow, put money into a high-interest business savings account. Find an account that gives you more than 1% for leaving cash in it, with a low minimum deposit. This can improve your cash position month by month and help you prepare for unforeseen impacts on your customers or suppliers. In a business bank account, you should maintain cash to the equivalent of 3-6 months of operating expenses.
- **Be realistic** and don't deny the reality that may show up in your numbers. Deal with money and money issues on a regular basis and before they become bigger problems.

## SUMMARY

**Why It Matters**

**Cash flow** is crucial information because it shows you how much money is coming in and going out of your business and whether you have enough cash on hand to pay your bills. Having a handle on the amount, timing, and uncertainty of cash flows is essential to evaluating your store's financial performance.

**9.1 The Basics**

The term cash flow refers to the net amount of cash or cash equivalents flowing into and out of your business. When you receive cash, it's an inflow; when you spend money, it's an outflow.

**9.2 How to Calculate Cash Flow**

The cash flow calculation is extremely simple:

**(Beginning Cash + Cash In) - Cash Out = Ending Cash**

**9.3 How to Calculate Break Even Rate**

Assuming Cost of Goods Sold is your main expense, you would use the simple formula below to calculate the total sales you need to "break even," or not lose money.

**Break Even = Fixed Costs / Gross Margin**

**9.4 How to Calculate Burn Rate**

**Burn rate**, or the amount of cash you pay out each month divided by the amount of revenue you bring in, shows you what your **runway** is, or the amount of time you can operate as is.

**Net Income / Cash Reserves = Burn Rate**

**9.5 Cash Flow vs Profit**

**Cash flow** and **profit** are not necessarily the same thing, which is why your **Profit & Loss Statement** and your **Cash Flow Statement** will look different and show different numbers. Your cash flow is the real-time money flowing in and out of your business, whereas your profit is what is left of your revenue after all your expenses are taken out.

**9.6 Why Sales May Not Directly Convert to Cash**

Customers preorder books, you send invoices for books, you offer discounts, you offer store credit, you offer gift cards, you accept credit cards, you remit sales tax, and/or you depreciate assets.

### 9.7 Cash Flow is About Timing

Timing is about when you actually receive money relative to when the money needs to be spent. This is just as important as how much money you have at the end of the month.

### 9.8 Using Budget to Improve Cash Flow

A **budget** lets you estimate upcoming income and expenses, and it enables you to monitor and more clearly comprehend whether your business generates enough income to cover its costs. In other words, you will be ready to anticipate future inflows and outflows of cash and set goals for business growth if you use a budget.

### 9.9 Strategies for Managing Cash Flow

See the list in the chapter for many strategies to help you manage cash flow.

### 9.10 How to Read a Cash Flow Statement

Hopefully, you start out the month with some money in the bank, which would be your **Beginning Cash**. Throughout the month, money flows in mostly from sales, but also potentially from loans, grants, miscellaneous income, etc. This is your **Cash In**. Money also flows out to pay bills, and this is your **Cash Out**. At the end of the month, the amount of cash left, which is your **Ending Cash**, is brought forward to the next month, and you start over.

The Cash Flow Statement is divided into three sections: Operating Activities, Investing Activities, and Financing Activities.

### 9.11 What to Do About a Cash Flow Deficit

See the list in the chapter for many strategies to help you with a cash flow deficit.

### 9.12 Getting Ahead of Cash Flow Issues

See the list in the chapter for proactive strategies to help you get ahead of cash flow issues.

## KEY TAKEAWAYS

- Cash flow is the money that flows in and out of your business. Use this formula to calculate: (Beginning Cash + Cash In) – Cash Out = Ending Cash.
- Cash flow is not always what it seems. You could show profit and have no cash, or vice versa.
- Cash management is about timing – it's important that you actually have cash *when* you need it.
- Using a budget enables you to monitor and more clearly comprehend whether your business generates enough cash to cover its expenses.

## TEMPLATES & RESOURCES

- **Resource**: NetSuite Article: *Cash Flow Analysis: Basics, Benefits and How to Do It* by Lisa Schwarz
- **Resource**: Quickbooks Guide to Cash Flow Statements
- **Video**: Harvard Business School Online: *Cash Flow vs. Profit: What's the Difference? | Business: Explained*

## KEY TERMS

- Accounts Payable
- Accounts Receivable
- Assets
- Beginning Cash
- Break Even
- Budget
- Burn Rate
- Cash Flow
- Cash Flow Statement
- Cash Inflow
- Cash Outflow
- Co-op
- Cost of Goods Sold (COGS)
- Depreciation
- Ending Cash
- Financing Activities
- Gross Margin
- Investing Activities
- Net Change in Cash
- Net Revenue
- Operating Activities
- Profit
- Profit & Loss Statement
- Runway

## REVIEW QUESTIONS

**True or False:**

- Avoiding credit reps when you're cash strapped is a good idea.
- Cash flow, profit, and sales are all the same thing.
- On an official Cash Flow Statement, "Investing Activities" include: loans, owner/member contributions, and/or distributions.

## ANSWER KEY

- F
- F
- T

DIG DEEPER

# HOW TO PROJECT CASH FLOW

To successfully project cash flow, you'll need to do three things.

## Forecast Expenses

The easiest way to forecast expenses is to list all of your fixed expenses first, including rent, utilities, regular web expenses, loan repayments, and anything else that represents the same cash outflow every month. Then, estimate your variable expenses. Variable expenses ebb and flow with your sales volume, so the amount will fluctuate each month. Notable variable expenses will be cost of goods sold, marketing, and payroll. You'll want to note the purpose, cost, and due date of each expense as well. Review your bank and credit card statements for other regular expected expenses. Once you have all your monthly cash outflows listed, move on to forecasting your revenue.

## Forecast Revenue

First, list all of your guaranteed income, like subscription boxes or unpaid invoices. You can then examine your historical data to see how much money you made during this time period last year. Accounting software like QuickBooks often includes a budget forecasting feature that will automatically plug in last fiscal year's monthly numbers for you. If you think your sales will surpass last year, you can increase the amount, but it's essential to be conservative just in case. You should also consider any sales declines brought on by holidays, the time of year, or the month as you estimate your revenue, as well as any significant sales or promotions that will increase it.

## Put It All Together & Update Regularly

Once you have listed all your expenses and your guaranteed and potential revenue for the month, subtract your total projected expenses from your projected total revenue to see what your cash position is for the month (or whatever time period you're projecting).

Your cash flow projections are a living document. Good cash flow projections are updated on a regular basis. You may decide to do it quarterly, monthly, or even more frequently.

*Chapter 10*

# Balance Sheet Deep Dive

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Run your balance sheet.
- Fully understand how to analyze it.
- Take action on your analysis.

## WHY THIS MATTERS

The **Balance Sheet** can help pinpoint your store's weaknesses and help you make informed purchasing and investing decisions. Your balance sheet will tell you if you're in danger of going bankrupt, and it helps banks and potential buyers better understand the store's overall financial position outside of just profit and cash flow. It also shows your equity, which includes everything the owner/founder initially invested, plus everything you now own, minus everything you owe. Every business decision you make impacts your balance sheet. Your balance sheet also provides investors, loaners, banks, etc. a basis for evaluating your store's financial stability. Knowing how to read your balance sheet can help you make decisions that affect the long-term viability of your business.

## CHAPTER OUTLINE

**10.1** The Basics
**10.2** Assets: What You Own
**10.3** Liabilities: What You Owe
**10.4** Equity: What You're Worth
**10.5** Analyzing Your Balance Sheet
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper:** Financial Ratios

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## 10.1 THE BASICS

The **balance sheet**, also known as a Statement of Net Worth or a Statement of Financial Position, is a financial report that shows your business's **assets**, **liabilities**, and **equity** at a specific point in time. The Balance Sheet will reveal aspects of your business not shown in other reports like the **Profit & Loss** and **Cash Flow Statements**, including what you own (assets), what you owe (liabilities), and what you're worth (equity).

When you run this report, think of it like an oil gauge in your car. It shows you the overall health of the car (business), but it doesn't tell you if, when, or how to change your oil, it is just an indicator. If you ignore your oil gauge, though, your engine will seize and your car will stop.

One important fact to keep in mind is that the balance sheet is only a snapshot of your business on a given day, meaning it shows what your store owns, owes, and is worth on *that day only*. Every business decision you make impacts your balance sheet, so it's important to understand that when you're looking at it, you're reviewing the cumulative result of all your decisions leading up to that day.

The Balance Sheet is basically an aggregate report of all your business decisions, sales activities, cash flow, budgeting, everything all in one place. It captures the cumulative results of running your business over time and shows you the overall health and financial strength of your business by measuring the value of your assets compared to the value of your liabilities.

Your balance sheet is only as good as your bookkeeping. Cash basis stores, for example, do not need to track accounts payable and receivable, nor do they need to track inventory in bookkeeping. This is why so many stores are on a "**modified cash**" basis - to track these things so they show up on a balance sheet to be able to analyze them.

It's important to understand that all the numbers presented on your balance sheet come from somewhere else in your bookkeeping, meaning you don't manipulate the balance sheet directly. It's a report your accounting software generates for you based on your bookkeeping records, or if you manually handle your own accounting using spreadsheets, the numbers on the balance sheet you create will be pulled from other spreadsheets.

The balance sheet is based on the fundamental equation:

**Equity = Assets - Liabilities**

The two sides of the equation have to match, which is why it's called a balance sheet. Assets are what your business owns, and liabilities are how the business paid for the assets. Subtracting your liabilities from your assets gives a clear sense of how your business decisions increase or decrease your equity.

## 10.2 ASSETS: WHAT YOU OWN

**Assets** are what your business owns, both liquid (like cash) and solid (like property and inventory). Assets are anything of value that can be liquidated into cash, meaning things you can sell to make money. Keep in mind that brand equity, customer goodwill, and trademarks count as assets as well. These are called "intangible" assets. **Intangible Assets** have no physical substance but can still be sold, licensed, and transferred. They must have a quantifiable value and lifespan to be recorded as an asset.

There are two types of assets: fixed and current. **Current** assets are those you could theoretically convert into cash within one year or are already cash; whereas **fixed** assets are those you cannot easily convert into cash within a year.

Assets are listed first on your balance sheet, and current assets are at the top. The first category is always cash, then accounts receivable, then inventory, then all your other current assets. Under current assets come fixed assets, which include buildings, land, equipment, furniture, and fixtures. Most fixed assets eventually need to be replaced, meaning they depreciate in value each year. Generally, these are items that cost more than $500. The IRS requires you to amortize the value of fixed assets over the "useful life" of the asset, which is something your accountant can handle.

The last type of asset listed on your balance sheet are Other Assets. These are assets that do not fall into the other categories. Good examples are rent and utility deposits, which are assets because they can be liquidated into cash quickly if you leave the space.

Let's go into more detail about the main asset categories.

### Current Asset: Cash

The first, simplest, and most obvious current asset is cash or cash equivalents. This is the balance of actual money in your cash registers, bank accounts, safe, petty cash box, or any other place you keep cash. This also includes any balances in digital accounts such as PayPal, Venmo, Stripe, etc. All monies that you're able to access are considered cash.

The cash number on your Balance Sheet comes from your Cash Flow Statement. It is the **ending cash**, which if you'll remember from Chapter 9, is the cash left over after you subtract your change in cash from your **beginning cash**. This number tells you how long the business can pay bills without any other source of cash and is what you use to calculate your **burn rate**. This number is your cash on hand and in your bank account at any given time.

Not many stores will have **cash equivalents**, but this term covers short-term investments that can readily be converted into cash, like money market accounts or CDs. Your balance sheet will group them together with cash under the heading "Cash & Cash Equivalents."

The amount of cash that shows on your balance sheet is pulled from all your bank and cash accounts you have in your accounting system.

## Current Asset: Accounts Receivable

The next current asset is **accounts receivable**, which is generally the balance of money owed to you but not yet paid by customers. This account will have a balance when you let customers purchase something on credit and/or when you create an invoice, for example, unpaid invoices from schools or other customers, pre-orders, and special orders.

Accounts Receivable is a current asset because it converts to cash once it is paid, and all receivables are payable within one year. If you have receivables outstanding that are more than a year old, you really need to look at that and clean it up. Generally, you should only offer invoicing terms of no more than 60 days and follow up to ensure those invoices are paid on time (much like your vendors do with you). The longer an invoice goes past the due date unpaid, the harder it gets to collect, so make sure to follow up.

Other receivables could include taxes receivable (like a tax refund your business is expecting or an Employee Retention Credit refund that you may or may not ever receive), employee advances they're expected to pay back, or a loan to a business partner.

The accounts receivable number that shows on your balance sheet is the cumulative amount of all outstanding invoices and anything else outstanding that is not yet paid.

## Current Asset: Inventory

In most cases, inventory will be your largest current asset account. It's the cumulative (or current) wholesale (or "at cost") value of everything in the store that's for sale: books, sidelines, cards, toys – everything you hope to sell within a year. This brings up an important point: when we talk about **cost of goods sold**, that should include any materials you use to make things you sell in your store. For example, if you make your own candles to sell, the cost of the wicks, wax, glass jars, etc. should be accounted for in the value of the inventory and in cost of goods sold, much like the ingredients for our lemonade.

This is also why it's important to verify the value of your inventory by conducting a physical inventory at least annually to ensure the value on the balance sheet is accurate to a reasonable degree.

In your **chart of accounts**, you may decide to place your inventory into categories, like new books, used books, remainders, cafe, sidelines, etc. This can be helpful on a balance sheet as well so you can see the value of your inventory on-hand in any given category at any given time.

If you look at the "at cost" value of your inventory in your point of sale system, it will only be as accurate as your receiving practices, so this is a good reason to have a detailed receiving process.

### Fixed Assets & Depreciation

Fixed assets are physical assets with a life expectancy greater than one year. Your largest fixed assets will be furniture, fixtures, equipment, and if you own it, your building and/or a bookmobile or other store vehicle. Fixed assets are anything with value that you don't expect to turn into cash within a year.

Most fixed assets eventually need to be replaced (land is an exception). Depreciating fixed assets accounts for that loss in value of the asset over time.

When you acquire a fixed asset, it's important to ensure you account for all associated costs in purchasing that asset. For example, if you incurred delivery fees, installation costs, or professional services needed to set up and integrate the asset, and/or indirect costs like sales tax, you should include all those into the total expense of the asset when recording in your bookkeeping. The full amount represents the asset's original cost in your accounting records.

### Intangible Assets

Intangible assets provide value even though you can't physically touch them. These include trademarks, copyrights, branding, domain names and websites, and the reputation of the business itself. They also include goodwill, digital assets, customer lists, and employee knowledge. Intangible assets only depreciate if they have a finite useful life, otherwise they remain at their original value.

Intangible assets can be created or acquired and either definite or indefinite. They're considered fixed assets, and their value can increase over time. For example, you may establish a copyright or a trademark, and when you do, you can write off the expenses from the process, such as filing the application, hiring a lawyer, or other related costs.

An indefinite intangible asset stays with your business as long as it remains in use, for example, a trademarked name; whereas, a definite intangible asset is something that loses its value after a specific timeframe, like if you purchase a copyright to allow you to use something for a certain period of time.

When intangible assets have an identifiable value and lifespan, you would record them in your accounting software, and they would appear on your balance sheet as fixed assets with a value equal to the cost of creating or acquiring them, considering their amortization schedules. If you want to try to value intangible assets of your store, talk to your accountant, as this isn't something you should do on your own because it's complicated.

## 10.3 LIABILITIES: WHAT YOU OWE

**Liability** can mean a legal or regulatory risk or obligation, but here, liabilities are the opposite of assets. If assets are what you own, then liabilities are what you owe. For example, **accounts payable** are amounts you owe in credit, like terms with a vendor or a credit card balance or a loan. If you're on an accrual basis, accrued expenses are also a liability.

Like assets, liabilities can either be current, meaning you have to pay them within one year, or fixed, meaning you have longer than one year to pay them. Current liabilities include accounts payable, wages payable, sales tax payable, credit card debt, gift cards, prepaid special orders, preorders, and store credit. Fixed liabilities include notes payable (loans or other long term debts), mortgages, car payments, or any other type of loan.

Liabilities are debts used to finance operations and pay for expansions or growth. As discussed in Chapter 3: Vendor, Debt, & Tax Management, not all debt is bad. Hopefully, your liabilities are productive debt helping you to continue operating.

Just like with assets, your current liabilities are listed first on your balance sheet, followed by your fixed liabilities. Let's take a closer look at each category.

## Current Liability: Accounts Payable

**Accounts payable** are considered current liabilities because they are generally due in less than a year. Accounts payable are also generally inventory or expenses purchased on credit from a vendor.

If you order inventory on terms with vendors, you will have accounts payable. These are basically invoices owed, or "open invoices." If you don't have terms and prepay everything with a credit card, however, you will have a current liability for the credit card debt, but no accounts payable.

For example, say you purchase books from a publisher, and they provide you terms, let's say Net 30. The invoice is entered into your accounting system as of the invoice date, but it isn't due until next month, so at the end of this month when it is still outstanding, it is called a liability, more specifically, accounts payable. Your balance sheet will show these amounts in aggregate rather than detailing them out by vendor, and that aggregate total is a good indicator of the debt you have that will need to be paid soon.

The accounts payable number on your balance sheet is pulled from all of your entered invoices and bills, so reviewing the accounts payable aging report, which shows the age of those bills, would be a useful tool to spot problems on a micro level.

## Current Liability: Gift Cards

Gift cards and gift certificates, although physically different, are treated generally the same for bookkeeping and accounting purposes. When gift cards are sold to customers, they become liabilities because the customer has already paid you, but you still owe them the inventory they paid for.

It can be confusing to think of gift card balances as liabilities, since they generate cash now in exchange for something that will get redeemed, possibly, at a later date. But if you think of it as a kind of merchandise IOU that you have to pay back to the gift card holder at some point, that may help you see why it is a liability and not an asset.

Due to the number of people who lose their gift cards or simply never use them, the liability balance will naturally grow over time. Make sure you research the laws in your state and talk with your accountant about how to handle unused gift cards and gift card breakage.

### Current Liability: Taxes Payable

**Taxes Payable** can include amounts owed to a state agency for sales tax collected from customers, but they can also include amounts the business may owe on state or federal taxes if applicable, depending on the entity type. Taxes payable would generally be a current liability because they would be due in less than one year.

### Fixed Liability: Notes Payable

**Notes Payable** can include general business loans, lines of credit, vehicle loans, merchant loans, and mortgage loans. These are generally money you owe to a lender, whether an institution or an individual, and generally last longer than one year. Notes payable are often used to purchase assets. Some notes payable are secured, meaning the asset you purchased with it is used as collateral on the loan and the creditor can claim that asset if you default or don't pay the loan.

If you're on an accrual basis, you may classify a portion of a note payable as current, or owed within one year, and the rest as fixed, or owed later than one year from now. This is done so your current liabilities can easily be identified and used to properly calculate ratios when third party entities like banks or potential buyers look at your balance sheet.

## 10.4 EQUITY: WHAT YOU'RE WORTH

In the simplest terms, **equity** is what you're worth, and is all of your assets minus all of your liabilities. Equity is always calculated, never manipulated.

On a business's balance sheet, the difference between its assets and liabilities shows how much equity the business has. For example, if a store's assets equal its liabilities, the owner has zero equity, because if the business is liquidated, meaning everything is sold off to pay all the store's debts, there is no money left for the owner(s).

Having no equity in the business may mean that the owner has taken out more value than has been earned or contributed. It could also indicate the business has lost more money than ownership invested, leaving no monetary value inside the business.

It is possible to operate with a very small equity balance or negative equity in the early stages of a business due to initial losses.

What shows under equity on your balance sheet depends on your business structure. If you're a corporation, you may see **retained earnings**. If you're an LLC, this is where owner contributions and draws would appear if you're an owner who doesn't pay yourself a salary, but rather takes "draws" from the business when there's enough money to do so.

Since equity is calculated, not manipulated, this means decisions you make as an owner affect equity. For example, since equity is ownership's stake in the business, when an owner contributes capital, that increases equity because it's considered an investment in the business. When an owner takes a draw, that means they're "drawing" from their equity investment, so that decreases equity.

If the owner pays themselves a salary instead of taking an owner's draw, that would not be a draw against equity; instead it's considered employee wages and would show under payroll expense on the profit & loss statement.

Looking at the equity calculation:

**Equity = Assets - Liabilities**

You can see that if your assets are more than your liabilities, your equity will be positive, and if your liabilities are more than your assets, your equity will be negative. Very simply, you always want the value of your assets to outweigh the value of your liabilities by as much as possible, which will give you the highest equity.

When third parties like banks and buyers review your balance sheet, they want to see positive equity, low liabilities, and high assets, as that makes your business the most valuable.

## 10.5 ANALYZING YOUR BALANCE SHEET

Generally, third parties like banks and potential buyers are the ones who will look at your balance sheet to determine the value of your business, but your balance sheet shows you things none of your other financial reports do, so it's important for you to review it at least quarterly to check in on the health of your business. Here are some things to look for.

### Analyzing Assets

With assets, your cash balances are important. What's nice about the balance sheet is that it shows your total cash all in one place, from your bank accounts, to your register, to your petty cash (if you record all of it). You can look at the cash balance and easily calculate your **break even** and burn rates to see how long you can operate without additional sources of cash.

You also want to make sure your cash balance is stable. If you notice wild swings in cash, that's an indicator your business isn't stable. If you see a swing to the negative, it means you've spent a lot of cash, which is an obvious red flag. However, if you see a ton of extra cash, that can also be concerning. It's worth investigating to see if you're coding something incorrectly in your bookkeeping. And if you really do have a lot of extra cash sitting around, consider what you might do with it. Should you build up your savings account?

Invest in growth or new assets? Give your employees a raise? Pay yourself, or pay yourself more? You want to make sure to invest extra cash back into the business.

Looking at accounts receivable quarterly is also a good idea. This is money other people owe to you, so you should collect on it. If you notice a high accounts receivable number, you should investigate to see how old the outstanding invoices are and contact those customers to pay. It could also mean you haven't closed out invoices in your bookkeeping.

Inventory is, of course, an asset to pay close attention to, and the only place you'll see inventory totals is on your balance sheet. You want to ensure your inventory totals match your point of sale system (one reason to do an annual physical inventory check), and you'll want to watch your total inventory levels.

If you notice your inventory levels are too high, it may be time for a sale or to do returns. It could also mean you're experiencing "inventory creep," which is when you plow all your extra cash into inventory. If you do this, you can be left with a lot of inventory and low cash levels.

If you notice your inventory is too low, on the other hand, hopefully this means you're turning over inventory at a higher rate, which means higher sales, and you can invest some money into growing your inventory.

Keeping an eye on your inventory levels on your balance sheet can help you keep your inventory stable, which helps with cash flow.

Generally, if you notice your assets seem really high, you'll want to check your accounts receivable to make sure you're collecting on and closing out invoices. You'll also want to look at your inventory levels to make sure you're adjusting them to match your point of sale and to lower inventory amounts as you sell things. You'll also want to check to make sure you're depreciating assets as necessary.

## Analyzing Liabilities

As far as liabilities, you want to make sure your accounts payable remains stable. Generally, you'll want to compare your accounts payable to your cost of goods sold percentage to make sure it's not getting out of control. If you know your COGS generally hangs around 55% of total sales, you don't want outstanding accounts payable to get much higher than that as a percentage of your projected sales. For example, if your average COGS percentage is 55%, and you project $50,000 in total sales for December, you wouldn't want much more than $27,000 (about 55% of projected sales) in outstanding accounts payable.

You also want to take into account the ebbs and flows of the retail year. Your accounts payable may be high in November when you've just stocked for the holidays, for example, but, you're projecting a lot more sales. In this case, you want to make sure your accounts payable isn't more than 55% of your projected sales. Conversely, accounts payable should be low in

January. If it's high, that's a red flag, because your projected sales will be lower. All of your sales money should not be going toward accounts payable, or you won't have money left to pay other bills and wages.

It's also good to keep track of gift card liabilities. In some states, if gift cards aren't claimed after a certain period of time, you could owe that money back to the state as "unclaimed funds." If your gift card liability is high, you may need to claim breakage, which means you received money without providing the customer with something in return.

If you use gift cards as a way to accept donations, meaning customers purchase them with the intention of never redeeming them, instead of coding those sales as gift cards, you would code them as "donations" or "tips" in your bookkeeping. This is important to ensure your gift card liability doesn't end up higher than it should be because of donations.

The biggest issue with gift cards is that, at some point or another, you're going to have to claim that money as income, whether it's donations, or redeemed, or breakage, or (in some cases) you'll have to pay it to the state. That's why it's important to keep an eye on this number on your balance sheet. Make sure you discuss gift cards with your accountant to determine how you should record these things in your bookkeeping and how your accountant recommends you deal with a high gift card liability account.

Finally, you can look at your total liability numbers on your balance sheet to determine your **debt-to-equity ratio** and whether you have too much debt. Your debt-to-equity ratio is calculated by dividing your total liabilities by your equity. This shows how much debt your business carries relative to the owner's equity in the business. The higher this ratio, the more debt you carry. A low debt-to-equity ratio means the business is mostly funded by the owners; whereas a high ratio means the business is mostly funded by lenders/debt. This ratio is also something banks will look at before agreeing to lend you money.

Overall, if your liabilities are increasing, you'll want to investigate why. Did you take out a major loan? Do you owe a lot in accounts payable? Have you not dealt with gift card breakage? Did you charge a lot of inventory to a credit card? While debt can be useful for growth and investment, excessive debt can lead to financial distress and even bankruptcy. If you review your balance sheet regularly to monitor your debt, you'll be able to catch issues earlier to better manage or fix them.

## Analyzing Equity

There are only a few ways to affect equity. Remember the equation:

**Equity = Assets - Liabilities**

Due to that equation, if you have more assets than liabilities, your equity will be positive, and if you have more liabilities than assets, your equity will be negative. Purchasing or increasing assets, decreasing or paying off liabilities, and an owner putting their own

money into the business will all increase equity. Conversely, losing assets, increasing liabilities, and taking owner's draws will all decrease equity.

Of course, if your equity is high, that's great! It means you have more assets than liabilities, and your business is strong.

If your equity balance is negative or zero, you'll want to make sure your liabilities aren't increasing in relation to your assets. It's more common to have lower equity if your store is newer because you may not have had a lot of time to gain assets yet. Negative equity could also mean you've taken on too much debt or have incurred significant losses. Another reason for lowering equity could be assets fully depreciating after ten years or so and falling off the books.

If you find that you have negative or zero equity, you can try to cut expenses, sell off assets to pay off debt, or renegotiate your debt. One thing you may find helpful is taking out a bank loan to pay off a high interest credit card. This allows you to pay off that debt in less time and with a much lower interest rate, versus not being able to pay it off at all.

## SUMMARY

### Why It Matters

The **Balance Sheet** can help pinpoint your store's weaknesses and help you make informed purchasing and investing decisions. It also shows your equity. Every business decision you make impacts your balance sheet. Your balance sheet also provides investors, loaners, banks, etc. a basis for evaluating your store's financial stability. Knowing how to read your balance sheet can help you make decisions that affect the long-term viability of your business.

### 10.1 The Basics

The balance sheet is a financial report that shows your business's assets, liabilities, and equity at a specific point in time. It will reveal aspects of your business not shown in other reports. All the numbers presented on your balance sheet come from somewhere else in your bookkeeping, meaning you don't manipulate the balance sheet directly. The balance sheet is based on the fundamental equation:

**Equity = Assets - Liabilities**

### 10.2 Assets: What You Own

**Assets** are what your business owns, both liquid (like cash) and solid (like property and inventory). Intangible Assets have no physical substance but can still be sold, licensed, and transferred. They must have a quantifiable value and lifespan to be recorded as an asset. There are two types of

assets: fixed and current. **Current** assets are those you could theoretically convert into cash within one year or are already cash; whereas **fixed** assets are those you cannot easily convert into cash within a year. Current assets include cash, accounts receivable, and inventory. Fixed assets depreciate over time and include furniture, fixtures, equipment, and if you own it, your building and/or a bookmobile or other store vehicle. **Intangible assets** include trademarks, copyrights, branding, domain names and websites, and the reputation of the business itself. They also include goodwill, digital assets, customer lists, and employee knowledge. Intangible assets only depreciate if they have a finite useful life, otherwise they remain at their original value.

### 10.3 Liabilities: What You Owe

**Liabilities** are the opposite of assets. Like assets, liabilities can either be current, meaning you have to pay them within one year, or fixed, meaning you have longer than one year to pay them. Current liabilities include accounts payable, wages payable, sales tax payable, credit card debt, gift cards, prepaid special orders, preorders, and store credit. Fixed liabilities include notes payable (loans or other long term debts), mortgages, car payments, or any other type of loan. Liabilities are debts used to finance operations and pay for expansions or growth.

### 10.4 Equity: What You're Worth

**Equity** is what you're worth, and is all of your assets minus all of your liabilities. Equity is always calculated, never manipulated. This means decisions you make as an owner affect equity. If your assets are more than your liabilities, your equity will be positive, and if your liabilities are more than your assets, your equity will be negative. Very simply, you always want the value of your assets to outweigh the value of your liabilities by as much as possible, which will give you the highest equity. When third parties like banks and buyers review your balance sheet, they want to see positive equity, low liabilities, and high assets, as that makes your business the most valuable.

### 10.5 Analyzing Your Balance Sheet

With assets, make sure your cash and inventory balances are stable and review accounts receivable at least quarterly and collect. With liabilities, make sure your accounts payable is stable and pay attention to your gift card liability. Check your **debt-to-income ratio** regularly to ensure you don't carry too much debt. If liabilities are increasing, investigate why. With equity, purchasing or increasing assets, decreasing or paying off liabilities, and an owner putting their own money into the business will all increase equity. Conversely, losing assets, increasing liabilities, and taking owner's draws will all decrease equity. If you find that you have negative or zero equity, you can try to cut expenses, sell off assets to pay off debt, or renegotiate your debt.

## KEY TAKEAWAYS

- The balance sheet is a financial report that shows your business's assets, liabilities, and equity at a specific point in time. It will reveal aspects of your business not shown in other reports.
- All the numbers presented on your balance sheet come from somewhere else in your bookkeeping.
- The balance sheet is based on the fundamental equation: Equity = Assets – Liabilities.
- Assets are what you own; liabilities are what you owe; equity is what you're worth.

## TEMPLATES & RESOURCES

- **Example**: Balance Sheet Example 1 – Large Store
- **Example**: Balance Sheet Example 2 – Medium Store
- **Example**: Balance Sheet Example 3 – Small Store
- **Example**: Lemonade Stand Balance Sheet

## KEY TERMS

- Accounts Payable
- Accounts Receivable
- Assets
- Beginning Cash
- Break Even
- Budget
- Burn Rate
- Cash Equivalents
- Cash Flow
- Cash Flow Statement
- Chart of Accounts
- Cost of Goods Sold (COGS)
- Current Assets
- Debt-To-Equity Ratio
- Depreciation
- Ending Cash
- Equity
- Fixed Assets
- Intangible Assets
- Liabilities
- Modified Cash
- Notes Payable
- Profit & Loss Statement
- Retained Earnings
- Taxes Payable

## REVIEW QUESTIONS

**Short Answer**:

- Are liabilities that are due more than one year in the future current or fixed?
- What category is outstanding gift cards listed in on the balance sheet?
- What is the formula to calculate Equity?
- What are some examples of fixed assets?

## ANSWER KEY

- Fixed
- Liabilities
- Equity = Assets – Liabilities
- Furniture, fixtures, equipment, building, land, vehicles

# FINANCIAL RATIOS

## Quick Ratio

**What It's Used For**: The quick ratio communicates how well a company will be able to pay its short-term debts using only the most liquid of assets. The ratio is important because it signals to internal management and external investors whether the company will run out of cash. The quick ratio also holds more value than other liquidity ratios, like the current ratio, because it has the most conservative approach on reflecting how a company can raise cash.

**Formula**: Liquid Assets (Current Assets – Inventory) / Current Liabilities

## Current Ratio

**What It's Used For**: The current ratio is a liquidity ratio that measures a company's ability to pay short-term obligations, or those due within one year. It tells investors and analysts how a company can maximize the current assets on its balance sheet to satisfy its current debt and other payables.

**Formula**: Current Assets / Current Liabilities

## Return on Equity (ROE)

**What It's Used For**: Return on equity (ROE) is a measure of financial performance calculated by dividing net income by shareholders' equity. Because shareholders' equity is equal to a company's assets minus its liabilities, ROE is considered the return on net assets. ROE is considered a gauge of a corporation's profitability and how efficient it is in generating profits. The higher the ROE, the more efficient a company's management is at generating income and growth from its equity financing.

**Formula**: Annual Net Income / Equity

*Chapter 11*

# Profit & Loss Deep Dive

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Run your profit & loss statement.
- Fully understand how to analyze it.
- Take action on your analysis.

## WHY THIS MATTERS

Your **Profit & Loss Statement (P&L)** shows your business's revenue and expenses over a specific period of time. It's considered one of the most important financial statements because it shows your ability to make a profit. It's difficult to stay in business if you operate at a loss for too long, and as it implies in the name, the Profit & Loss Statement is one of the best ways to monitor this. Also, the bulk of your federal and state income tax reporting comes from the data on your Profit & Loss Statement, and no one wants the hassle of an IRS audit. Because the P&L shows both your income and your expenses, it's also a great basis for budgeting.

## CHAPTER OUTLINE

**11.1** The Basics
**11.2** How to Generate a P&L Statement
**11.3** Top Line vs Real Revenue
**11.4** Cost of Goods Sold (COGS)
  **11.4.1** Closing the Books
  **11.4.2** Income/COGS Subcategories
  **11.4.3** Cash vs Accrual
  **11.4.4** COGS vs COGS Percentage
**11.5** Gross Profit Margin Percentage
**11.6** Expenses
  **11.6.1** Contra Accounts
  **11.6.2** Fixed vs Variable Expenses
**11.7** Other Income & Expense
**11.8** Net Income
**11.9** Owner's Pay vs Profit
**11.10** P&L Variations
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions

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## 11.1 THE BASICS

The **Profit & Loss Statement**, also known as an income statement, is a financial report that summarizes your **Net Revenue**, **Cost of Goods Sold**, **Gross Margin**, **Expenses**, and **Net Income** over a specific time period. This financial statement provides information about your store's ability to generate sales, manage expenses, and make a profit.

When you run this report, think of it like the speedometer in your car. It shows you how fast your business is moving and how much you're making and spending, but it doesn't tell you if, when, or how to change your speed, it is just an indicator. You want to use it to determine how fast (or slow) your business is moving and help you make financial decisions and strategies based on that information.

Comparing P&Ls from different accounting periods is important because it will show you how your business changes over time and trends, which can sometimes be more meaningful than knowing whether you made a profit or loss during one specific period.

## 11.2 HOW TO GENERATE A P&L STATEMENT

Before generating a P&L statement, you first need to decide what period of time you are analyzing and make sure your bookkeeping for that period has been done. It's typical to run P&Ls for a year, a quarter, or a month. If you use accounting software, it will easily generate a P&L for you. If you're not using accounting software, then you can refer to the Excel template in **Templates & Resources** and fill in your own numbers. The template has some formulas built in, so if you add other subcategories, just double-check that it's still calculating correctly. When you're generating P&Ls from within your accounting software, it's important that you know whether or not cost of goods sold has been calculated for the period you are reporting on.

The P&L displays information from four sections of your **Chart of Accounts**: **Income**, Cost of Goods Sold, Expenses, and **Other Income/Expense**. The information is summarized over time and includes some simple calculations on the data.

## 11.3 TOP LINE VS REAL REVENUE

Net Revenue is the first thing that shows on your P&L. Because of its location on the report, net revenue is also referred to as "top-line revenue." The term "net" means that something has been subtracted from the amount. The reason this is "net" revenue even though it's at the top is because customer returns should already be subtracted out.

Some P&Ls break out income into subcategories, such as new books, used books, café, sidelines, etc. Sometimes, returns and customer discounts are also separated out as **contra** subcategories of income. The detail you wish to see here is up to you and your business needs.

If you use accounting software, it will automatically include subtotals on your P&L, along with some lines that subtract one set of

numbers from another. These lines are called "netting lines." The first netting line on your P&L shows your **Gross Profit**. It's called "gross profit" when it's showed in dollars. This number can also be displayed as a percentage of revenue. When shown as a percentage, it's called **Gross Margin**. To calculate gross profit, you subtract total COGS from total income.

Your gross profit is your "real revenue," meaning this is what your business actually runs on. Your gross profit is the money you can spend to cover business expenses. Because of this, it's generally more useful to look at gross profit instead of net revenue (top-line sales). Since booksellers don't have a lot of control over vendor terms, the main control you have over your financials comes from how you choose to spend your gross profit and your prowess in increasing top-line sales.

## 11.4 COST OF GOODS SOLD

In Chapter 7: Accounting Basics, you learned the official calculation for cost of goods sold:

**COGS = Starting Inventory + Net Purchases - Ending Inventory**

There are two ways to code your **Purchases**, which are your invoices and return/credit memos, in your accounting software.

### Method 1: Purchases Account

Under this method, you code inventory purchases directly into a temporary "purchases" account. This is a type of COGS account and shows on your P&L right away. Once your accountant calculates COGS, then theoretically they will zero the purchases account and debit a separate cost of goods sold account so that your P&L shows an accurate cost of goods sold. If you look at your chart of accounts, it should show two different COGS accounts with this method.

The issue with this method is that when viewing your P&L for a period, it may not be clear to you whether COGS has been calculated or not. Because of this, we strongly recommend discussing with your accountant whether there's a way to make it crystal clear on the P&L what your actual COGS is.

### Method 2: Inventory Method

Most bookstores use the inventory method. This means that when you purchase inventory, whether outright or on terms, your inventory account is debited in your accounting software so that its balance increases. On the other side of the transaction, either your bank account, credit card account, or **Accounts Payable** account is credited so its balance decreases.

As you learned in Chapter 10: Balance Sheet Deep Dive, assets show on your **balance sheet**, not on your P&L. Thus, inventory should not show as an expense on your P&L until the items actually sell. At that point, the IRS allows you to figure out the cost of the items and do a journal entry moving the cost amount – and only that amount – from your inventory asset account to your cost of goods sold expense account. Only once that journal entry is done should inventory expense appear on your P&L,

and it should be called cost of goods sold. Stores are required to calculate COGS yearly, but many also do it monthly. The stores doing daily COGS are usually just having their point of sale system auto-calculate it, which means they are not using the traditional COGS formula. This is fine as long as you and your accountant are in sync.

If you file a Schedule C with your taxes to report your business income, that form includes lines for starting inventory, purchases, and ending inventory, then for your calculated cost of goods sold. If the only data you have is the calculated COGS from your point of sale system, you simply can't extrapolate from that to get the other pieces of info. It's a good idea to take a look at your last tax filing to see exactly how your accountant is documenting your cost of goods sold. If you're using your point of sale figures, but your accountant has entered data for the entire formula onto your tax form, then you're probably not on the same page and need to have a discussion as soon as possible.

### 11.4.1 CLOSING THE BOOKS

Because cost of goods sold is a calculation, it's standard to set a closing date in your accounting software after you calculate it to ensure that none of the underlying data for the period changes after you've made the calculation. Some publishers don't send you separate return credits – they just appear on your monthly statement. And if you're getting your statements by mail, you may not learn about a credit dated January until some time in February. You don't want to enter that credit into your accounting software under its January date if you've already calculated your COGS for January. If you've set a closing date of January 31st and you try to enter the credit with a January date, the software will warn you. When that happens, you just change the date of the credit to February 1st so it will be included in the next month's calculation.

When you close your books at the end of the fiscal year, you traditionally are also resetting all your P&L balances to zero and transferring any net income or loss to the equity account on your balance sheet. Modern accounting software makes this closing entry for you automatically.

### 11.4.2 INCOME/COGS SUBCATEGORIES

You may have a single category for both income and COGS, or you may break each into multiple categories. The American Booksellers Association (ABA) is currently encouraging you to track these different departments separately: new books, used books, calendars, café/food/beverage, and other gift, but you could also have others, such as remainders. Though it's more work, it's also useful to calculate the COGS for each category separately to help you make business decisions about where you might want to grow or shrink your inventory or what additional expenses may be a profitable investment. If your most profitable department is gift, you may want to invest in special fixtures to display gifts, extra training for your staff on how to sell gifts, or pay for your gift buyer to attend a gift trade show.

With shipping income, it's possible to have a shipping subcategory as part of your top-line income or under other income; however, the ABA prefers that you list shipping income as a contra subaccount under postage expense. If your state requires you to charge sales tax on shipping income, be mindful that moving the account around in your chart of accounts could affect that reporting.

### 11.4.3 CASH VS ACCRUAL

If you'll remember, cash basis accounting means that income and expenses that were made and paid during the reporting period are what will show on your reports, whereas accrual accounting means that what shows on reports are income and expenses that were billed (not necessarily paid) during the reporting period. COGS is always calculated on an accrual basis, even if the rest of the report is on a cash basis.

It's possible for stores that use modified cash basis to have cash and accrual reports that don't match. For example, if you take a school or business-to-business order, deliver the books before you receive payment, then keep an open order/invoice in your point of sale system until you receive the payment, your accrual and cash reports will match. However, if you actually ring the sale through your point of sale system before you receive the payment for whatever reason, your accrual and cash reports may differ. In this case, the accrual report would show the income in the period you rang the sale through your system, whereas the cash report would show the income when you actually received the payment.

Since COGS is always calculated on an accrual basis, that number should always be the same no matter which way you run the report.

### 11.4.4 COGS VS COGS PERCENTAGE

The standard P&L shows COGS as a flat number; however, you may want to also view it as a percentage. To turn your COGS into a percentage, you divide COGS by net revenue. You can either divide total COGS by total net revenue, or if you have subcategories for new books vs used books in both your income and COGS, then you can get different percentages for each type of inventory. You can usually get your accounting software to calculate COGS percentage for you on the P&L with a "customize" function. COGS percentage is useful for comparisons, either your business from year to year or also to compare to other businesses within your industry.

Keep in mind that COGS percentage also reflects your discounting policies. Imagine two businesses both source their inventory at the same 40% discount and sell exactly $60,000 worth of inventory at cost each year, and thus have the same COGS. One business sells everything at full retail price, so their income is $100,000. The other business discounts everything 20%, so their income is only $80,000. In this case, the first business has a COGS percentage of 60% ($60,000/$100,000). The second business, however, has a higher COGS percentage of 75%, because although they spent the same amount of money on inventory, their income was less ($60,000/$80,000).

The standard COGS percentage (combined book and non-book) from ABACUS 2021 is 54.5%. If your COGS percentage is higher than the ABACUS average, you may want to consider looking at your discounting policies.

## 11.5 GROSS PROFIT MARGIN PERCENTAGE

As stated above, your gross profit is what's left after your subtract your COGS from your net revenue. You can also express gross profit, or "real revenue," as a percentage, in which case it's called your gross margin. COGS percentage and gross margin should always add up to 100%. If your COGS percentage is 60%, for example, then your gross margin is 40%. This means that for every $1 of income earned, $0.60 goes to inventory cost and $0.40 is available for everything else - occupancy, payroll, operations, owner's pay, and profit.

## 11.6 EXPENSES

After the gross profit line on the P&L comes all your **expenses**. Expenses are totaled, then subtracted from your gross profit to show your **Net Ordinary Income**. Several P&L lines start with the term "net," and in accounting, this usually refers to a combination of positive and negative amounts.

Expenses are the basis of your operating budget. It can be helpful to think of your expenses as belonging to one of three categories: Payroll, Occupancy, or Operating Costs. Payroll includes your W-2 employees and any benefits you provide to staff and owners, and may or may not include owners pay depending on your business structure. Occupancy covers rent, utilities, business license, repairs, cleaning, and anything to do with your physical location or locations. Operating costs include everything else, such as marketing, supplies, software, liability insurance, etc. The percentage guidelines from ABACUS on each of these expense categories can be helpful for budgeting or even negotiating with landlords.

### 11.6.1 CONTRA ACCOUNTS

**Contra accounts** are a special type of account you may or may not be using, but it is important to understand how they work. These accounts have the opposite balance from a similar type of account, or contra to the normal balance. The benefit of a contra account is to be able to keep track of the balance so you know how much you receive each year in relation to how much you spend in that category.

Discounts are a contra revenue account - they have a negative balance contra to revenue, which is positive. You may have this type of account if you want to record your discounts and see what they're costing you.

Co-Op Marketing is a contra expense account - they have a positive balance contra to an expense, which is negative. You may use a co-op contra subaccount under marketing to track the co-op you receive and offset your marketing costs. Some stores put co-op as a contra account against COGS expense instead of a contra marketing expense. The key is to be consistent with where you put it.

Accumulated **depreciation** is a contra asset account. Accumulated depreciation represents how much **Fixed Assets** on your balance sheet have been written down over time. Most likely your tax advisor is making this entry for you every year – debiting depreciation expense and crediting accumulated depreciation. This is a helpful expense to reduce your taxes due!

Shipping and handling income is a contra expense account with a credit balance. Stores record the monies they receive from customers for shipping to them as a credit balance against all the freight out costs to ship books to customers and publisher returns.

Contra accounts help provide clarity in financial reports. The more things you track consistently and with enough detail, the more your reports will tell the story of your business and give you things to work on to ensure you remain profitable.

### 11.6.2 FIXED VS VARIABLE EXPENSES

Expenses can also be categorized as fixed or variable. Fixed means they don't change based on your sales, though they could vary based on other factors. For example, utilities are considered a fixed cost even though the actual amount varies based on the weather and other situations. Rent is also a fixed expense. In both of these cases, you must pay that bill whether you have a stellar sales month or a dismal one. The classic variable expense for bookstores is cost of goods sold, which of course varies based on how much you sell. Another example of a variable expense is postage/shipping to customers.

It's useful to categorize your expenses as fixed or variable to help you figure out the minimum amount of cash you have to pay out each month, no matter what. You can do this by taking your previous year's total fixed expenses, then divide that number by 12. This averages out things like utilities or supplies that can vary based on usage.

## 11.7 OTHER INCOME & EXPENSE

After all your expenses are listed on your P&L, you'll see your net ordinary income, which is the income you made from regular business operations. Below that comes our **Other Income** and **Other Expenses**, which is income you made or expenses you paid that are outside of your "ordinary" operations. Generally, for bookstores, ordinary income comes from selling books, sidelines, and potentially café operations, all of which have a cost of goods component.

These days, though, bookstores have found other streams of income as well. For example, you may sell services to independent authors, such as self-publishing guidance, event hosting, and shelf space. Other Income also usually includes space rental, interest earned, affiliate income (like from Bookshop.org and Libro.fm), and gift card breakage, which you learned about in Chapter 10. Other Expenses can include interest paid, depreciation, and amortized costs.

You could argue that all of this is related to primary operations, but for the sake of ABACUS and how they prefer data to be

reported, these are all considered “other” income or expenses.

## 11.8 NET INCOME

The last netting line on the P&L is **Net Income**, which is also called your “bottom line.” Since P&L stands for profit & loss, many small business owners look at the last line, net income, and declare themselves profitable if it’s positive. However, owner’s pay may not be included on your P&L depending on your business structure, so your P&L may need an adjustment to determine true profitability.

As you learned in Chapter 10, if owners take draws on equity, as with a sole proprietorship, single-member LLC, or a partnership, then owner’s pay will not appear on your P&L, because it instead decreases equity on your balance sheet. In this case, to see your true profit or loss on your P&L, you need to do yet another netting and subtract total owner draws for the period from the P&L’s net income.

Keep in mind that if you only calculate COGS at the end of the year, then each monthly P&L you run before that number is calculated may only show income and your operating expenses and your biggest expense of all – inventory – may not be included. Because that can make for such a surprise, calculating your COGS on a monthly or at least quarterly basis is useful.

## 11.9 OWNER’S PAY VS PROFIT

You may wonder why it’s important to separate out profit from owner’s pay if your P&L doesn’t already do so. Owner’s pay should fairly compensate you for the work you do in the store. To determine if your pay is fair, think about how many staff you’d have to hire to replace you and what you’d have to pay them. Most owners are not paying themselves enough and thus have a false sense of the profitability and value of their business. This can lead to a rude awakening as you try to transition out of the business by either selling it or replacing some or all of your hours with staff. And if you are an S corporation, keep in mind that the IRS has been cracking down on owners who try to avoid tax by classifying too little of their compensation as wages and taking the bulk as a shareholder distribution.

Profit, on the other hand, is the return on investment (ROI) for the capital the owner(s) invested to start the business. If the owner invested $100,000 originally, are paying themselves a fair owner’s wage, and the store is making $5000 yearly profit above that, then the current return on investment is 5%, which is considered by most financial investors to be a good, but not great return. However, if it took several years before your store generated that much profit, your average ROI will be lower.

To find a buyer for your business, you generally need to be fairly compensating working owners *and* showing a decent profit, though exceptions to this rule can occur.

## 11.10 P&L VARIATIONS

Profit & Loss statements come in many different variations. Here are some you may find useful.

## Previous Year Comparison

The IRS requires you to report a P&L for your tax period; however, you can also run P&Ls that show comparisons over a previous year. This is very useful for showing trends, possible coding mistakes, or other oddities to investigate. Two ways to run P&L comparisons are to look at a comparative P&L for the month - like March 2024 versus 2023 - and a year-to-date comparative P&L for the first three months of the current year and prior year. Look at the percentage change year-over-year and at the net income or loss at the bottom of the report.

## Quarterly Totals

The P&L statement has other options beside cash and accrual. If you have to pay estimated self-employment tax throughout the year, it's useful to run a quarterly statement because if you estimate wrong, you may owe a penalty. But if you can show that most of your profit came in the fourth quarter, then there's a form your accountant can fill out to exempt you from the penalty.

Quarterly reports can also be useful when budgeting if you have seasonality in your sales.

## Totals by Class

If you have different income streams, such as in-store, online sales, events, café, and/or business-to-business sales, you may also want to break your P&L out by those streams so you can see whether growth or weakness is across the board or only in one area. If you separate out sales by category, you will need to figure out ways to indicate these sales types in your point of sale system to get the data to put into your accounting software.

## Year-to-Date Column

Your P&L is also useful for showing your actual expenses to compare to your budget/ spending plan. For budget analysis, it can be useful to run a monthly P&L that also adds a column showing your year-to-date expenditures. For example, if you have a monthly payroll budget, but some months have two payrolls and others have three, it's useful to see your year-to-date numbers to determine whether the yearly average is on track even if this particular month is high.

## 12-Month Trailing P&L

Another type of P&L is the 12-month trailing P&L. You run it based on the twelve months ending at the end of the previous month. So if you're in the middle of June, you'd run it for June of the previous year through May of this year. For the profit part of this report to be useful, you have to calculate COGS on a monthly basis, which is ideal, but not legally required.

If you keep up with bookkeeping and reconciling your monthly statements, the trailing P&L will at least show your current yearly run-rate for income and expenses. If you run it as a previous-year comparison report every month, you can see whether your trends are improving or declining.

### Other Variations

If you are a successful company, you may have multiple locations and would want to see a combined P&L, but also separate ones for each location. As you learned in Chapter 5: Event, Promo, & Co-Op Management, you can create a simple P&L for every event you host to see if it was profitable and worth repeating or to show where you could cut costs to make it profitable if you repeated it. Even if you're a smaller business like a bookmobile or a pop-up shop, it might be useful to track sales and expenses by location or event to see which are more profitable for you. Perhaps one location charges you a booth fee or another is far away and takes more gas to get to.

The beauty of accounting software is not only the standard reports like P&L that are already set up for you, but also the variety of ways you can customize those reports. Once you find a custom set of parameters to use frequently, you can save or "memorize" that custom report, which is a great time saver!

## SUMMARY

**Why It Matters**

Your **Profit & Loss Statement (P&L)** shows your business's revenue and expenses over a specific period of time. It's considered one of the most important financial statements because it shows your ability to make a profit. Because the P&L shows both your income and your expenses, it's also a great basis for budgeting.

**11.1 The Basics**

The Profit & Loss Statement, also known as an income statement, is a financial report that summarizes your **Net Revenue**, **Cost of Goods Sold**, **Gross Margin**, **Expenses**, and **Net Income** over a specific time period. This financial statement provides information about your store's ability to generate sales, manage expenses, and make a profit.

**11.2 How to Generate a P&L Statement**

First, decide what period of time you are analyzing and make sure your bookkeeping for that period has been done. It's typical to run P&Ls for a year, a quarter, or a month. You can easily generate a P&L from your accounting software, or you can keep your own spreadsheet. The P&L displays information from four sections of your Chart of Accounts: Income, Cost of Goods Sold, Expenses, and **Other Income/Expense**.

**11.3 Top Line vs Real Revenue**

Net Revenue is the first thing that shows on your P&L. Because of its location on the report, net revenue is also referred to as "top-line revenue." Your gross profit, which is your Net Revenue - Cost of Goods Sold, is your "real revenue," meaning this is what your business actually runs on. Your gross

profit is the money you can spend to cover business expenses. Because of this, it's generally more useful to look at gross profit instead of net revenue (top-line sales).

### 11.4 Cost of Goods Sold

The official calculation for cost of goods sold is:

**COGS = Starting Inventory + Net Purchases - Ending Inventory**

There are two ways to code your net purchases, which are your invoices and return/credit memos, in your accounting software: using a Purchases account or using the Inventory method. With a Purchases account, you code inventory purchases directly into a temporary COGS expense account called "purchases" that shows on your P&L right away. With the Inventory method, when you purchase inventory, your inventory asset account is debited so that its balance increases. On the other side of the transaction, either your bank account, credit card account, or Accounts Payable account is credited so its balance decreases.

#### 11.4.1 Closing the Books

Because cost of goods sold is a calculation, it's standard to set a closing date in your accounting software after you calculate it to ensure that none of the underlying data for the period changes after you've made the calculation.

#### 11.4.2 Income/COGS Subcategories

The ABA is encourages you to track these different departments separately: new books, used books, calendars, café/food/beverage, and other gift, but you could also have others, such as remainders. Though it's more work, it's also useful to calculate the COGS for each category separately to help you make business decisions about where you might want to grow or shrink your inventory or what additional expenses may be a profitable investment.

#### 11.4.3 Cash vs Accrual

COGS is always calculated on an accrual basis, even if the rest of the report is on a cash basis, which means the number should always be the same no matter how you run the report.

#### 11.4.4 COGS vs COGS Percentage

To turn your COGS into a percentage, you divide COGS by net revenue. COGS percentage is useful for comparisons, either your business from year to year or also to compare to other businesses within your industry. Keep in mind that COGS percentage also reflects your discounting policies.

**11.5 Gross Profit Margin Percentage**

Gross Profit is what's left after your subtract your COGS from your net revenue. You can also express gross profit, or "real revenue," as a percentage, in which case it's called your gross margin.

**11.6 Expenses**

Expenses are totaled, then subtracted from your gross profit to show your Net Ordinary Income. Expenses are the basis of your operating budget. It can be helpful to think of your expenses as belonging to one of three categories: Payroll, Occupancy, or Operating Costs.

**11.6.1 Contra Accounts**

Contra accounts have the opposite balance from a similar type of account, or contra to the normal balance. The benefit of a contra account is to be able to keep track of the balance so you know how much you receive each year in relation to how much you spend in that category.

**11.6.2 Fixed vs Variable Expenses**

Expenses can also be categorized as fixed or variable. Fixed means they don't change based on sales, though they could vary based on other factors, like utilities. Variable means they do change based on sales, like cost of goods sold.

**11.7 Other Income & Expense**

Other Income and Other Expenses is income you made or expenses you paid that are outside of your "ordinary" operations. Examples of Other Income include space rental, interest earned, affiliate income (like from Bookshop.org and Libro.fm), and gift card breakage. Examples of Other Expenses are interest paid, depreciation, and amortized costs.

**11.8 Net Income**

The last netting line on the P&L is Net Income, which is also called your "bottom line." Keep in mind that owner's pay may not be included on your P&L depending on your business structure, so your P&L may need an adjustment to determine true profitability.

**11.9 Owner's Pay vs Profit**

Owner's pay should fairly compensate you for the work you do in the store. Profit, on the other hand, is the return on investment (ROI) for the capital the owner(s) invested to start the business. To find a buyer for your business, you generally need to be fairly compensating working owners and showing a decent profit, though exceptions to this rule can occur.

**11.10 P&L Variations**

Profit & Loss statements come in many different variations. Here are some you may find useful: previous year comparison, quarterly totals, totals by class, year-to-date column, and a 12-month trailing P&L.

## KEY TAKEAWAYS

- Your Profit & Loss Statement (P&L) shows your business's revenue and expenses over a specific period of time and summarizes your Net Revenue, Cost of Goods Sold, Gross Margin, Expenses, and Net Income.
- Gross profit (Net Revenue - Cost of Goods Sold) is your "real revenue," meaning this is what your business actually runs on.
- COGS is always calculated on an accrual basis.
- It can be helpful to think of your expenses as belonging to one of three categories: Payroll, Occupancy, or Operating Costs.
- Owner's pay may not be included on your P&L depending on your business structure.

## TEMPLATES & RESOURCES

- **Template**: Excel P&L Template
- **Example**: Owner's Draw P&L
- **Example**: Simple Breakeven Analysis

## KEY TERMS

- Accounts Payable
- Balance Sheet
- Chart of Accounts
- Contra Accounts
- Cost of Goods Sold (COGS)
- Depreciation
- Expenses
- Fixed Assets
- Gross Margin
- Gross Profit
- Income/Revenue
- Net Income
- Net Ordinary Income
- Net Revenue
- Other Income/Expense
- Profit & Loss Statement
- Purchases

## REVIEW QUESTIONS

**True or False**:

- Gross Profit, or "real revenue," is Sales – Discounts.
- Bookstore utilities are considered a fixed cost.

**Multiple Choice**: Other Income and Expense items include these accounts:

A. Consignment Fees

B. Interest Expense

C. Used Book Sales

D. A & B

E. A, B, & C

## ANSWER KEY

- F
- T
- D

*Chapter 12*

# Creating & Analyzing Your Budget

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Create a spending plan (budget).
- Fully understand how to use and analyze your plan.
- Take action on your analysis.

## WHY THIS MATTERS

A **budget** helps you with operational and strategic decision making, and it is forward-looking, meaning it's based on projections and estimates. A good budget can help you make informed decisions, identify your growth opportunities and where you might be over- or under-spending, weather leaner business times, manage risk, and measure your overall business performance. It also helps you to know not only *what* to spend your money on, but *when* to spend it, which is just as important.

## CHAPTER OUTLINE

**12.1** The Basics
**12.2** Determine Financial Goals & Values
**12.3** Wants vs Needs
**12.4** Align Expenses
**12.5** Categorize Expenses & Revenue
**12.6** Create Your Spending Plan
**12.7** Create an Inventory Spending Plan
**12.7.1** Determining How Much to Spend on Inventory
**12.8** Set Realistic Spending & Revenue Goals
**12.9** Planned vs Actual
**12.10** Set Actions Based on Deviations
**12.10.1** What Causes Deviations?
**12.11** Analyze & Adjust
**12.12** Potential Actions to Take
**12.13** Budgeting Tips & Tricks
**12.14** Tips for Budget Analysis
**12.15** Special Considerations
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions
**Dig Deeper**: Budgeting Challenges & How to Overcome Them

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## 12.1 THE BASICS

A **budget** is an ongoing real-time tool that will help you steer your way to your financial goals. You estimate how much revenue you expect to have, then plan how, when, and where you're going to spend it.

Instead of thinking of budgeting in the traditional way of a line-by-line spreadsheet that accounts for every single dollar you spend, it may be useful to think of it more as intentional spending. If you align your purchases with your financial goals and the things you care most about and track your spending to ensure it stays aligned, you're budgeting!

## 12.2 DETERMINE FINANCIAL GOALS & VALUES

Before you begin to budget, you need to determine your financial goals and values. Knowing your goals when creating a budget enables you to monitor and more clearly comprehend whether your business generates enough income to cover its costs and whether you can actually meet the goals you set.

You should also understand your financial values. This will vary from store to store depending on each unique mission and vision, but values may include sustainability, paying a living wage, giving back to the community, or supporting local causes. Identifying your goals and values can require introspection and collaboration, but it's an essential first step.

Once you understand your goals and values, you will be able to determine if you're spending your money in a way that supports them. This means supporting businesses and organizations with similar values. For example, if environmental sustainability is important to you, you'll want to choose eco-friendly companies and products as a spending priority.

So before you start sifting through your expenses, first make a list of your financial values and your short and long term financial goals. Short-term goals should take around one to three years to achieve and may include setting up an emergency fund or paying down credit card debt. Long-term goals, such as opening a second location or buying and outfitting a bookmobile, take more than three years to reach. Remember, your goals don't have to be set in stone, but identifying them can help motivate you to stick to your budget.

Next, map each of your goals to at least one of your financial values, or determine what kinds of value-driven activities you could do if you accomplish your goal. For example, if you have a goal to pay off all your business loans or pay down credit card debt, you could also make some notes about what you'll be able to do with that money after the loans are paid. Or you may have a goal as a one-person operated store to hire some help to be able to reduce your own hours, which could align with values of paying a living wage and personal freedom.

## 12.3 WANTS VS NEEDS

The next step to creating a good budget is to understand your business **wants** and your business **needs**. A business need is something you require for your store to survive. Needs include utilities, rent or mortgage (if you have a storefront), inventory, payroll (including paying yourself if you're an owner), and a POS system. If any need is cut out, your business will at minimum see a dip, and at worst case have to close. A business want, on the other hand, is anything else that isn't absolutely required for your business to survive. Wants include things like digital subscriptions, meals and entertainment, charitable donations, store decor, and travel. These are all great things! But they are not absolutely necessary for your business's survival.

You should really think about what your minimum needs are because it's easy for wants to creep into your needs budget. For example, even though rent and payroll are needs, is the amount you're paying necessary? For most needs, there are many ways of meeting them. You can and should examine your needs regularly.

Sometimes, your brain will trick you into making a want into a need. For example, you may rationalize new store décor by saying it will entice customers. This is great, but you don't *need* that in order to keep doing business. Identifying the difference between "needs" and "wants" is the cornerstone of money management in general. This enables you to figure out what expenses are necessary and which ones can be deferred or cut entirely. It's not that you should avoid wants altogether, and in fact you absolutely shouldn't! Instead, you can set your wants as goals and start saving for them.

Try categorizing business expenses into wants and needs to help you take a closer look. Your spending plan should include everything you *need* for sure and make sure you can cover those expenses first. Next, figure out what you REALLY want. Are you looking to expand your inventory, open another location, buy a bookmobile, or sell online? What are your future goals? After your needs are met, set money aside for your REALLY WANTS so you can purposely plan and prioritize them. This way, when you're tempted by a want that's not something you REALLY WANT, it will be easier to skip that impulse purchase. Impulse purchases can kill an intentional spending plan pretty quickly.

Remember that savings and paying yourself (if you're an owner) are **needs**. You need to learn to save, especially for emergencies, and to provide all employees, including owners, a living wage.

## 12.4 ALIGN EXPENSES

Now that you know your goals, values, wants, and needs, you can look at your expenses to see what aligns and what doesn't. Start by looking for expenses that are wildly off from your goals and values, and cut those first.

Then, look for expenses you can cut that would be fairly painless. Are there vendors where you might be able to get the same thing for less (for

example, ordering directly from publishers vs from Ingram)? Is there anything you're paying for you aren't really using, maybe digital subscriptions or things you signed up for but forgot about? Look for things you could negotiate, like rent, credit card interest rates, etc. You could even try asking your vendor representatives for a higher discount, free shipping if you don't already get it, and/or better terms.

Next, go through your wants and needs and prioritize your spending based on those. Finally, look more closely at things that feel like a sacrifice even if they don't align. For example, you might have a core value of giving money back to the community, but your business is in a ton of debt. So, maybe you want to pay down the debt first. Or, you might really value freedom of time, so even though you're trying to save to launch a bookmobile, you might decide to hire someone first.

The key to intentional spending is to center your spending around what you most value and realizing your biggest hopes and dreams. Where your money goes should reflect what you value as a business. Take some time to go through your expenses and dig into how your spending aligns with your values, goals, needs, and wants.

## 12.5 CATEGORIZE YOUR EXPENSES & REVENUE

Now that you see how your spending aligns with your goals, values, wants, and needs, the next step is to categorize your expenses. Placing expenses into buckets then calculating the totals as a percentage of your **net revenue** helps you to analyze where you may have budgeting issues. We recommend including these overall categories in your spending plan:

- Cost of Goods Sold
- Payroll
- Occupancy
- Operations

**Cost of Goods Sold** will help you track your inventory spending, and the other three categories align with ABACUS and will make filling out the annual survey that much easier. Organizing expenses into these larger categories helps you look at the bigger picture.

You can also drill down into smaller categories if that works for you, and especially if you want to track something specific. For example, you may add a "supplies" category to operations to specifically track supplies spending, or an "events" category because you're trying to grow your events program.

You may also want to add categories based on wants and needs, or based on goals and values. For example, if you have a goal of paying off loans, you might want to add those numbers to your spending plan, or if you're looking to make an investment like a bookmobile or second location, you could add that. Your categories can be as detailed as you want them to be. Do what works best for you!

Your **Chart of Accounts/Profit & Loss Statement** expense categories could be

useful in deciding which categories you want to track in your spending plan, or you can be more broad. If you want to invest in growing certain revenue streams, such as Bookshop or event sales, you could choose to break out a revenue category like online sales or book sales into its own budget line (as long as you have a reliable way to differentiate and track those sales). Essentially, the categories you add to your plan are the expenses and revenue you want to track.

## 12.6 CREATE YOUR SPENDING PLAN

Now it's time to create your intentional spending plan. There are a million ways to do this, but you'll need a tool of some sort. That could be Airtable, Google Sheets, Excel, your accounting software – any tool you're comfortable with using. If it's complicated and intimidating and therefore you never use it, it's not doing any good.

If you use something like Excel, Airtable, or Google Sheets, you can automate your template with formulas to increase accuracy. If you have to manually enter data each time, your margin of error increases.

If you don't have time to create a spending plan in a separate place, you can also use your accounting software. In your Chart of Accounts, you can make sure all the categories you specified for your plan are there and that your goals are included in the category name. Then, as you do your bookkeeping, you will see the overall spending numbers for those categories and how they match up to your goals right in your software.

Once you have a tool, fill it in with the expense and revenue categories you determined you wanted to track in the last step. You'll then want to set your time period. Are you budgeting for the year, the quarter, the month?

Next, estimate how much revenue you will bring in during the time period and list it at the top of your document. This will be the baseline for what you're able to spend during the time period. And finally, list your planned spending in each category. What do you think you're actually going to spend?

Determining how much you'll make and spend is where historical data comes into play. This is called **forecasting**. You should use history, your profit & loss statement, and your cash flow projections to help you forecast both your revenue and your expenses.

Your profit & loss statement particularly comes in handy at this step. The biggest thing you can use your P&L for is to see all your expenses listed out and how much you spend in each area. You can (and should) also use the same expense categories in your plan, which means you should create chart of accounts categories for each item you want to track. You can look at past P&Ls for total revenue and cost of goods sold. Those will also show trends, which can help in forecasting.

The numbers in your plan are going to be educated estimates of revenue and expenses for the time period. Predicting revenue can be difficult because it can fluctuate month-to-month based on things beyond your control.

You may find it helpful to first list all guaranteed income: subscription boxes, unpaid invoices, and/or memberships. You can then examine historical data to see what you made during the same period last year. If you think your revenue will surpass last year, you can increase the amount in your plan, but it's essential to be conservative to avoid getting into trouble. You should also consider any sales declines brought on by holidays or the time of year as well as any significant sales or promotions that will increase it, like school sales, one-off events, and business-to-business orders.

Having a plan for how much you think you're going to make and spend is extremely useful, because it can help you plan for months that will be leaner and set aside money for big projects during months with higher revenue.

## 12.7 CREATE AN INVENTORY SPENDING PLAN

One of the biggest expenses as a bookstore is inventory, so it's important to have a specific spending plan for it. If you do frontlist buying, you'll especially need to pay attention to release dates, as those invoices will hit when the books ship. Some stores do seasonal buying, pop-ups may buy for each individual event, and there's also event buying. Since there are many different ways to buy, the first step to creating an inventory spending plan is to determine *how* you buy. Do you want to buy frontlist by publisher season? Seasonal buying by quarter? Buying just for events or pop-ups? Looking at new releases each month? There are as many ways to buy as there are buyers!

Once you know how you buy, the next step is to look at the revenue you predicted in your overall spending plan to see when you will actually have money to spend on inventory, then determine the best times for you to buy to maximize cash flow. As you learned in Chapter 9: Cash Flow Deep Dive, it's important to try to align when your invoices hit to when you will actually have the cash to pay them. When ordering frontlist, you want to make sure your biggest invoices will hit during high sales months or coincide with a large sale, like an event or school order. If you don't order frontlist, you'll want to determine the best frequency of ordering based on your predicted revenue. If you'll remember, cash flow is about timing, so ordering is also a lot about timing!

### 12.7.1 DETERMINING HOW MUCH TO SPEND ON INVENTORY

To determine how much to actually spend on inventory, it's useful to look at your general cost of goods sold percentage. For example, if you average a COGS at 55% of sales, you want to ensure you don't plan to spend more than 55% of predicted sales on inventory. It's also useful to break down that overall percentage into smaller percentages based on your inventory mix. If you have

70% new books, 20% used, and 10% sidelines, you can break down your overall COGS percentage into those categories. Let's look at an example.

For ease of math, let's say you predict $10,000 of sales. 55% of that is $5500, so that would be the overall maximum you should spend on inventory. Of that $5500, you want to spend 70% on new books, which is $3850. 20% goes to used books, which is $1100, and 10% to sidelines, which is $550. And there's your buying budget!

Making a spending plan for inventory means knowing how and when you buy, matching it up to when you're going to have cash, and having a maximum budget based on your COGS percentage.

## 12.8 SET REALISTIC SPENDING & REVENUE GOALS

Now that you're set up, set your maximum spending amounts for each category for the time period. How much can you actually afford to spend in each category? How much do you need to spend to reach your goals? Go back through your needs in each category and determine how much you *need* to spend. Then go back through your REALLY WANTS and figure out what your expenses are there.

You may find the idea of "Backwards Budgeting" useful when it comes to bigger picture goals. This involves starting with your end goal and how much money you need for it, then calculating backwards to determine what you need to put aside to reach that goal. For example, if you determine it will cost you $50,000 to buy and outfit a bookmobile, and you have a goal to do that in three years (36 months), you'll need to save $1388 per month ($50,000 / 36 months). Once you know that, you could figure out how to save that amount, or you could stretch the timeline to get to a more realistic monthly savings number. After that exercise, you'll know both what you need to save each month AND your timeline for meeting your goal. Rinse and repeat for all your major goals and projects!

You should also set realistic sales goals. Overestimating sales is one of the biggest budgeting mistakes, because if you overestimate, it will look like you have more money to spend than you actually will. Be conservative when estimating sales!

Every category in your spending plan should have a corresponding goal, whether that is a solid number or a percentage of sales. List those goals in your plan. If you use a spreadsheet type system, add a column. If you use your accounting software or even different bank accounts for all your large buckets, you can include the goal amount in the name of the accounts/categories. Now, when you look at your categories, you'll be able to see right away where you are in relation to your goals.

## 12.9 PLANNED VS ACTUAL

Now that you have your intentional spending plan, it's important to review it on a regular basis to be sure you stay on track and in alignment with your goals, values, wants, and needs. Few elements of your budget are set in stone. Your expenses may change, or you may reach a goal and want to plan for a new one. Whatever the reason, get into the habit of regularly checking in with your plan to determine if what you're tracking makes sense based on your goals, values, wants, and needs, how your planned spending matches up to your actual spending, and where you sit with reaching your goals.

You'll want to add another column to your spending plan: actual expenses and revenue. Thus far, you have listed your planned expenses and revenue, but it's important to understand what you actually make and spend and how that compares to what you planned to make and spend. Running a profit & loss statement to get your actual numbers is one of the easiest ways to do this if you keep up with your bookkeeping.

There are two main questions you want to answer during this step:

- **Is your revenue plan realistic?** Compare your actual revenue over the past 3-6 months against your planned revenue and see.
- **Are your expenses steady?** If your expenses don't differ that much from your plan, you're good to go. But if your actual expenses differ wildly from your plan, you need to pay attention to how they're growing or shrinking. This is particularly important for variable expenses that are tied directly to sales, like COGS. If your COGS is really different from what you predicted it to be, something might be off. Why are you spending so much more money on inventory than you thought? It could be that your sales are a lot higher, or that you didn't take advantage of publisher promos, or something else. Looking at this and figuring out why is the most important part.

Generally, if your actual spending is a lot more than you planned, you'll want to investigate why. Did something happen that increased your expenses in that category, or did you just go buck wild? If your actual spending is a lot less than you planned, it may mean that you could consider spending more on a variable expense like inventory, or consider a staff bonus, etc. Overall, looking at your actual versus planned expenses and revenue will make you much more nimble in adjusting your spending and investing, big and small.

## 12.10 SET ACTIONS BASED ON DEVIATIONS

Next, you'll want to set thresholds for what deviations from your plan are acceptable and the actions you will take if you deviate too far. Decide what amount of deviation from your plan is acceptable (green), something you need to carefully investigate (yellow), or a red flag that you need to take action on immediately (red). If you use a

spreadsheet type tool, the visual of seeing the greens, yellows, and reds makes it easy to see at a brief glance how you're doing if you're good with colors. If not, you can certainly use a different indicator, as long as it's easily recognizable to you where you're at.

Once you know what level of deviation is acceptable or not, you can then determine the actions you want to take for each level. Generally, if something is green, meaning it's within an acceptable range, you'll remain on strategy. If something is yellow, meaning you want to investigate, you'll need to specify *what* you want to investigate. For example, if you determine that your COGS goal is 50% of sales or lower, but a 5% deviation is acceptable, then your green value would be 55% or lower. If your COGS within that range, you don't need to change anything.

You might then set your yellow number for investigation to be between 56-60%, meaning if your COGS is in that range, you'll want to investigate your spending. This may mean reviewing your inventory mix, looking at vendors and terms, digging into your inventory turns, etc. Finally, you might set your red flag number to be higher than 60%. In that case, you're spending too much, and actions might include completely overhauling your inventory, doing a big return, and/or changing your purchasing strategy.

Looking at deviations offers you a starting point to dig deeper into your expenses and see where you are over- or underspending, the quality of your spending, if your money allocation is right for your goals and values, and whether or not you can reduce expenses.

In effect, setting deviation thresholds and actions and coloring or labeling your spending plan in this way turns it into an actionable financial dashboard that is easy to review quickly and determine how you're doing on spending. You may also find it useful to list your financial goals and values on a separate spreadsheet or table and then link them to each of your spending categories to give you yet another visual of whether or not your spending is in alignment.

### 12.10.1 WHAT CAUSES DEVIATIONS?

Deviations can happen for a number of reasons

#### Inaccurate Expectations/Faulty Assumptions

Probably the most common! Expenses and sales can be difficult to forecast, especially if you don't have good historical data. For example, if you make a false assumption about how much your sales will increase for the holiday season, it will result in you having a plan you couldn't meet.

#### Bad Data

Make sure you examine every source of data you use and incorporate it properly and that you adjust your plan for known changed factors. Data formatting errors

such as misplaced decimal points or missing zeroes will also result in errors. If you're using a manually calculated spreadsheet, human error is a big factor.

### Changes in Economic Conditions/External Factors

Macroeconomic changes like market demand, increased labor costs, and tax laws can wreck even the best financial management strategies. If economic conditions change, you could be hit with additional costs. Alternatively, you may have to pay higher salaries if inflation rises dramatically, or more inventory costs because you're preparing for a UPS strike.

These factors can change throughout the year and can create plan deviations that are not within your control, so you should build a margin of safety into your plan and your deviation action grid to mitigate this as much as possible.

Another external factor to think about is weather. For example, forest fires causing smoky conditions, a big blizzard the weekend before Christmas, or a hurricane hitting would cause people not to shop during what normally might be a busy time, and there's no way to predict those things. If you predicted good sales, then a weather event happens, that would cause a pretty big plan deviation.

### Regulatory Changes

For example, your state passes a law that says you have to restrict access to certain materials online, and your IT costs go up.

### Operational Changes

Adjustments to internal processes, new projects, employee hiring, and big changes (like opening another location or procuring a bookmobile) are common and can heavily impact both revenue and expenses.

### Over- or Under-Performing

You just performed better or worse than you expected.

### Miscellaneous Reasons

There are other miscellaneous things that could create a plan deviation. For example, an employee stealing from the till could result in temporarily being lower than you thought in cash, or customers demanding that you implement safety measures for events or speed up your special order process might strain your budget. Changes in industry competition will also create deviations. More competition means higher marketing expenses, which could lead to a potentially negative deviation.

## 12.11 ANALYZE & ADJUST

Now that you've documented your plan, your actual numbers, your acceptable deviations, and how much you're deviating from your plan, you can make any necessary adjustments so you don't overspend and have money to put toward your goals.

If you need to cut costs, look toward your regular "wants" as the first area for cuts. If you've already adjusted your spending on wants, take a closer look at your spending on REALLY WANTS, and if you still need to adjust, look at your needs last. On close inspection a "need" may just be a "hard to part with." Could you, for instance, save more by shopping around for a better rate on business insurance? Such decisions come with big trade-offs, so make sure you carefully weigh your options. Remember, even small savings can add up to a lot of money. You might be surprised at how much extra money you accumulate by making one minor adjustment at a time.

The whole point of analyzing your plan is so you can investigate those deviations and diagnose issues. Once you know why a deviation exists, you can then decide what to do about it right now, if anything.

It's important to remember that not every deviation warrants a change to your plan or even taking action. For instance, if you planned to spend $2000 a month for marketing, and you spent $2050 one month because you had an extra event, that's not a reason to overhaul your plan. However, if you planned $2000 a month and over the past three months you spent $2050, $2150, and $2250, then you should update your plan accordingly.

## 12.12 POTENTIAL ACTIONS TO TAKE

If you notice deviations in your analysis, there are a few actions you can take.

- If there are deviations from your plan across the board, you can increase or decrease your overall planned spending.
- If you're spending a lot less than planned in one category and a lot more than planned in another, you could reroute the amount planned from the positive category to the negative one.
- Make moves to try to increase sales/revenue to cover the increased expense.
- Assess how you can reduce the cost of the expense – negotiating with vendors, changing from ordering from Ingram to ordering from publishers, etc.
- Adjust your tactics and adapt to new information. For example, if you're overspending, you may look for possible cost reductions. You can also adjust to take advantage of new industry trends, like selling through social media.
- Manage your expectations. Say your costs are significantly higher because of something out of your control, like inflation. You can't reduce them, but you can adjust your planned spending to reflect that change.

You want to make sure to adjust as necessary, but also that you aren't adjusting if you don't need to. Again, look at your green/yellow/red deviations and actions, investigate why a deviation exists, then make changes only when it makes sense.

Once you've made the necessary adjustments to your plan, the last step is to set your next planning cycle/time period. You can use the information from one planning cycle to set up for the next. This means the end totals for your selected time period become the beginning totals for the next cycle. Remember to make any necessary changes for the next cycle based on your deviation grid and analysis.

## 12.13 BUDGETING TIPS & TRICKS

The following are some budgeting tips and tricks you may find useful.

- Know how seasons affect your business. The fourth quarter automatically skews your plan. If you're a tourist business, know the seasons that are best and worst for you.
- Different business models will have different plans.
- To estimate future revenue and expenses, looking at historical data is the best tool. You can also take into account other factors you know or predict will affect the next cycle – a better margin with a major vendor, increasing sidelines percentage, expanding to a new customer base or income stream, etc.
- ABACUS can be a big help, especially for new stores.
- Don't be overly optimistic. It's better to end up with more revenue than you expected than to fall short.
- Overestimating expenses helps ensure your finances aren't threatened when surprises come up or projects go over budget. You will be much better equipped to weather financial hardship if you've made room in your budget to respond to unexpected changes.
- Factor in some slack. Your plan is not set in stone. Because of this, it's wise to factor in some slack and make sure you have more than enough money socked away (or coming in) before expanding the business or taking on new employees.
- Note changing costs. Products and services don't always cost the same amount every cycle. Be sure the expenses listed in your plan are accurate at all times.
- Spend within your means. Whenever possible, do not spend more money than you make. As you learned in Chapter 3: Vendor, Debt, & Tax Management, make sure your debt is productive and use loans and credit wisely so as not to dig yourself into a hole.
- Create a review schedule. You should review your plan at least monthly. Track and store your monthly data so you can reference it for future months and make changes as needed.
- Explore a variety of solutions. When you find structural issues or problems, remember to explore your options. Brainstorming techniques can help make existing financial information more useful and also inform future planning cycles.
- Examine your successful areas too! Knowing what you're good at allows you to keep being good at it!.

- Just do it! Budgeting can be difficult and scary, but it is so important for a business to know where its money is being spent. Sit down, get organized, and create a budget for the health of your bookstore.

## 12.14 TIPS FOR BUDGET ANALYSIS

The following are some tips for analyzing your budget.

**Leverage technology**: Budgeting software can help you track and monitor your spending plan and automatically calculate deviations for you. If you decide to use software, you should reevaluate it periodically to ensure it's still working the way you need it to.

**Collaborate with your team**: Financial information can be complex and confusing. It's helpful to collaborate with your bookkeeper, accountant, and staff when creating your spending plan to ensure the highest level of accuracy in your predictions. It also helps to have some level of transparency with staff, as it could motivate them to see sales numbers, and if they know what the budget is as it relates to their role, they can help you both stick to it and better forecast.

**Stay flexible**: Make sure your plan continues to serve your needs. It should be a living document you revisit regularly so you can make adjustments and identify issues early. You may find it helpful to implement a formal plan analysis schedule to make sure you're actually looking at and taking action upon the information it gives you.

**Identify trends**: Analyzing your spending plan can be a useful way to figure out how financially healthy your store is at any given time. It can also help you make predictions. See if you notice any trends while doing your analysis, and determine whether you can better forecast based on that data.

**Think of the future.** Unforeseen circumstances may greatly affect your budget. Think toward the future and what things you foresee that could cause potential issues. This also helps minimize deviations.

**Ask for help.** If something seems off, talk to your bookkeeper/accountant/financial advisor. You should also include them in your financial planning process upfront.

**Make use of visuals.** Graphs and charts may more easily present statistical data and make things more clear than just numbers on a page.

**Review your calculations.** Human error is a common, yet crucial, problem when dealing with numbers. Double check your calculations to ensure everything is correct.

**Don't fixate on the percentages**: Although you should set thresholds for deviations and look at them, it's important not to fixate on the percentages and lose track of the actual amounts. Some expenses are a larger proportion of overall costs than others. Seemingly small percentage changes in them

could lead to outsized effects on your actual results. Because of this, you should always look at the actual deviation amounts along with the percentages to keep perspective and get a more accurate picture.

**Unify data sources**: We all have multiple sales channels these days - store sales, online sales, events, Bookshop, Libro, etc. All these channels impose different costs, and you must account for them accurately. Because of this, you should make sure your financial data sources are unified and remove any data silos. This is why we recommend putting your income and expenses into those bigger buckets and using accounting software - to unify your data sources. Doing this ensures you receive accurate actual numbers.

Ultimately, deviations are a starting point for you to conduct a deeper analysis. Look at all the factors that affect your costs and examine the return on investment your expenses generate. Most importantly, do not assume that positive deviations are automatically good or that negative deviations are automatically bad. The **why** is what's most important.

## 12.15 SPECIAL CONSIDERATIONS

**Seasonal Businesses**: Some bookstores operate at a much higher volume at certain times of the year. If this is you, you should consider that your busy season will bring in much more income than your slow season(s). One way to tackle this is to take an average of your monthly income for the year and use that as your monthly operating budget. Don't project based on the biggest numbers — use the smaller numbers or an average. For seasonal businesses, it is especially important to establish an emergency fund so that a surprise expense during the slow season doesn't become a catastrophe.

**E-Commerce**: Online businesses may have fewer fixed costs, such as rent, but may have more variable ones. Shipping costs, shipping zones, taxes, and shipping supplies will change based on sales volume, so find an average or inflated number that works for these budget items. Stores that operate exclusively online should also invest in a well-made, working website and have a system in place for potential returns. These two things will help improve remote customer service, which can lead to more sales — and a larger budget — in the future.

**Nonprofits**: Not-for-profit businesses are funded in a variety of ways, including through grants, donations, and dues. For nonprofits, it is even more important to keep the budget as realistic as possible at all times, as there is commonly less money to move around.

**Other Novel Models**: If you own a pop-up, bookmobile, co-op, employee-owned, or other novel model business, both your sales and your expenses may look drastically different. You may or may not have fewer fixed costs. You might have higher inventory turns, or if you're a co-op or employee-owned, your payroll will look completely different. Budgeting for novel

models can be more OR less complicated, depending on your model.

**Startups**: Budgeting with no existing financial history can be tough. You will need to do research on the industry and use those numbers to create a rough estimate for your budget. ABACUS is a great tool for this! When you estimate a budget from scratch, be sure to really overestimate your costs to mitigate risks.

**Don't forget to factor in taxes and fees!** There are a shocking number of business owners that don't make any self-employment tax payments to the IRS, for example. Make sure this is included in your plan!

## SUMMARY

**Why It Matters**

A **budget** helps with operational and strategic decision making. A good budget can help you make informed decisions, identify your growth opportunities and where you might be over- or under-spending, weather leaner business times, manage risk, and measure your overall business performance. It also helps you to know not only what to spend your money on, but when to spend it, which is just as important.

**12.1 The Basics**

Instead of thinking of budgeting in the traditional way, it may be useful to think of it more as intentional spending. If you align your purchases with your financial goals and the things you care most about and track your spending to ensure it stays aligned, you're budgeting!

**12.2 Determine Financial Goals & Values**

First, make a list of your financial values and your short and long term financial goals. Next, map each of your goals to at least one of your financial values, or determine what kinds of value-driven activities you could do if you accomplish your goal.

**12.3 Wants vs Needs**

A business need is something you require for your store to survive. A business want is anything else that isn't absolutely required for your business to survive. Try categorizing business expenses into wants and needs to help you take a closer look. Your spending plan should include everything you need. Next, figure out what you REALLY want, and include those expenses as well.

**12.4 Align Expenses**

Look at your expenses to see what aligns and what doesn't. Start by looking for expenses that are wildly off from your goals and values, and cut those first. Then, look for expenses you can cut that would be fairly painless. Next, go through your wants and needs and prioritize your spending based on those. Finally, look more closely at things that feel like a sacrifice even if they don't align.

The key to intentional spending is to center your spending around what you most value and realizing your biggest hopes and dreams. Where your money goes should reflect what you value as a business. Take some time to go through your expenses and dig into how your spending aligns with your values, goals, needs, and wants.

### 12.5 Categorize Your Expenses & Revenue

Now that you see how your spending aligns with your goals, values, wants, and needs, the next step is to categorize your expenses. We recommend including these overall categories:

- Cost of Goods Sold
- Payroll
- Occupancy
- Operations

Your **Chart of Accounts/Profit & Loss Statement** expense categories could be useful in deciding which categories you want to track in your spending plan.

### 12.6 Create Your Spending Plan

First, choose a tool. Then, fill it in with the expense and revenue categories you determined you wanted to track in the last step. Next, set a time period. Estimate how much revenue you will bring in during the time period and list it at the top of your document. This will be the baseline for what you're able to spend during the time period. And finally, list your planned spending in each category.

### 12.7 Create an Inventory Spending Plan

Look at the revenue you predicted in your overall spending plan to see when you will actually have money to spend on inventory, then determine the best times for you to buy to maximize cash flow. To determine how much to actually spend on inventory, it's useful to look at your general cost of goods sold percentage.

### 12.8 Set Realistic Spending & Revenue Goals

Set maximum spending amounts for each category for the time period. Go back through your needs in each category and determine how much you need to spend. Then go back through your REALLY WANTS and figure out what your expenses are there. Every category in your spending plan should have a corresponding goal.

### 12.9 Planned vs Actual

Review your plan on a regular basis to be sure you stay on track and in alignment with your goals, values, wants, and needs. Look at your actual spending and revenue in comparison to your planned

spending and revenue. Ask yourself if your revenue plan is  realistic and if your expenses are steady. Generally, if your actual spending is a lot more than you planned, you'll want to investigate why.

### 12.10 Set Actions Based on Deviations

Set thresholds for what deviations from your plan are acceptable and the actions you will take if you deviate too far. You may also find it useful to list your financial goals and values on a separate spreadsheet or table and then link them to each of your spending categories to give you yet another visual of whether or not your spending is in alignment.

#### 12.10.1 What Causes Deviations?

- Inaccurate Expectations/Faulty Assumptions
- Bad Data
- Changes in Economic Conditions/External Factors
- Regulatory Changes
- Operational Changes
- Over or Under Performing
- Miscellaneous Reasons

### 12.11 Analyze & Adjust

If you need to cut costs, look toward your regular "wants" as the first area for cuts. If you've already adjusted your spending on wants, take a closer look at your spending on REALLY WANTS, and if you still need to adjust, look at your needs last.

### 12.12 Potential Actions to Take

See the section in the chapter for potential actions.

### 12.13 Budgeting Tips & Tricks

See the section in the chapter for tips & tricks.

### 12.14 Tips for Budget Analysis

See the section in the chapter for tips.

### 12.15 Special Considerations

Seasonal businesses, online only stores, nonprofits and other novel models, and startups may all have spending plans that look different. Don't forget to figure in taxes and fees.

**In Review**

- Determine your financial goals and values.
- Identify your needs, wants, and REALLY WANTS.
- Review your spending and cut anything that doesn't align with your goals and values.
- Categorize your expenses and revenue.
- Create your intentional spending plan.
- Set realistic spending and revenue goals.
- Set actions based on deviations from your plan.
- Review planned vs actual spending and revenue and follow your action plan.
- Analyze and adjust.
- Set the next planning cycle.
- Rinse, wash, repeat!

## KEY TAKEAWAYS

- A good budget helps you to know not only what to spend your money on, but when to spend it, which is just as important.
- Instead of thinking of budgeting in the traditional way, it may be useful to think of it more as intentional spending.
- Your Chart of Accounts/Profit & Loss Statement expense categories could be useful in deciding which categories you want to track in your spending plan.

## TEMPLATES & RESOURCES

- **Template**: Simple Budget Template

## KEY TERMS

- Budget
- Chart of Accounts
- Cost of Goods Sold (COGS)
- Expenses
- Forecasting
- Net Revenue
- Profit & Loss Statement
- Spending Plan

## REVIEW QUESTIONS

**True or False**:

- You should be optimistic when forecasting revenue.
- Every deviation is important and warrants a change to your plan.
- Your Chart of Accounts/Profit & Loss Statement expense categories could be useful in deciding which categories you want to track in your spending plan.

## ANSWER KEY

- F
- F
- T

DIG DEEPER

# BUDGETING CHALLENGES & HOW TO OVERCOME THEM

## Erratic Cash Flow

A common money problem for small businesses is cash flow. Your spending plan might show more sales than expenses one month, but you might need to pay bills long before the revenue from those sales arrives. To ensure you can pay bills, meet payroll, and buy inventory and everything else you need, you have to look at your cash flow to prevent surprises. Cash flow statements (formal or informal) will let you know when you need to conserve cash, defer purchases, and/or arrange for more credit or loans. Remember, cash is the gas your business runs on – you don't want to run out!

## Deficits

You might need to run at a cash deficit at varying points during the year, especially if you have a seasonal business but can't shut down when sales are slow or nonexistent. One key to dealing with deficits is to do your best to negotiate with vendors, landlords, lenders, and other creditors that address your cash flow situation. Other ways to deal with deficits include increasing sales volume by using discounts, selling old inventory at a loss, cutting overhead expenses, raising prices where you can, and depreciating assets. Take a second look at the tips provided in Chapter 9: Cash Flow Deep Dive to see more about how to deal with cash deficits.

## Missed Targets

Projections that aren't met can affect the entire spending plan. If you miss sales targets, for example, you can disrupt cash flow. If your expenses are larger than expected in a certain area, you could drain cash paying your bills. To catch missed targets, it's helpful to conduct a spending plan analysis each month to see if you're on track. This will allow you to make changes immediately if you spot a serious problem. When you create your annual spending plan, you should run different sales and expense scenarios to see the effect they'll have and make plans to deal with them should they arise.

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### Lack of Analysis

To make your spending plan more useful, divide your expenses into larger buckets of Cost of Goods Sold, Payroll, Occupancy, and Operations, then calculate each as a percentage of sales. This information will tell you the overall areas where you might be off track, and you can use that to drill down further.

### Setting Unrealistic Goals

Your spending plan is a tool to help you reach your goals, but the tool can only do what you tell it to. Remember, your plan is a road map, but you have to program the destination. If you set your saving or expense limits too low, it may cause you to be stretched too financially thin later. Setting your goals too high can cause you to get discouraged. Think realistically and forecast your expenses to the best of your ability. Make sure to build your plan around your store's business model. Budgets are not one size fits all. Creating a spending plan that is unique to your needs will help you stay on top of things and stick to your plan more easily.

### Forgetting to Track One-Time Expenses

Your spending plan can quickly become inaccurate if you forget to track one-time expenses. Those annual expenses can creep up on you! This mistake can be easily avoided if you budget month to month and put all of your unusual/one-time expenses on your calendar so you don't miss them when creating your plan. You can also divide the annual amount by 12 and include it in your plan.

### Not Planning for Emergency Expenses

Even if you do a good job planning for all your regular expenses, if you don't leave room for emergencies, it can throw your budget for a major loop. Without the proper planning for these unexpected expenses, there is a chance that you can add a lot to your debt, get strapped for cash, or even close altogether. As mentioned in previous chapters, it's important to create an emergency savings fund so you can have a safety net to take care of any irregular expenses.

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## Getting Discouraged When Your Plan Isn't Working

Budgets help you manage your debt and spending habits in the long term. If you haven't noticed any changes in your finances, you likely haven't given your plan enough time yet. Even though it can be tough trying to stick to a budget, don't get discouraged! Just make sure that you are being realistic. Try to find ways to make budgeting fun for yourself. If you think of budgeting (or any financial activity, really) as a chore, that's all it's ever going to be. Do what you can to reward yourself!

## Not Fixing Your Budgeting Failures

If you find yourself constantly failing to make your plan work, take a step back. Are you overspending? Are you not making necessary adjustments? Your spending plan needs to be realistic, but also flexible. Focus on identifying the issues, then fixing any specific budgeting failures. Watch your overspending and be aware of the common budgeting challenges listed here. It's okay if you have to start your plan from scratch a few times before getting it right, and it's fine to do a smaller, bigger picture plan versus a more detailed one. The main thing is being able to identify when issues arise!

*Chapter 13*

# Creating Your Ongoing Financial Dashboard

## LEARNING OUTCOMES

By the end of this class, you will be able to:

- Create an ongoing financial dashboard.
- Fully understand how to analyze your dashboard.
- Take action on your analysis.
- Finalize your course project.

## WHY THIS MATTERS

A **financial dashboard** keeps all your data in one place. When you create something that gives an effective overview of your fiscal performance, you have a powerful tool to make smart decisions. Besides being a one-stop shop to view information, your dashboard also allows you to manipulate your financial data to develop reports, generate forecasts, and adjust your spending plan continuously. Ultimately, your dashboard will empower you to develop actionable insights for managing and growing your business.

## CHAPTER OUTLINE

**13.1** The Basics
**13.2** Questions to Ask
**13.3** Defining Metrics
**13.4** Gathering Data
**13.5** Tracking Performance & Trends
**13.6** Tips for Creating a Financial Dashboard
Summary
Key Takeaways
Key Terms Used in This Chapter
Templates & Resources
Review Questions

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## 13.1 THE BASICS

A **financial dashboard** is an essential tool for easily viewing the financial reports you want to run and when, metrics and actions to take, and your general financial status. Unlike a **profit and loss statement**, a **balance sheet**, or a **chart of accounts**, this is not an official, universally recognized document. Rather, it's a term we use for something that puts all financials together in one place. Everyone's dashboard will look different depending on personal preferences, but the use of the tool is the same.

Modern digital financial dashboards typically rely heavily on visuals to portray a large amount of information in a single view. But a well-built financial dashboard will do way more than just show fancy charts and graphs. While of course it should include helpful data visualizations, a robust dashboard will bring together all your information in one place to give you a complete view of your wealth and business in real-time. The dashboard should be a broad view with enough functionality to slice up the data any way you want.

Different dashboards can exist for different roles. Bookstore staff may want to look at sales and inventory. Your accountant will always want access to a balance sheet, but they don't need to see individual vendor balances. If you're a nonprofit, your board will need one that is different from all of the above. The same goes for different store models and sizes - if you're a pop-up or bookmobile or a one-person shop, what you want to look at will be different from what large brick-and-mortar stores want to see. And if you're really new to finances, you may want to start with a stripped down dashboard and build from there, whereas if you've done this for a while, you might want something more robust.

Throughout this course, you have begun to create your own financial dashboard in your workbook by noting in your grids what reports and metrics you want to track. You can finalize your dashboard by adding your spending plan, specific numbers, and even visuals.

## 13.2 QUESTIONS TO ASK

Harking back to Chapter 1, here are some questions to ask when creating a financial dashboard:

- What are your financial goals and values?
- What financial reports do you want to review regularly?
- What metrics do you want to track?
- How do you want to look at your data?
- How often do you want to look at your data?
- How often do you want to change your data and make changes to your business?
- If the dashboard is for someone else to view, what is their purpose for viewing the dashboard and what information do they want to see?

Once you have these basic questions answered, the next step is to look at the various tools and software you can use to build your dashboard. Do you have something inside of your accounting software or point of

sale system that you can customize? Do you want to build something in Excel or Airtable or some outside system? If some of your data is tracked outside of your accounting software or point of sale or if there are folks who need to view the dashboard who don't have access to those systems, then you'll need to create something separately.

Finally, the biggest question is: **What actions will you take if you notice a red flag or a downward trend?** Dashboards are really great, but having the data means nothing if you don't use it.

## 13.3 DEFINING METRICS

Once you know who your dashboard is for, what your goals are, and what data you want to track, you can finalize what metrics you want to see on your dashboard. This will be different for everyone and for each audience, but there are two important things to keep in mind when choosing metrics for any dashboard:

1. Don't display an overwhelming amount of data. Keep it high-level while offering the ability to drill down into details if needed.
2. Summarize and interpret the numbers, versus just reporting them.

Your dashboard should give information at a glance, but it should also be clear whether the information is helping you get to your goals or not. You should be able to see red flags and issues right away.

When thinking about the final metrics to include, you should also consider the audience. Who will view this dashboard? What numbers do they care about? For example, if you're a nonprofit, you'll likely have one version of a financial dashboard posted on your website showing how donations are spent in a format that's easily understood by the public, and you'll have a second version containing more detailed, confidential numbers and "insider information" suited for the eyes of the Executive Director and the Board.

You should also set targets for your metrics so you can better catch red flags and issues. With targets, you can easily see if you are above or below your plan.

### Example Metrics

At a minimum, you probably want to track sales and income, **cost of goods sold**, expenses, and cash flow (if you notice, most of this comes from your profit & loss statement). You may also want to track things like **accounts payable** and **receivable**, savings, **net worth**, investments, and loans/credit/debt (from your balance sheet).

**Revenue** can be an important metric to track because it's usually the basis for your spending plan. If your revenue is below your projections, that's a red flag and you may need to increase marketing and/or revise your spending plan. Even once your store hits a sustainable level of sales, your sales need to be rising enough each year to keep up with inflation, so static or falling sales are a red flag.

Cost of goods sold is also a number you should calculate regularly, ideally monthly,

using the official calculation (**Starting Inventory + Purchases - Ending Inventory**).

You also want to make sure you're on the same page as your accountant with what they're using to calculate cost of goods sold. Other inventory metrics to potentially track include current inventory on-hand at cost, returns waiting to be credited by the publishers, and co-op funds received against the previous year.

**Gross margin** is what pays your expenses, so it's really important to know this number and that it's enough to pay your bills. Your **spending plan** also typically rests on some gross margin assumptions. Your sales for the period may seem on track, but if they include a bunch of business-to-business orders with high discounts, then your margin may be off, and you may not have as much cash for expenses as you expected at that level of sales. Or perhaps Ingram increased their minimum in the middle of the year, and you ended up doing less business with publishers than expected. Every extra unanticipated point you pay in inventory has to be made up somewhere else - either by increasing sales or reducing expenses - so your gross margin number is important to track.

If you've created a spending plan, then you want to track planned vs actual expenses and revenue. Even if you don't have a spending plan, you can look at year-over-year expenses to identify trends and ensure expenses are not increasing faster than income. If they are, you can look for ways to rein in any categories that have gotten out of control - but only if you track them!

Cash flow is one of the more important metrics and should probably be tracked weekly. This means knowing the actual cash that is going in and out of your bank account, what bills and checks are about to hit, etc. This can be as simple as tracking how much money the store brought in that week vs how much you spent, to a checkbook-like register, to a more complicated calculation of inflows and outflows. However you do it, knowing your cash flow is IMPORTANT.

If you're saving for a particular goal, tracking savings every month can keep you motivated. Or, simply tracking your savings percentage rate may be a shortcut metric indicating that both income and expenses are under control.

If your store is doing well and you're contemplating taking out a loan to expand in some way, then net worth can be useful to track. However, if you're currently struggling, this one is probably too depressing to be useful.

Accounts Payable and credit card balances are the debt that will likely fluctuate the most, and you may want to track weekly, or at least monthly. And if you've taken out multiple loans AND have credit cards, it's useful to know how much total outstanding debt you have so you can see how long it will take to pay off. Also, if you have extra cash, it's good to know how much debt you have and whether putting some extra cash toward it would help you pay it down faster (sometimes it does, sometimes it doesn't, depending on interest).

This is only the tip of the iceberg of possible metrics. If you're starting from scratch, start with your goals and values and the basic metrics of revenue, cost of goods sold, gross margin, expenses, and cash flow and build from there. Look at what you've listed in your workbook throughout this course, and narrow it down to a handful of key metrics to start.

## 13.4 GATHERING DATA

After you've created goals and metrics, next up is to gather data. Data will come from various sources: your point of sale system, accounting software, payroll system, even your head, depending on what you're tracking. Keep your goals and metrics in mind and gather the data most appropriate for what you're trying to do.

The easiest data to track consistently is revenue and expenses, because these are already tracked via your point of sale system and/or accounting software. Your monthly bills should also be fairly easy, as you are hopefully tracking those already. Cash flow is important and likely another thing you're already tracking somewhere. Finally, open invoices should be fairly easy to find either within your accounting software or in Batch if you use it, and again, something that you may be already tracking. Running an Accounts Payable with Future Due report is easy if you enter your invoices into your accounting software. If you take these few things and put them together in one place, congratulations, you have a dashboard!

Cost of Goods Sold and gross margin take a little more work to track, because for both to be accurate, you need to do that COGS calculation regularly. You can also include profit & loss statement and balance sheet information if you want to look at those things regularly. Having your ABACUS mapping handy may be useful, especially if you've categorized your expenses into the larger ABACUS buckets. And your spending plan should be a part of your dashboard as well.

There is an endless amount of data you can track. The important thing is to make sure you don't overwhelm yourself and that you're tracking things that will help you make business decisions. You being comfortable with what you're tracking, how, and why is the most important, because if you're not comfortable, you won't use it.

Here is a handy list of some of the reports/data you may want to consider tracking on your financial dashboard:

- Profit & Loss statement
- Profit & Loss for the month with 1-3 year comparison and percentage increase/decrease
- Profit & Loss year to date with 1-3 year comparison and percentage increase/decrease
- Balance Sheet
- Cash Flow statement or tracking
- Cash Flow Analysis
- COGS/Inventory spending
- Point of Sale ZTape or End of Day report
- Sales Summary Report
- Monthly bills
- ABACUS mapping
- Budget/Spending Plan

- Buyer's Budget Month End
- Budget/Spending Plan Deviation Analysis
- Assets/Liabilities
- Gross Margin
- Shareholder Equity
- Debt/Loans/Investments
- Accounts Receivable Report with Future Due
- Accounts Payable Report with Future Due
- Open invoices
- Gift Card Balance Report
- Event Profit & Loss statements
- Event Year-Over-Year comparison and percentage increase/decrease
- Publisher Promo tracking
- Co-Op tracking
- Savings Account Earmarks
- Sales Tax
- Donations
- Mileage

## How Often to Look at Data

You may want to have multiple dashboards for different periods of time, for example, an operational one you look at monthly and a strategic one you look at quarterly or yearly. You will look at different parts of your own dashboard at different times.

On a daily or weekly basis, you'll want to look at your register and cash reconciliation, bank deposits, payables, and coding your transactions. Calculating your cost of goods sold, reconciling your bank accounts, running reports, and checking on your budget are things to do monthly. Quarterly dashboard checks include examining your balance sheet, quarterly taxes, and certain reports. Finally, as you wrap up your fiscal year and start a new one, you'll want to check in on property taxes and your spending plan. You'll do your physical inventory, submit co-op, prepare for ABACUS, and run year-end reports.

In the **Templates & Resources** section at the end of this chapter, we have linked a Financial Task Calendar to help you get started.

## How Often to Make Changes

You must ask yourself how often you want to review the data you're tracking AND how often you want to make changes to your business strategy based on the data you're collecting. By now, you know it's a bad idea to tinker with your strategy constantly. But you also know that you need to set checkpoints and goals to make meaningful changes. Otherwise, the weeks and months of running your store get away from you, and those big-picture tasks can move farther and farther down your to-do list until they fall off completely.

In addition to making sure all the data gets added to your dashboard at the designated frequency, you should review and verify the data in each reporting period. It's critical that it remains accurate and relevant so you catch mistakes and discrepancies as soon as possible.

## 13.5 TRACKING PERFORMANCE & TRENDS

One of the most useful aspects of a financial dashboard is the ability to track your performance and any trends emerging in your business over time. Depending on the data and metrics you use, some may be more suited to revealing trends, while others may simply tell a story for that time period. For example, revenue and expenses are ideal to track over time to understand important trends like whether they are trending up or down. In contrast, something like a ratio may be best when looking at balance sheet data.

If you look at certain metrics regularly, you'll see red flags more quickly and be able to fix them. Things your financial dashboard can reveal include:

- **Trends in sales and expenses.** Of course, if your sales are low, that's a clear indicator that you need to fix something. But if your expenses are very high or very low, that is also a red flag that you need to investigate.
- **Inventory Turns.** If your turns are super high or low, this is also a flag. Very high turns means you're not keeping things in stock that customers want, and turns too low means you're keeping too much dead stock.
- **Spending Plan Deviations.** If you notice a deviation well above or below your set threshold, it means your predictions are off, and you need to investigate and possibly adjust your plan.
- **Major changes in COGS**. If you actually calculate your COGS monthly, you'll be able to see if it's well above or below your average and investigate your inventory spending if needed.
- **Cash Flow Changes**. If you have a deficit, it would behoove you to calculate your **burn rate** and implement some cash management strategies.
- **Gross Margin stability**. If it's too low, it means you aren't making enough money to pay your expenses.

## 13.6 TIPS FOR CREATING A FINANCIAL DASHBOARD

Don't get hung up on perfecting your dashboard right away. The most important thing is to get some version out there. You can gradually experiment, tweak, and adjust until it's just how you want it. The earliest version of your dashboard can be just a few metrics.

Look at what you've added in your workbook throughout the course, narrow it down to your top five things to track, and start there.

This is essential: there should be a single source controlling the contents and distribution of your dashboard. Typically it's the store owner, but it could be an accountant, bookkeeper, or financial advisor. You can have several different dashboards, but you don't want everyone fiddling with your numbers from every direction. Check in consistently to ensure everything is accurate. And finally, don't overdo it. Remember, this is supposed to save you time, so if it's becoming a burden, slim it down, and keep it simple.

## SUMMARY

**Why It Matters**

Besides being a one-stop shop to view information, your **financial dashboard** also allows you to manipulate your financial data to develop reports, generate forecasts, and adjust your spending plan continuously. Ultimately, your dashboard will empower you to develop actionable insights for managing and growing your business.

**13.1 The Basics**

While of course it should include helpful data visualizations, a robust dashboard will bring together all your information in one place to give you a complete view of your wealth and business in real-time. The dashboard should be a broad view with enough functionality to slice up the data any way you want. Different dashboards can exist for different roles.

**13.2 Questions to Ask**

See a list of questions in the section.

**13.3 Defining Metrics**

There are two important things to keep in mind when choosing metrics:

- Don't display an overwhelming amount of data.
- Summarize and interpret the numbers, versus just reporting them.

Your dashboard should give information at a glance, but it should also be clear whether the information is helping you get to your goals or not. You should be able to see red flags and issues right away. Dashboard metrics will differ based on the audience, and every metric should have a corresponding goal or target. See a list of example metrics in the section.

**13.4 Gathering Data**

The easiest data to track includes: **revenue** and **expenses**, monthly bills, cash flow, and open invoices. Data that's a little more complicated to track, but nonetheless important, includes **cost of goods sold** and **gross margin**. Get a list of potential data to track in the section. You can also view the example **Financial Task Calendar** in the Templates & Resources section below.

**13.5 Tracking Performance & Trends**

Things your financial dashboard can reveal include: trends in revenue and expenses, inventory turns, spending plan deviations, major changes in cost of goods sold, cash flow changes, and gross margin stability.

## KEY TAKEAWAYS

- Your financial dashboard empowers you to develop actionable insights for managing and growing your business.
- The dashboard should be a broad view with enough functionality to slice up the data any way you want. Different dashboards can exist for different roles.
- When choosing metrics, don't display an overwhelming amount of data, and make sure you summarize and interpret the numbers versus just reporting them.
- The easiest data to track includes: revenue and expenses, monthly bills, cash flow, and open invoices. Data that's a little more complicated to track, but nonetheless important, includes cost of goods sold and gross margin.

## TEMPLATES & RESOURCES

- **Example:** Staff Sales Dashboard
- **Resource**: Financial Task Calendar
- **Resource**: 13 Financial Dashboard Examples
- **Resource**: The Ultimate Dashboard Template from Monday.com
- **Resource**: Free Financial Dashboard Templates from Databox

## KEY TERMS

- Accounts Payable
- Accounts Receivable
- Balance Sheet
- Burn Rate
- Chart of Accounts
- Cost of Goods Sold (COGS)
- Expenses
- Financial Dashboard
- Gross Margin
- Inventory Turns
- Net Worth
- Profit & Loss Statement
- Revenue
- Spending Plan

## REVIEW QUESTIONS

**True or False**:

- You can only have one financial dashboard for one role.
- A financial dashboard brings together all your financial information in one place to give you a complete view of your wealth and business in real-time.
- The easiest data to track includes cost of goods sold and gross margin.

## ANSWER KEY

- F
- T
- F

*Appendix A*

# Formulas

**Asset Turnover** = Net Sales / Total Assets

**Break Even Rate** = Gross Margin % / (Desired Owner Wage + Fixed Expenses)

**Budget Variance** = Actual – Projected

**Budget Variance Percentage** = (Total Difference / Expected Amount) x 100

**Burn Rate** = Net Income / Cash Reserves

**Cost of Goods Sold** = (Beginning Inventory + Purchases – Ending Inventory)

**Gross Margin** = Net Revenue – Cost of Goods Sold

**Inventory Turnover/Turns** = Cost of Goods Sold / Inventory

**Return On Assets** = Annual Profit Before Tax / End-of-Year Total Assets

**Return On Investment** = Cost of Investment / Net Return on Investment × 100

**Year-Over-Year** = (This Year's Number – Last Year's Number) / Last Year's Number

*Appendix B*

# Glossary of Terms

**401K.** A retirement savings plan that allows employees to contribute a portion of wages to individual accounts.

**80/20 Rule.** Spend 80% of the time looking forward, because you can impact what happens next. You should only spend 20% of your time looking back and analyzing.

**ABACUS Report.** A free annual report filled with detailed information highlighting how your store compares to other stores in a range of areas, including profitability, productivity, and financial management.

**Accounts Payable Aging Report.** A critical accounting document that summarizes the bills and invoices owed by a business, broken down by vendor and due date. It shows columns with amounts grouped into Current, ranges for the number of days past due, and a Total amount column. A detailed AP aging report shows invoices with reference number, due date, payment terms, and balance due. The opposite of accounts payable aging report is an accounts receivable report, which outlines when a business can expect payment from their customers.

**Accountant.** A person whose job is to keep, inspect, and analyze financial accounts.

**Accounting.** The action or process of keeping financial accounts.

**Accounting Software.** A computer program that enables electronic and, often, automated recording, tracking and reporting of an organization's financial transactions and accounts. The software can perform real-time accounting to simplify analysis and audits, and improve decision making.

**Accounts Payable.** Money owed by a company to its creditors.

**Accounts Receivable.** Money owed to a company by its debtors.

**Accrual Accounting.** A procedure that records revenues and expenses when they are incurred, regardless of when cash transactions occur.

**Actuals.** The actual revenue and expenses that occurred during a time period.

**Affiliate Marketing Income.** Affiliate marketers get paid a commission for referring customers to companies where they make purchases. These commissions can range from less than 1% to 20% or more, depending on the product and level of referral volume. Sites like Bookshop and Libro offer booksellers affiliate marketing income.

**Affordable Care Act (ACA).** A healthcare reform law passed in 2010 to make health insurance more accessible and affordable.

**Amortization.** *1.* Used in the process of paying off debt through regular principal

and interest payments over time. An amortization schedule is used to reduce the current balance on a loan—for example, a mortgage or a car loan—through installment payments. *2.* The practice of spreading out capital expenses related to intangible assets over a specific duration—usually over the asset's useful life—for accounting and tax purposes.

**Asset.** Property owned by a person or company, regarded as having value and available to meet debts, commitments, or legacies.

**Asset Turnover.** Net Sales/Total Assets. Presents a good overall indicator of total company productivity. The ratio tells us how many sales dollars are being generated by each dollar of assets employed in running the business.

**Audit.** An official inspection of an individual's or organization's accounts, typically by an independent body.

**Author Event Co-Op.** This type of co-op is given for promoting titles in conjunction with author events. In some cases, it requires pre-approval, but in all cases, the event must be set up via an in-house publicist to qualify. Typically either a set amount or based on your event order. Requires proof the event actually happened, as the event must occur in order to claim. Meant to cover advertising costs for the event.

**Automated Clearing House (ACH).** The primary system that agencies (like bookstores) use for electronic funds transfer (EFT). With ACH, funds are electronically deposited in financial institutions, and payments are made electronically. Your bank might offer ACH services or you can use a third party service like Melio.

**Average Cost.** A way to estimate cost of goods sold. Track the amounts spent on inventory and the quantity of books bought and sold, then calculate an average cost per book.

**Balance Sheet.** A statement of the assets, liabilities, and capital of a business or other organization at a particular point in time, detailing the balance of income and expenditure over the preceding period.

**Bank Trace.** A trace number that is used to track inbound and outbound ACH transfers. It is issued by the sending institution (usually your bank), and can be provided to your receiving institution (publisher/vendor) to track the impending transfer even before it has arrived in their system.

**Batch for Books.** An electronic invoicing system created for booksellers and publishers in the U.S. The software-assisted service helps initiate payments between vendors and bookstore retailers at no cost to bookstores.

**Beginning Cash.** The balance of cash at the beginning of the month that is carried over from the previous month.

**Bi-Weekly.** Paying employees every two weeks, resulting in 26 paychecks per year that are more or less the same throughout the year, since the pay period is the same number of days each time.

**Bookkeeper.** A person whose job is to keep records of the financial affairs of a business.

**Bookkeeping.** The activity or occupation of keeping records of the financial affairs of a business.

**Bottom Line.** A company's net income, or the "bottom" figure on a company's income statement. More specifically, the bottom line is a company's income after all expenses have been deducted from revenues. These expenses include interest charges paid on loans, general and administrative costs, and income taxes. A company's bottom line can also be referred to as net earnings or net profits.

**Breakeven.** The level of commercial activity at which the total cost and total revenue of a business enterprise are equal.

**Budget.** An estimate of income and expenses for a set period of time.

**Budget Deviation.** When your budget/spending plan does not match your predictions, or when it deviates from set thresholds.

**Burn Rate**. A measure of how fast a company uses up its capital before becoming profitable.

**Business Advisor.** A professional who provides specialized advice to help businesses improve.

**Business Credit**. A business's ability to borrow funds.

**Business Property Tax.** A tax assessed on tangible personal property businesses own.

**Business-to-Business (B2B) Sales**. Transactions between two businesses rather than between a business and an individual consumer for the consumer's personal use.

**Capital.** A large sum of money which you use to start a business, or which you invest in order to make more money.

**Cash Accounting.** Cash accounting is a bookkeeping method where revenues and expenses are recorded when actually received or paid, and not when they were incurred.

**Cash Cycle.** The cash conversion cycle (CCC) is a metric that expresses the time (measured in days) that it takes for a company to convert its investments in inventory and other resources into cash flows from sales. Also called the net operating cycle or simply cash cycle, CCC attempts to measure how long each net input dollar is tied up in the production and sales process before it gets converted into cash received. This metric takes into account how much time the company needs to sell its inventory, how much time it takes to collect receivables, and how much time it has to pay its bills.

**Cash Equivalents.** Financial assets that are easy to convert to cash and are liquid and short-term, such as CDs.

**Cash Flow.** The money that moves into or out of a business over a period of time.

**Cash Flow Statement.** A financial statement that summarizes the amount of cash flowing into and out of a company. This includes all cash inflows a company receives from its ongoing operations and external investment sources. It also includes all cash outflows that pay for business activities and

investments during a given period. This is usually done monthly, quarterly and/or annually depending on how the owner wants their books done.

**Cash Inflow.** Money flowing into your business.

**Cash Outflow.** Money flowing out of your business.

**Certified Public Accountant (CPA).** A designation given to those who meet education and experience requirements and pass an exam.

**Chart of Accounts (COA).** An index of all the financial accounts in the general ledger of a company. In short, it is an organizational tool that provides a digestible breakdown of all the financial transactions that a company conducted during a specific accounting period, broken down into subcategories.

**Close the Books.** To make no further entries into accounting for that period, balance the books, and draw up statements from them.

**Closing Entry.** A journal entry made at the end of accounting periods that involves shifting data from temporary accounts on the income statement to permanent accounts on the balance sheet. Temporary accounts include revenue, expenses, and dividends, and these accounts must be closed at the end of the accounting year. As part of the closing entry process, the net income (NI) is moved into retained earnings on the balance sheet. Modern accounting software automatically generates closing entries.

**Coding.** Specifying the account the transaction should be entered under in your accounting software.

**Collaborative Consumer Marketing (CCM).** Offered via Edelweiss360. Publishers can sponsor or "boost," placement of titles in your email campaigns. Technically not co-op, as it comes from a different department. Funds come as cash via Stripe.

**Collection Period.** Also sometimes called "days receivables outstanding." Measures the average days between sales and receipt of customer payment. This measure is an indication of effectiveness of credit and collection policies.

**Contra Account.** An account with a balance that is the opposite of the normal balance of a related account.

**Co-Op.** Short for co-operative advertising credits. Publishers issue statement credits to offset agreed upon advertising costs for their titles undertaken by the bookstore. There are four major types of co-op: pool, newsletter, display/exempt, and author events.

**Cost of Goods Sold (COGS).** The direct costs of producing the goods sold by a company. This amount includes the cost of the materials and labor directly used to create the goods. It excludes indirect expenses, such as distribution costs and sales force costs. This may also be referred to as "cost of sales."

**Credit.** An entry recording a sum received, listed on the right-hand side or column of an account.

**Credit Memo.** A memo from a vendor giving you credit against an invoice or on your account for reported problems such as shipment damages and shortages, credit memos also issued for co-op funds awarded to you.

**Credit Terms.** Payment terms mentioned on the invoice at the time of buying goods. It is an agreement between the buyer (you) and seller (publisher/wholesaler) about the timings and payment to be made for the goods bought on credit. It can be also known as payment terms.

**Current.** The payment status of accounts with no past due amount. Making all required monthly payments on time maintains a current payment status on the account. This is the opposite of delinquent. Do not confuse current with present (now) or open (available for transactions). Also known as paid on time, or paid as agreed.

**Current Assets.** Assets expected to convert into cash within one year.

**Data Universal Number System (DUNS) Number.** Used by lenders and potential business partners to help determine the reliability and financial stability of the business they are considering working with.

**Days In Inventory.** The average time a company keeps its inventory before they sell it. Some organizations call it days inventory outstanding or inventory days of supply. Finding a company's days in inventory can tell you about its efficiency in terms of operations and finances, as it shows how rapidly a company can sell its inventory. A low days in inventory figure can indicate that the company is exchanging its products for cash quickly and that they're operating efficiently. If a company finds that its conversion through sales is slow, this can show which areas might need additional help, such as building or revising a brand image or adapting to changes in the industry.

**Days In Payables.** Days payable outstanding (DPO) is a financial ratio that indicates the average time (in days) that a company takes to pay its bills and invoices to its trade creditors, which may include suppliers, vendors, or financiers. The ratio is typically calculated on a quarterly or annual basis, and it indicates how well the company’s cash outflows are being managed. A company with a higher value of DPO takes longer to pay its bills, which means that it can retain available funds for a longer duration, allowing the company an opportunity to use those funds in a better way to maximize the benefits. A high DPO, however, may also be a red flag indicating an inability to pay its bills on time.

**Debit.** An accounting entry that results in either an increase in assets or a decrease in liabilities on a company’s balance sheet. In fundamental accounting, debits are balanced by credits, which operate in the exact opposite direction. The abbreviation for debit is sometimes “dr,” which is short for “debtor.”

**Debt To Equity Ratio.** Total liabilities/Net Worth. Another common measure of company leverage.

**Depreciation.** A reduction in the value of an asset with the passage of time, due in particular to wear and tear.

**Display/Exempt Co-Op.** This type of co-op is given for titles that the publisher chooses, and you receive a flat credit if you order a certain number of copies of the book. The credit may be automatic or may require a rep to code it. May require you to feature the titles on display at the front of your store and/or in your newsletter. This is the only co-op outside of pool that Penguin Random House offers.

**Distribution.** The disbursement of assets from a fund, account, or individual security to an investor.

**Doing Business As (DBA).** Also known as a fictitious business name, trade name, or an assumed name. A name that the legal owners of a business register with the state. Owners must register a DBA only if they use a name — on business signs, letterheads, advertisements, and so on — other than the names of the legal owners of the business (for sole proprietors and partnerships) or the name the owners listed on the formation paperwork (for LLCs and corporations). For example, if Sherry Smith owns a flower shop as a sole proprietor, she could use the name "Smith's Flowers" without registering. However, she would have to register the name "Sunshine Flowers" if that's the name she uses when doing business.

**Double-Entry Accounting.** An accounting term stating that every financial transaction has equal and opposite effects in at least two different accounts.

**Earned Value Analysis.** A method of measuring your progress and performance and forecasting future outcomes. This analysis helps you assess the scope, schedule, and cost of a project and identify any issues. Based on your analysis, you can see whether your project is actually returning the value you anticipated and take corrective actions if needed. This type of analysis is project based and is great for looking at individual programs.

**Employee Bonus.** Compensation given to an employee in addition to their regular salary/hourly rate.

**Ending Cash.** The balance of cash at the end of the month, after all cash inflows and outflows are accounted for. Formula: Beginning Cash + Cash In - Cash Out = Ending Cash

**Enrolled agent (EA).** A tax professional authorized by the U.S. government to represent taxpayers in matters regarding the Internal Revenue Service.

**Equity.** Typically referred to as shareholders' equity (or owners' equity for privately held companies), represents the amount of money that would be returned to a company's shareholders if all of the assets were liquidated and all of the company's debt was paid off in the case of liquidation. Equity can be found on a company's balance sheet and is one of the most common pieces of data employed by analysts to assess a company's financial health.

**Exempt.** Someone whose job is not subject to the Fair Labor Standards Act (FLSA) requirements for minimum wage and overtime pay.

**Expense.** The cost required for something; the money spent on something.

**Fair Labor Standards Act (FLSA).** A federal law that sets minimum wage, overtime pay, recordkeeping, and child labor standards for private sector and government employees.

**Federal Income Tax (FIT).** See SIT & FIT.

**Federal Insurance Contributions Act (FICA).** Federal Insurance Contributions Act, Social Security and Medicare. Social Security is 6.2% of gross compensation up to the Social Security wage base limit of $147,000. Medicare is 1.45% of the employee's gross compensation, no wage based limit.

**Federal Unemployment Tax (FUTA).** If you spend $1,500 per quarter on wages, you are required to pay FUTA which is 6% for the first $7,000 of an employee's wages per year.

**Finance/Financial Management.** The business function concerned with profitability, expenses, cash and credit, so that the "organization may have the means to carry out its objective as satisfactorily as possible."

**Financial Dashboard.** An essential tool for easily viewing the financial reports you want to run and when, metrics and actions to take, and general financial status.

**Financial Statements.** Reports that summarize a business's financial performance and activities.

**Financing Activities.** Business transactions that involve creditors, generally to raise capital and manage financial obligations. These include debt and equity activity.

**First In, First Out (FIFO).** Commonly known as FIFO, an asset-management and valuation method in which assets produced or acquired first are sold, used, or disposed of first. For tax purposes, FIFO assumes that assets with the oldest costs are included in the income statement's cost of goods sold (COGS). The remaining inventory assets are matched to the assets that are most recently purchased or produced.

**Fiscal Year.** A year as reckoned for taxing or accounting purposes.

**Fixed Assets.** Assets which are purchased for long-term use and are not likely to be converted quickly into cash, such as land, buildings, and equipment.

**Fixed Expense.** Any type of expense that recurs on a regular basis, regardless of the volume of sales.

**Fixed Term Loan.** A loan with a fixed interest rate and monthly payment for the entire loan term.

**Forecasting.** The estimated amounts you budgeted for revenue and expenses during a time period.

**General Ledger (GL).** The main accounting record of a company or organization.

**Generally Accepted Accounting Principles (GAAP).** A common set of accounting rules, standards, and procedures issued by the Financial Accounting Standards Board (FASB). Public companies in the U.S. must follow GAAP when their accountants compile their financial statements.

**Gross.** Without deductions; total, as the amount of sales, salary, profit, etc., before taking deductions for expenses, taxes, or the like (opposed to net).

**Gross vs Net Pay.** Gross pay is what employees earn before taxes, benefits and

other payroll deductions are withheld from their wages. The amount remaining after all withholdings are accounted for is net pay or take-home pay.

**Gross Margin.** The percentage of revenue retained after cost of goods sold is subtracted from Net Revenue. This is a percentage of sales.

**Gross Profit.** The amount of money left after subtracting cost of goods sold from Net Revenue. This is the money your business runs on.

**Hourly vs Salaried.** Salaried employees are usually paid the same amount each pay period, based on their total salary. An hourly worker, on the other hand, earns a set payment for each hour they work. For example, if they earn $20 per hour and work eight hours in a day, they would earn $160 for that day (before taxes).

**Income/Revenue.** The money that a person or entity receives in exchange for their labor or products.

**Individual IRA.** A tax-advantaged savings account that allows employees to save for retirement.

**Intangible Assets.** Non-physical assets that have value, but are difficult to record, such as copyrights, trademarks, and goodwill.

**Internal Controls.** Help companies to comply with laws and regulations, and prevent fraud. They also can help improve operational efficiency by ensuring that budgets are adhered to, policies are followed, capital shortages are identified, and accurate reports are generated for leadership.

**Inventory Turnover/Turns.** Cost of Goods Sold/Inventory. This ratio shows how rapidly inventory is moving from your shelves. Inventory turnover is expressed as "annual turns."

**Investing Activities.** The purchase and sale of fixed assets and business investments.

**Invoice.** An itemized list of goods shipped usually specifying the price and the terms of sale. An invoice from a publisher can be received in the box of books sent, or is mailed/electronically sent to you.

**Last In, First Out (LIFO).** A method used to account for inventory that records the most recently produced items as sold first. Under LIFO, the cost of the most recent products purchased (or produced) are the first to be expensed as cost of goods sold (COGS), which means the lower cost of older products will be reported as inventory.

**Ledger.** A book or other collection of financial accounts of a particular type.

**Leverage.** The extent to which a company is financed by debt as opposed to the owners' funds. It is the amount of liabilities in relation to the amount of net worth on the right hand side of the balance sheet.

**Liability.** Something a person or company owes, usually a sum of money. Liabilities are settled over time through the transfer of economic benefits including money, goods, or services. Recorded on the right side of the balance sheet, liabilities include loans, accounts payable, mortgages, deferred revenues, bonds, warranties, and accrued expenses.

**Line of Credit.** Allows a business to borrow money up to a certain amount (like a credit card) and only charges interest on the amount borrowed. Generally has lower interest rates than credit cards.

**Liquidity.** The short-term financial strength of the company. It is your ability to meet short-term obligations out of currently available funds. Two liquidity measures are commonly used are the Current Ratio and the Quick Ratio.

**Loan Covenants.** Things you are required to provide periodically to keep the loan in compliance. This could be a certificate of insurance or annual financial statements, or it could be that it requires you to do an annual inventory.

**Median.** The midpoint of the data for a particular measure, with one-half of the respondents reporting figures above it and one-half below. Unlike the mean, the median is not distorted by a few unusually high or low values that may exist in the sample due to special circumstances.

**Memorized Transaction.** One of the features provided in QuickBooks. This feature helps a company by giving reminders of the business transactions that are recurring or can be quickly entered using a template. As they work like templates, companies can quickly make the entries of their transactions.

**Merchant Account.** A bank account that enables the holder to accept credit cards for payment.

**Modified Cash Accounting.** An accounting method that combines elements of the two primary bookkeeping practices: cash and accrual accounting. It seeks to get the best of both worlds, recording sales and expenses for long-term assets on an accrual basis and those of short-term assets on a cash basis. The goal here is to provide a clearer financial picture without dealing with the costs of switching to full-blown accrual accounting.

**Month-End Close.** The accounting process of collecting and filing all financial transaction information for review, reconciliation, and reporting at the end of each month. Businesses care about filing their financial statements monthly because it helps maintain a healthy cash flow, facilitate financial planning, assist in making strategic business decisions, and measure progress towards long-term goals. At the end of each month, companies often make sure their books are closed so that the records are set in stone.

**Negative Budget Variance.** Actual spending is more than planned.

**Net.** Remaining after deductions, as for charges or expenses (opposed to gross).

**Net Change in Cash.** Measures the change in a company's cash and cash equivalents over a period of time. This is Cash In - Cash Out.

**Net Income.** The last line on the Profit & Loss Statement, or the "bottom line." The amount of money a business has left after subtracting all expenses, taxes, and deductions.

**Net Operating Income.** Operating income is revenue less any operating expenses, while net income is operating income less any other non-operating expenses, such as interest and taxes.

**Net Operating Profit.** Net profit as a percent of sales. This ratio measures the difference between a, company's net sales and what it spends over a period of time. It is highly dependent upon a company's pricing policy and expense control. If gross margin (Net Sales - Cost of Goods Sold) increases or expenses decrease as a percent of net sales, net operating profit will rise. Some companies prefer to use profit before income taxes, since income tax in small business is often influenced by factors other than those involved in running the business. No matter which you prefer to use, net operating profit is a good overall measure of how well gross margin and expenses are being controlled.

**Net Ordinary Income.** The amount of money retained after all expenses are subtracted from gross profit, but before "other" expenses and income are accounted for.

**Net Purchases.** Invoices and return/credit memos.

**Net Revenue.** The amount of money that shows first on your profit & loss statement. Because of its location on the report, net revenue is also referred to as "top-line revenue." The reason this is "net" revenue even though it's at the top is because customer returns should already be subtracted out.

**Net Worth.** The same as Equity - all of a business's assets minus all liabilities.

**Newsletter Co-Op.** This type of co-op is given for titles promoted in a store's direct newsletter (Shelf Awareness, Indie Next, etc. do not qualify). The store chooses the titles to promote, and a supporting order, photo, and/or blurb may be required. Mostly limited to frontlist titles and require them to be featured within 3 months of the publication date. All publishers have a standard rate, which could be between $20-80/title, depending on the publisher. HarperCollins, Sourcebooks, and Hachette/Workman all offer newsletter co-op.

**Non-Exempt.** An employee who is entitled to minimum wage and overtime pay protections under the Fair Labor Standards Act (FLSA).

**Notes Payable.** Money you owe to a lender, whether an institution or an individual, and generally last longer than one year; used to purchase assets.

**Operating Activities.** Regular expenses, inventory purchased or sold, accounts receivable and payable, preorder sales, and gift cards. These could be cash in or cash out, depending on the transaction.

**Other Expense.** Expenses that do not relate to a company's main business. As well as operating costs, the company needs to consider other expenses including interest expense and losses from disposing of fixed assets.

**Other Income**. Income that does not come from a company's main business, such as interest. Examples include income from interest, rent, and gains resulting from the sale of fixed assets.

**Owner Loan/Shareholder Loan**. An amount that you, as a shareholder, owe to your corporation. Typically, a shareholder is paid from the corporation through either salary or dividends. Dividends are paid from after-tax corporate profits and taxed at a personal level.

**Owner's Compensation.** The payments made to owners of businesses for providing services which could be provided by third parties.

**Owner's Draw.** A drawing account is an accounting record maintained to track money and other assets withdrawn from a business by its owners. A drawing account is used primarily for businesses that are taxed as sole proprietorships or partnerships. Owner withdrawals from businesses that are taxed as separate entities must be accounted for generally as either compensation or dividends.

**Packing Slip.** Information included in the shipment that shows what has been included, might also show items from the original order that were NOT shipped and have been backordered. Packing slips do not usually show the price, discount, or remittance information for paying the invoice.

**Payroll Tax Payable.** A liability account that contains the combined total of payroll taxes deducted from employee pay and the employer portion of payroll taxes. The balance in this account is increased by the addition of new liabilities, and reduced by payments made to the applicable governing authorities.

**Percentage Threshold.** Helps you understand if a deviation is concerning. You should set a maximum percentage deviation to tell you when you should investigate each budget item.

**Periodic Inventory System.** Under the periodic system, the amount of purchased inventory is compiled throughout a period and added to the beginning inventory to arrive at the amount of inventory available for sale. A physical count at the end of the period establishes the ending inventory valuation, which is subtracted from the amount of inventory available for sale to arrive at the cost of goods sold for the period. Thus, the calculation in which the contents of the purchases account is used is: (Beginning inventory + Purchases – Ending inventory) = Cost of Goods Sold.

**Perpetual Inventory System.** The purchases account is not used in a perpetual inventory system, where inventory purchase and usage transactions immediately update the inventory records, with the intent of maintaining accurate record balances at all times (not just at the end of the reporting period).

**Petty Cash.** An accessible store of money kept to spend on small items.

**Physical Inventory.** An actual count of the goods in stock. This can involve counting, weighing, and otherwise measuring items, as well as asking third parties for counts of inventory items that have been consigned to them. If a business is maintaining inventory records for each item in stock, then these counts are compared to the recorded balances; the recorded amounts are then changed to match the physical counts.

**Pool Co-Op.** This type of co-op is based on how much money you spend with a publisher. Some publishers calculate this based on the last fiscal year, and others based on the current fiscal year. Usually, it's about 2-4% of your retail spend. Some publishers have multiple pools. Pools can be automatically credited, but some are not automatic. Every Big 5 publisher offers pool co-op.

**Prepaid Account.** You pay upfront for orders.

**Prepaid Expenses.** Expenses that have been paid for in advance but not yet incurred. In business, a prepaid expense is recorded as an asset on the balance sheet that results from a business making advance payments for goods or services to be received in the future. Prepaid expenses are initially recorded as assets, but their value is expensed over time onto the income statement. Unlike conventional expenses, the business will receive something of value from the prepaid expense over the course of several accounting periods.

**Productive Debt.** Debt, such as money owed to vendors, that is tied directly to your productivity, or sales.

**Profit**. An amount of money that you gain when you are paid more for something than it cost you to make, get, or do it.

**Profit & Loss Statement (P&L)**. A financial statement that summarizes the revenues, costs, and expenses incurred during a specified period, usually a quarter or fiscal year. These records provide information about a company's ability or inability to generate profit by increasing revenue, reducing costs, or both. P&L statements are often presented on a cash or accrual basis. Company managers and investors use P&L statements to analyze the financial health of a company. Can also be referred to as "income statement" or "statement of operations."

**Publisher Promotions (Promos)**. Promos, or promotions, are deals that publishers offer that typically get you extra points on your discount, but also sometimes include things like swag or signed copies. Promos get you higher discounts, which means higher profit and lower cost of goods sold.

**Purchase Order Number (PO number).** A unique identifying number assigned to a purchase order – the document detailing the buyer's intention to purchase goods or services from a specific vendor or supplier. The PO number is important for managing and tracking purchases, as well as an asset in record keeping for AP and accounting teams.

**Purchases Account.** A general ledger account in which is recorded the inventory purchases of a business. This account is used to calculate the amount of inventory available for sale in a periodic inventory system.

**Quickbooks Classes**. In QuickBooks, you can create classes that you assign to transactions. This lets you track account balances by department, business office or location, separate properties you own, or any other meaningful breakdown of your business.

**Ratio**. An expression of the relative size of two numbers by showing one divided by the other.

**Real Revenue**. A term used in *Profit First* to show an entrepreneur that their top line revenue is not truly representative of the size of the business.For example, a home builder may have $10M in annual revenue and to complete their projects require materials and subcontractors that cost $7M a year. What this means is that the company really has $3M of "real revenue" and manages another $7M of transactions (effectively moving money from the customer directly to

the purchase of materials and the cost of subcontractors. This business needs to operate like a $3M company and not a $10M company. The term Real Revenue is used to make it very clear that the entrepreneur really has a $3M business.

**Reconciliation.** The accounting process that takes place at the end of a period when two sets of financial data are compared to ensure accuracy.

**Remit.** To transmit or send (money, a check, etc.) to a person or place, usually in the form of a payment.

**Remittance Advice.** The information you send to your vendor when sending a payment to indicate exactly which invoices you are paying and which credit memos you are applying with that payment. This is essential when sending payments via ACH, or if paying by paper check, if the list of items being paid is too long to fit on the check stub. You can enclose a paper printout or a copy of your statement with your check that shows exactly which items are being paid, or you can send this information via email to an email address they have especially for this purpose.

**Retained Earnings.** A business's cumulative net profit after accounting for dividends.

**Retirement Plan.** A method for saving and investing money for retirement.

**Return On Assets.** Annual Profit Before Tax/End-of-Year Total Assets. It is an excellent indicator of the return rate received, based on total assets employed in running the business. Return On Assets measures ROI from a business management standpoint.

**Return On Investment (ROI).** The key measure of the profit derived from any investment. It is a ratio that compares the gain or loss from an investment relative to its cost. Although ROI is a ratio, it is typically expressed as a percentage rather than as a ratio. One method of calculating is ROI= Cost of Investment /Net Return on Investment ×100%.

**Return On Net Worth.** The best measure of return to the owners of the business. It is typically defined as profit before tax to net worth. Return on net worth is the return rate owners receive, compared to the amount of equity that they are maintaining in the business.

**Roth IRA.** A type of individual retirement account that allows for tax-free growth and withdrawals in retirement.

**Runway.** The number of months a company has before the company is out of cash.

**Sales.** The amount of money a business makes selling items.

**Sales Tax Payable.** A liability account in which is stored the aggregate amount of sales taxes that a business has collected from customers on behalf of a governing tax authority. The business is the custodian of these funds, and is liable for remitting them to the government on a timely basis.

**Semi-Monthly.** When you pay your employees twice a month on specific dates

**SIMPLE IRA.** Savings Incentive Match Plan for Employees of Small Employers. A retirement plan that allows employers and employees to contribute to a traditional IRA for the employee.

**Single-Entry Accounting.** Where a transaction only has to be recorded against one category, either an income account or an expense account.

**SIT & FIT.** State income tax & Federal Income Tax. Depending on the income bracket the employee falls into, they are required to pay a percentage of their taxable income to income tax. Employers withhold these amounts from employees paychecks and submit to the federal or state government on a regular basis, monthly or quarterly as required.

**Sole Proprietorship.** A business owned and operated by a single person, with no legal distinction between the owner and the business.

**Specific Cost.** Under this method, you receive against invoices, and the point-of-sale system tracks the cost of each individual item so when you run your starting and ending inventory reports, you get the cost of just the particular books remaining in inventory.

**Spending Plan.** A more accessible way of budgeting.

**State Unemployment Tax (SUTA).** Depending on the state it's 2% to 5% of an employee's wages.

**Statement.** A monthly summary from a vendor of all open (unpaid) invoices and open (unused) credit memos, showing the amounts due, dates due, and aging information.

**Subaccount.** Entities set up sub accounts for a variety of bookkeeping and administrative purposes. A sub account is often used to compartmentalize larger accounts, thereby allowing for better tracking of various budget details and expenses. For ease of record-keeping, a company might set up sub accounts for each of its departments. Can also be called a "subsidiary ledger."

**Taxes Payable.** The actual amount owed in taxes.

**Tax Professional.** A person with the knowledge, credentials, and hands-on experience to assist with tax preparation.

**Terms Account.** You can send an order, which will ship, but the bill won't be due for at least 30 days (Net 30), but sometimes not for 60, 90, or even 120 days. Taking advantage of terms means maximizing the amount of time you have to sell merchandise before you pay for it.

**Till.** Cash drawer/register where cash is kept.

**Top Line Revenue.** A company's revenues or gross sales. Therefore, when a company has "top-line growth," the company is experiencing an increase in gross sales or revenues.

**Trailing Twelve-Month (TTM) P&L.** Keeps a running tab of how well an investment or project has performed over the prior twelve-month period. It takes the monthly or quarterly returns over that time period and reports a weighted average profit or loss figure.

**Turn & Earn Profitability Index.** Helps you balance turnover and profits. It is calculated by multiplying inventory turns by the gross margin percentage. It highlights situations

where high margins can compensate for low inventory turns. A similar measurement to the Turn/Earn Index is Gross Margin Return on Investment (GMROI). Please note that while the Turn/Earn Index and GMROI both measure profitability, they do so based on two different scales (sort of like Fahrenheit and Centigrade temperatures). It doesn't matter whether you calculate a T/E Index or GMROI. Either is a wonderful gauge of the profitability performance of your investment in stock inventory.

**Variable Expense.** Depends on the volume of sales.

**Vendor Balance Summary Report.** Shows your company's current balance with each vendor.

**Year-End.** The end of the fiscal year.

**Year-Over-Year Tracking (YOY).** Tracking the finances of a specific event each year and comparing. The formula for Year-Over-Year tracking is: YOY = (This Year's Number – Last Year's Number)/Last Year's Number

## TAX FORMS

**940**. Employer's annual FUTA tax return.

**941**. Employer's quarterly tax return reporting withholding and the employer's share of FICA.

**944**. For small employers eligible to pay employment taxes annually rather than depositing them according to a schedule.

**1099**. One of several IRS tax forms used in the United States to prepare and file an information return to report various types of income other than wages, salaries, and tips. This is used to report independent contractor annual earnings.

**1099-K**. You should receive Form 1099-K by Jan. 31 if, in the prior calendar year, you received any payments from payment card transactions ( including debit cards, credit cards, or stored-value cards), and/or in settlement of third-party payment network transactions (PayPal, Venmo, Zelle, etc.) involving: for the 2022 tax year and beyond, gross payments of more than $600 with no transaction threshold.

**1128.** To request a change in tax/fiscal year.

**3115.** To request a change in accounting method.

**I-9**. Officially the Employment Eligibility Verification, is a United States Citizenship and Immigration Services form. Mandated by the Immigration Reform and Control Act of 1986, it is used to verify the identity and legal authorization to work of all paid employees in the United States.

**Schedule C.** Schedule C: Profit or Loss from Business is an Internal Revenue Service (IRS) tax form that is used to report income and expenses for a business. Schedule C must accompany Form 1040, which is a taxpayer's main tax return. Self-employed individuals, sole proprietors of a business, or a single-member limited liability company (LLC) must report any activity conducted for income or profit using Schedule C. The resulting profit or loss calculations are commonly considered self-employment income.

**W2.** An Internal Revenue Service tax form used in the United States to report wages paid to employees and the taxes withheld from them. Employers must complete a Form W-2 for each employee to whom they pay a salary, wage, or other compensation as part of the employment relationship.

**W4.** An Internal Revenue Service tax form completed by an employee in the United States to indicate his or her tax situation to the employer. The W-4 form tells the employer the correct amount of federal tax to withhold from an employee's paycheck.

**W9.** An Internal Revenue Service tax form that provides taxpayer information to the entity that requested it. It is not filed with the IRS; it's returned to the requester. The form is filled out by independent contractors who provide services to companies that have not hired them as full-time employees. If contractors are paid $600 or less in a single year by a company, they will not need to fill out the form for that company.

*Appendix C*

# Further Reading

*Accounting for Dummies* by John A. Tracy & Tage C. Tracy, ISBN: 9781119837527

*The Accounting Game* by Darrell Mullis & Judith Orloff, ISBN: 9781402211867

*The Accounting Game: The Ultimate Guide to Accounting Basics, Learn All About Financials That Every Business Owner Should Know and Become Your Very Own Accountant* by Hans Angove (audiobook only), ISBN: 9781662127595

*Accounting for the Numberphobic* by Dawn Fotopulos, ISBN: 9780814434321

*The Emotion Behind Money* by Julie Murphy Casserly, ISBN: 9781935766797

*Financial Feminist: Overcome the Patriarchy's Bullsh*t to Master Your Money and Build a Life You Love* by Tori Dunlap, ISBN: 9780063260269

*The Mathematics of Bookselling* by Leonard Shatzkin, ISBN: 9780878380251

*Profit First* by Mike Michalowicz, ISBN: 9780735214149

*Quickbooks 2023 All-in-One for Dummies* by Stephen L. Nelson, ISBN: 9781119906131

*Unf*ck Your Worth: Overcome Your Money Emotions, Value Your Own Labor, and Manage Financial Freak-Outs in a Capitalist Hellscape* by Faith G. Harper, ISBN: 9781621064565

*Appendix D*

# Online Resources

*5 Steps to Learn Financial Accounting Without an Accounting Background*. Cote, Catherine. July 1, 2020. https://online.hbs.edu/blog/post/how-to-learn-accounting

*The 6 Best Online Accounting Courses of 2023*. Hanna, Megan. April 5, 2023. https://www.thebalancemoney.com/best-online-accounting-courses-5115826

**Free Course:** *Basic Accounting*. Offered by Accounting Intuition. https://alison.com/course/basic-accounting

**Free Course:** *Fundamentals of Financial and Management Accounting*. Offered by Politecnico di Milano via Coursera. https://www.coursera.org/learn/financial-accounting-polimi

**Free Course:** *Financial Accounting: Foundations*. Offered by the University of Illinois at Urbana-Champaign via Coursera. https://www.coursera.org/learn/financial-accounting-basics

**Free Course:** *Financial Accounting Fundamentals*. Offered by the University of Virginia via Coursera. https://www.coursera.org/learn/uva-darden-financial-accounting

*Appendix E*

# Sources

* Note: All sources were accessed when developing the course in 2022.

*AccountingTools: Accounting CPE Courses & Books*. http://accountingtools.com. *Beginner-Bookkeeping*. www.beginner-bookkeeping.com.
*American Booksellers Association Bookweb*. https://bookweb.org.
*Collins Dictionary*. www.collinsdictionary.com.
*Conectier*. www.conectier.com.
*Dictionary.com*. www.dictionary.com.
*Effective Inventory Management, Inc*. https://effectiveinventory.com.
*FBC Tax Bookkeeping and Payroll*. http://fbc.ca.
*Gartner*. www.gartner.com.
*Harvard Business School Online YouTube Channel*. https://www.youtube.com/@HBSOnline
*Indeed*. https://indeed.com.
*Investopedia*. www.investopedia.com.
*Kubera*. www.kubera.com.
*Netsuite*. www.netsuite.com.
*NOLO*. www.nolo.com.
*Oxford Languages*. https://languages.oup.com/dictionaries.
*Profit First University*. https://profitfirstuniversity.com.
*QuickBooks*. https://quickbooks.intuit.com.
*TD Bank*. www.td.com.
*Tipalti*. www.tipalti.com.
*Tipalti Approve*. www.approve.com.
*Toucan*. www.toucantoco.com/en.
*Valupaedia*. www.valupaedia.com/index.php/business-dictionary.
*Wikipedia*. https://wikipedia.com.
*Zeni*. www.zeni.ai.