

# How to read a financial statement

A simple guide for small business owners



|               |          |      |
|---------------|----------|------|
| Sales         | \$10,948 | +28% |
| Purchased     | \$34,341 | 12%  |
| Customer      | 4,220    | +29% |
| Total Earning | \$81,416 | +24% |



## Your guide to understanding financial statements

We're happy to see you here, digging into another educational resource developed to help you feel confident about your financial health by breaking down the components of a financial statement in a way that's easy to understand.

### The importance of knowing your financial health

When it comes to running a successful small business, understanding the state of your financial health is *just as important* as the quality of the products and services you provide. But the world of financial statements can feel confusing and overwhelming. If you've ever felt lost trying to make sense of your balance sheet, income statement or cash flow statement, you're not alone.

In fact, **40% of small business owners** consider themselves to be financially illiterate. And at the same time, 81% of them are doing their business's finances.

While that may sound dire, there's good news. Financial statements don't have to be overwhelming. Think of them as the tools that give you a clear picture of your business's financial condition. They'll help you make informed decisions that drive the success of your business.

Whether you're looking to manage your cash flow more effectively, improve your profitability or simply understand where your money is going, having a solid grasp on your financial statements is key.



In this eBook, we'll break down the components of a financial statement in a way that's easy to understand and absorb, giving you the straightforward explanations you need to make sense of—and take control of—your business's finances.

We'll also show you how to work with your trusted advisor to get the most out of your financial statements. After all, understanding the numbers is the first step; knowing how to use that information to make smart business decisions is where you'll find the real value.

So, let's get started.

**Understanding the numbers is the first step; knowing how to use that information to make smart business decisions is where you'll find the real value.**

## Financial statement basics

Before we dive into the nitty-gritty of financial statements, it's important to understand what they are and why they're essential for your business. Simply put, a financial statement is a report that gives you an overview of your business's financial health and performance. Think of it as a report card of sorts.

There are three main types of financial statements:

- Balance sheet
- Income statement
- Cash flow statement

Each of these statements serves its own purpose. But together, they provide a complete picture of your business's financial health.

### The balance sheet

The balance sheet is a snapshot of your business at a specific moment in time. It shows you what you own (assets), what you owe (liabilities) and what's left over for the owners (equity).

Let's dive into each.

■ **Assets** are what your business owns and are divided into two categories:

- **Current assets.** These are the assets that can be converted into cash within a year, like cash itself, accounts receivable (money owed to you) and inventory.
- **Non-current assets.** These are long-term investments, property, equipment and intangible assets, like patents, that will benefit your business in the long run.

| [ COMPANY NAME ]               |                           | BALANCE SHEET        |  |
|--------------------------------|---------------------------|----------------------|--|
| TIME PERIOD COVERED            |                           |                      |  |
| May 4th, 20XX - July 4th, 20XX |                           |                      |  |
| TOTAL CURRENT ASSETS           | TOTAL CURRENT LIABILITIES | TOTAL CURRENT EQUITY |  |
| \$7,850.00                     | \$4,000.00                | \$6,723.00           |  |
| BALANCE SHEET                  |                           |                      |  |
| CATEGORIES                     | FY1                       | FY2                  |  |
|                                | PRIOR YEAR                | CURRENT YEAR         |  |
| ASSETS                         |                           |                      |  |
| Current Assets                 | \$ 1,500.00               | \$2,200.00           |  |
| Fixed Assets                   | \$ 1,200.00               | \$3,300.00           |  |
| Other                          | \$ 2,200.00               | \$2,350.00           |  |
|                                | \$ -                      | \$-                  |  |
| <b>TOTAL ASSETS</b>            | <b>\$ 4,900.00</b>        | <b>\$7,850.00</b>    |  |
| LIABILITIES                    |                           |                      |  |
| Current Liabilities            | \$ 500.00                 | \$1,245.00           |  |
| Intermediate Liabilities       | \$ 123.00                 | \$2,232.00           |  |
| Long-Term Liabilities          | \$ 678.00                 | \$523.00             |  |
|                                | \$ -                      | \$-                  |  |
| <b>TOTAL LIABILITIES</b>       | <b>\$ 1,301.00</b>        | <b>\$4,000.00</b>    |  |
| EQUITY                         |                           |                      |  |
| Owner Equity                   | \$ 5,683.00               | \$6,723.00           |  |
|                                | \$ -                      | \$-                  |  |
| <b>TOTAL EQUITY</b>            | <b>\$ 5,683.00</b>        | <b>\$6,723.00</b>    |  |

Sample balance sheet

■ **Liabilities** are what your business owes to others. They're also divided into two categories:

- **Current liabilities.** These are obligations you need to pay within the year, like accounts payable (money you owe to suppliers), short-term loans and taxes.
- **Non-current liabilities.** These are your longer-term obligations, such as mortgages or long-term loans, that aren't due in the near future.

■ **Equity** represents the owners' interest in the business once all liabilities are settled.

- It's calculated as **Equity = assets - liabilities**.
- It includes things like retained earnings (profits that have been reinvested into the business), common stock and any initial investment made by the owners.



**The balance sheet is a snapshot of your business at a specific moment in time.**

## The income statement

The income statement, also known as the profit and loss (P&L) statement, tells you how your business performed over a specific period. It shows your revenue, expenses and the resulting profit or loss (i.e., net income).

■ **Revenue.** This is the total amount of money your business earns from its operations. It's often referred to as the "top line" because it appears at the top of the income statement. Revenue, also known as sales or turnover, can come from selling products, providing services or any other core business activities.

■ **Expenses.** These are the costs incurred by your business to generate revenue. They're typically divided into the following three categories:

- **Cost of goods sold (COGS).** This refers to the direct costs related to producing goods or services, like raw materials and labor.
- **Operating expenses.** These are indirect costs, like rent, utilities, salaries, marketing and other day-to-day expenses.
- **Non-operating expenses.** These are costs unrelated to your core business operations, such as interest payments on loans.

■ **Net income.** This is the profit your business makes after deducting all expenses as revenue. It's often called the "bottom line" because it's the final figure on your income statement.

- It's calculated as **Net income = revenue - expenses.**
- If the number is positive, you made a profit (i.e., you're "in the black")! If it's negative, your business incurred a loss (i.e., you're "in the red").

| INCOME STATEMENT                         |                            |                   |
|--|----------------------------|-------------------|
| COMPANY NAME                             | STATEMENT REPORTING PERIOD |                   |
|  | STARTING DATE              | ENDING DATE       |
|  | XX/XX/XX                   | to XX/XX/XX       |
| REVENUE                                  | STARTING                   | ENDING            |
| Sales revenue                            | \$ 150,000                 | \$ 175,000        |
| (Less sales returns and allowances)      | \$ -                       | \$ -              |
| Service revenue                          | \$ 50,500                  | \$ 75,000         |
| Interest revenue                         | \$ -                       | \$ -              |
| Other revenue                            | \$ -                       | \$ -              |
| <b>Total Revenues</b>                    | <b>\$ 200,500</b>          | <b>\$ 250,000</b> |
| EXPENSES                                 | STARTING                   | ENDING            |
| Advertising                              | \$ 500                     | \$ 450            |
| Bad debt                                 | \$ -                       | \$ -              |
| Commissions                              | \$ -                       | \$ -              |
| Cost of goods sold                       | \$ 55,000                  | \$ 75,000         |
| Depreciation                             | \$ -                       | \$ -              |
| Employee benefits                        | \$ -                       | \$ -              |
| Furniture and equipment                  | \$ -                       | \$ -              |
| Insurance                                | \$ -                       | \$ -              |
| Interest expense                         | \$ 2,000                   | \$ 2,500          |
| Maintenance and repairs                  | \$ -                       | \$ -              |
| Office supplies                          | \$ -                       | \$ -              |
| Payroll taxes                            | \$ -                       | \$ -              |
| Rent                                     | \$ -                       | \$ -              |
| Research and development                 | \$ -                       | \$ -              |
| Salaries and wages                       | \$ 65,000                  | \$ 85,000         |
| Software                                 | \$ -                       | \$ -              |
| Travel                                   | \$ -                       | \$ -              |
| Utilities                                | \$ -                       | \$ -              |
| Web hosting and domains                  | \$ -                       | \$ -              |
| Other                                    | \$ -                       | \$ -              |
| <b>Total Expenses</b>                    | <b>\$ 122,500</b>          | <b>\$ 142,950</b> |
| <b>Net Income Before Taxes</b>           | <b>\$ 78,000</b>           | <b>\$ 87,050</b>  |
| <b>Income tax expense</b>                | <b>\$ 15,600</b>           | <b>\$ 17,410</b>  |
| <b>Income from Continuing Operations</b> | <b>\$ 62,400</b>           | <b>\$ 69,640</b>  |
| <b>Net Income</b>                        | <b>\$ 62,400</b>           | <b>\$ 69,640</b>  |

Sample income statement

The income statement, also known as the profit and loss (P&L) statement, tells you how your business performed over a specific period.

## The cash flow statement

A cash flow statement shows how cash moves in and out of your business. It helps you understand whether your business generates enough cash to cover its expenses and invest in future growth. It also shows whether you rely too much on external financing to stay in business.

A cash flow statement is divided into three sections:

- Operating activities.** This section includes the cash generated or used by your business's core operations, like cash receipts from sales and payments for expenses like suppliers and salaries.
- Investing activities.** This section covers the cash spent on purchasing long-term assets like equipment or property, as well as any cash received from selling these assets.
- Financing activities.** This section shows how cash flows from transactions with the business's owners and creditors, like borrowing or repaying loans, issuing or buying back shares, and paying dividends to shareholders.

| SIMPLE SMALL BUSINESS CASH FLOW TEMPLATE   |                |     |                 |     |                        |
|--|----------------|-----|-----------------|-----|------------------------|
| COMPANY NAME   | MANAGER NAME   |     | COMPLETED BY    |     | DATE COMPLETED         |
|  | CURRENT PERIOD |     | PREVIOUS PERIOD |     | INCREASE (or DECREASE) |
|  | BEGIN          | END | BEGIN           | END |                        |
| BEGINNING BALANCE / CASH ON HAND   | \$             | -   | \$              | -   | \$                     |
| <b>(+) CASH RECEIPTS</b>   |                |     |                 |     |                        |
| CASH SALES   | \$             | -   | \$              | -   | \$                     |
| CUSTOMER ACCOUNT COLLECTIONS   | \$             | -   | \$              | -   | \$                     |
| LOAN / CASH INJECTION  | \$             | -   | \$              | -   | \$                     |
| INTEREST INCOME  | \$             | -   | \$              | -   | \$                     |
| TAX REFUND   | \$             | -   | \$              | -   | \$                     |
| OTHER CASH RECEIPTS  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| <b>TOTAL CASH RECEIPTS</b>   | \$             | -   | \$              | -   | \$                     |
| <b>(-) CASH PAYMENTS</b>   |                |     |                 |     |                        |
| <b>(-) COST OF GOODS SOLD</b>  |                |     |                 |     |                        |
| DIRECT PRODUCT / SERVICE COSTS   | \$             | -   | \$              | -   | \$                     |
| PAYROLL TAXES / BENEFITS - DIRECT  | \$             | -   | \$              | -   | \$                     |
| SALARIES - DIRECT  | \$             | -   | \$              | -   | \$                     |
| SUPPLIES   | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| <b>TOTAL COST OF GOODS SOLD</b>  | \$             | -   | \$              | -   | \$                     |
| <b>(-) OPERATING EXPENSES</b>  |                |     |                 |     |                        |
| ACCOUNT FEES   | \$             | -   | \$              | -   | \$                     |
| ADVERTISING  | \$             | -   | \$              | -   | \$                     |
| BANK FEES  | \$             | -   | \$              | -   | \$                     |
| CONTINUING EDUCATION   | \$             | -   | \$              | -   | \$                     |
| DUES / SUBSCRIPTIONS   | \$             | -   | \$              | -   | \$                     |
| INSURANCE  | \$             | -   | \$              | -   | \$                     |
| INTERNET   | \$             | -   | \$              | -   | \$                     |
| LICENSES / PERMITS   | \$             | -   | \$              | -   | \$                     |
| MEALS / ENTERTAINMENT  | \$             | -   | \$              | -   | \$                     |
| OFFICE SUPPLIES  | \$             | -   | \$              | -   | \$                     |
| PAYROLL PROCESSING   | \$             | -   | \$              | -   | \$                     |
| PAYROLL TAXES / BENEFITS - INDIRECT  | \$             | -   | \$              | -   | \$                     |
| POSTAGE / SHIPPING   | \$             | -   | \$              | -   | \$                     |
| PRINTING   | \$             | -   | \$              | -   | \$                     |
| PROFESSIONAL SVCS  | \$             | -   | \$              | -   | \$                     |
| OCCUPANCY  | \$             | -   | \$              | -   | \$                     |
| RENTAL FEES  | \$             | -   | \$              | -   | \$                     |
| SALARIES - INDIRECT  | \$             | -   | \$              | -   | \$                     |
| SUBCONTRACTORS   | \$             | -   | \$              | -   | \$                     |
| TELEPHONE  | \$             | -   | \$              | -   | \$                     |
| TRANSPORTATION   | \$             | -   | \$              | -   | \$                     |
| TRAVEL   | \$             | -   | \$              | -   | \$                     |
| UTILITIES  | \$             | -   | \$              | -   | \$                     |
| WEB DEVELOPMENT  | \$             | -   | \$              | -   | \$                     |
| WEB DOMAIN AND HOSTING   | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| <b>TOTAL OPERATING EXPENSES</b>  | \$             | -   | \$              | -   | \$                     |
| <b>(-) ADDITIONAL EXPENSES</b>   |                |     |                 |     |                        |
| CASH DISBURSEMENTS TO OWNERS   | \$             | -   | \$              | -   | \$                     |
| CHARITABLE CONTRIBUTIONS   | \$             | -   | \$              | -   | \$                     |
| INTEREST EXPENSE   | \$             | -   | \$              | -   | \$                     |
| INCOME TAX EXPENSE   | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| OTHER  | \$             | -   | \$              | -   | \$                     |
| <b>TOTAL ADDITIONAL EXPENSES</b>   | \$             | -   | \$              | -   | \$                     |
| <b>TOTAL CASH PAYMENTS</b>   | \$             | -   | \$              | -   | \$                     |
| <b>NET CASH CHANGE<br/>(CASH RECEIPTS - CASH PAYMENTS)</b>                           | \$             | -   | \$              | -   | \$                     |
| <b>MONTH ENDING CASH POSITION<br/>(CASH ON HAND + CASH RECEIPTS - CASH PAYMENTS)</b> | \$             | -   | \$              | -   | \$                     |

Sample cash flow statement



A cash flow statement shows how cash moves in and out of your business.

## How to work with your trusted advisor

Being able to understand financial statements is one thing—making informed business decisions based on them is another. This is where your trusted advisor comes in. And here's how you can make the most of that relationship.

### Ask questions

Don't be afraid to ask your advisor questions about anything you don't understand. If something is unclear, ask for an explanation in simple terms. Financial statements can be complex, and your advisor is there to help you understand and interpret the numbers.

### Communicate regularly

Schedule regular meetings with your advisor to discuss your financial statements. Staying in touch ensures that you stay informed about the financial health of your business and helps you spot potential issues early.

### Set goals

Work with your advisor to set realistic financial goals for your business. Whether you're considering an expansion, taking on new debt, managing cash flow or reducing debt, having clear goals allows you to create strategies to achieve those goals—and track progress over time.

### Review key metrics

Focus on the key financial metrics that are important to your business. Your advisor can help you identify and track these metrics so you can monitor the performance of your business.

### Use financial statements to make decisions

Remember, your financial statements are the tools that guide your business decisions. Your advisor can help you analyze your statements and guide you to make informed decisions.

## Practical tips for small business owners

Here are some tips to help you get the most out of your financial statements.

### ■ Keep accurate records

Accurate record-keeping is essential for reliable financial statements. Make sure to keep detailed records of every financial transaction.

### ■ Use accounting software

Consider using accounting software to streamline record-keeping and reporting. Software can automate tasks and provide real-time insights into your finances.

### ■ Monitor your cash flow

Keep an eye on your cash flow statement to make sure you have enough cash to cover your expenses and invest in growth.

### ■ Analyze your profit margins

Identify areas where you can cut costs or increase revenue by using your income statement to calculate profit margins.

### ■ Plan for taxes

Work with your advisor on your tax plan. Understanding your obligations and planning ahead can help you avoid surprises.

### ■ Check balance sheet ratios

Assess your business's liquidity and financial stability by calculating ratios, such as the current ratio (current assets divided by current liabilities).

### ■ Plan for the future

Use your financial statements to create budgets, forecast future performance and help you plan for long-term growth.



## Summing it all up

We hope this eBook will help you better understand financial statements so you can run your business more effectively. If you'd like an experienced guide to assist you in the financial areas of your business—someone who can provide personalized advice based on your specific business situation—and would prefer to work with a trusted advisor, we're available and ready to help.

Just click the **GET IN TOUCH** button and complete the brief form or give us a call. We look forward to hearing from you!