• A •

ABLs (asset-based lenders), 220-221 accelerated deductions, 235 account offsets, 98, 100, 302 accountants CPAs, 2, 128, 129, 271 focus on errors by, 267 offsetting not allowed by, 44 usage in this book, 2 accounting. See also cash management accrual-basis, 13, 15, 27-28, 31-34, 62-65 business versus personal, 23 cash-basis, 13, 18, 24, 31-34, 228-229 controlling electronic-based systems, 259 - 262disbursement cycle view, 312 errors masked in balance sheet, 44 for financial reporting, 27, 29–31 four functions of, 24-31 IRS requirements, 27, 28, 32, 33-34, 228 limiting access to records, 274 managerial, 26-27 more than recordkeeping, 23 purchase-order system 314 recordkeeping, 23, 25-26, 31 scrubbing the balance sheet, 103-110 selling cycle view, 282 for tax law compliance, 28-29 Accounting For Dummies (Tracey), 11 Accounting Periods and Methods (IRS publication), 28 accounting-driven budgets, 184-185 accounts payable. See also disbursement cycle; vendors and suppliers on balance sheet, 34, 49, 89 cash trail in, 242-243 decrease in statement of cash flows. 64 - 65described. 35 disputed, 101 expected payment terms for, 101

in expense accounting, 12 JIT payment strategies, 320 leveraging, 111-112 negotiating terms for, 89, 225 NSTOP figured using, 117 trade receivable offsets, 98, 100, 302 accounts receivable. See also customers; selling cycle allowance for returns and discounts, 98 on balance sheet 34, 48, 86 bankrupt customers, 294 cash trail in 242-243 collectability of, 97-98 concentration of, 305 converting to cash, 110-111 currency for payment, 303 days sales outstanding, 86, 95 described, 35 electronic payments, 257-258, 286, 288, 300 eligible for leveraging, 304–305 factoring, 223-224 increase in statement of cash flows, 62 invoices, 291-292 liquidity issues for, 144 loan advances against, 152 mismanaging, 341-342 NSTOP figured using, 117 old trade, liquidating, 149 overdue amounts in, 42 in revenue accounting, 12 with sales growth or decline, 75, 76 scrubbing (case study), 104 terms and conditions, 289-291 trade payable offsets for, 98, 100, 302 accredited investors, 200 accrual, meaning of, 31 accrual-basis accounting cash flows not well shown by, 13, 15, 27 cash-basis compared to, 13, 31-33 defined. 31 deriving statement of cash flows, 62-65 deviations from, 33-34

accrual-basis accounting (continued) IRS requirements for, 27, 28 recognizing in financial reports, 32-33 required for business, 23 accrued expenses payable, 34, 35, 49, 65, 117 accrued liabilities, 89, 105-106 accumulated depreciation, 43-44, 49, 63-64 ACH (automated clearing house), 257, 288, 301 acid-test or quick ratio, 95, 139 advance rates, 305-306 advances from customers, 299-300 Alight Planning Enterprise software, 174 amortization on intangible assets, 74, 104 angel investors, 200 Arm forecasting, 186 asset-based lenders (ABLs), 220-221 assets. See also depreciation in accrual accounting, 33 appraising regularly, 274–275 on balance sheet, 34, 84, 85-88 book value of, 43 cash flow effect of changes, 63 cash sources in, 110-111 changes in statement of cash flows, 69-72 current, 84 evaluating, 96-100 fixed, 43, 52 intangible, amortization on, 74 leasing as capital source, 221–223 leveraging, 151–152 liquidating, 149–151 liquidity affected by, 143–145 loan advances against, 152 long-term operating, 20, 43, 52, 84 material versus immaterial, 88 nonrecurring write-downs of, 19 off-balance-sheet, 155 offsetting liabilities against, avoiding, 44 quick turnover for small businesses, 337 ratios to liabilities, 95 as real accounts, 38 real cash availability for, 97 revenue compared against, 52 sale lease-back of, 152-153 scrubbing (case study), 103-104 securing debt, 213, 214-215 soft, 343-344 audit trails. 273-274

audited financial statements, 85 audits of cash activity, 253 by CPAs, 128, 129, 271 internal auditing, 280 internal controls required for, 271 surprise, 273 automated clearing house (ACH), 257, 288, 301 available current working capital, 140

• B •

back of the envelope (BOTE), 163 balance sheet accrued liabilities on, 89 age of values on, 46, 96–97 assets segregated from liabilities on, 42 benchmarks with income statement, 52 capitation, 49-52 cash rules for, 115, 119 cash sources on, 86–89, 110–112 comparative format for, 45 condensed, 115-118, 121 current and longer-term categories, 44 current assets on, 84, 86-88 current liabilities on, 85, 89-90 current portion of long-term debt on, 90 defined, 30, 34 disclosure issues for, 43 evaluating assets, 96-100 evaluating liabilities, 100-102 external cash sources not shown, 92-93 fraud or errors masked by, 44 Great Recession driven by, 83 guaranteed debt commitments on, 91 historical nature of, 91-92 importance of, 83-84 information shown by, 37 intent issues for, 97 interrelation with other statements, 37 inventory on, 48, 86-87 knowledge presumed in reader of, 45 layout of, 42, 46 limitations of, 45-47, 91-93 line of credit borrowings on, 90 location of items on, 34, 84-85 long-term assets on, 84, 88 long-term liabilities on, 85, 90, 91

_ Index

net worth in, business value versus, 47 NSTOP on, 116–119 number of accounts on, 42 off-balance-sheet data, 92-93, 102, 154-155 original costs used for, 46 other names for, 34 performance-measurement tools, 93-96 PP&E on, 43-44, 48-49, 52, 88 prepaid expenses on, 48, 87 prevalence of distortion in, 96 prototype, 42 revenue and expenses on, 47-49 rounding of balances on, 45 scrubbing, 103-110 for small businesses, 338 as snapshot in time, 91 standard structure for, 84-85, 86 statement of cash flows compared to, 70 - 72statement of cash flows not reconciled with, 78-79 subsequent events, 47 timing and frequency for, 45, 47 trade accounts payable on, 49, 89 trade accounts receivables on, 48, 86 unaudited versus audited, 85 bank reconciliations, 253 bankrupt customers, 294 banks account types, 250 authorization for accounts, 251 borrowing from, 218-220 cash management tools from, 260-261 compensating balances, 254-255 controlling accounts, 252-254 criteria for loans from, 219-220 establishing accounts, 249-252 FDIC insurance for accounts, 251 lockboxes at, 254, 255, 300 number of accounts needed, 251 percent of people without accounts, 261 roll over refusal by, 73 signers for accounts, 251-252, 276 stop payments, 254 sweep accounts and ZBAs, 255 bartering, 302 behavior of accounts analysis, 117 Better Business Bureaus, 287 bonuses, timing, 325-326

book entry, 64 book value net of accumulated depreciation, 43-44 book value of assets, 43 bookkeeping, 23, 25-26, 31 BOTE (back of the envelope), 163 bottom line, 59, 128, 182 bottom-up forecasting strategy, 175–176 break-even cash-flow scenario, 74 break-even point, 181 budget. See also financial forecasts department responsible for, 173 information for, 174 operating plan implementation, 190 sales-driven versus accounting-driven, 184-185 software for 174 variance analysis, 188-190 Budget Maestro software, 174 Buffet, Warren (investor), 241, 347 burn rate, 76-77, 126, 140, 182 business plan accumulating data for, 160, 166, 170 basic outline for, 160-163 CART concept for, 171–172 coordinating the timing of, 166 creators mirrored in, 160 developing, 163-169 GIGO principle for, 167 historical information for, 165-166 involving key management in, 166 KISS principle for, 169 methods for starting, 163-164 required for loans, 159, 220 SWOT analysis for, 167-169 third-party information in, 169-171 business valuation, 39, 79, 92

• C •

CA (confidentiality agreement), 317 cap table, 182 capital. *See also* debt and debt capital; equity capital on balance sheet, 36, 49–52 in capital expenditures, 20 cash on hand versus, 195 concept of, 194–195 condensed balance sheet showing, 118 353

capital (continued) essence of, 194 free, 51 from generating internal cash flow, 224 gifts and grants for, 225 good use of, 204-208 government aid for, 225 importance for success, 193, 194, 196 net working capital, 95 off-balance-sheet sources of, 92-93. 154-155 from partnerships, 225 qualifying sources of, 209 seed, 197 small business focus on, 335 tips for raising, 209-210 types of, 194 capital expenditures, 20, 61, 66 capital stock, 50, 67-68, 195-196, 203-204 capitalization structure analysis, 118 capitalization table, 182 capitalized start-up costs, 100 CART (complete, accurate, reliable, and timely) information for business plan, 171–172 internal management aided by, 109 invoices, 291-292, 305 for outsiders' confidence, 109-110 for small businesses, 340 cash benchmarks for cash level, 265–266 capital versus, 195 creating from inventory, 323 importance of managing, 241-242 investing in, 51-52 as key business indicator, 262-266 liquidity versus available cash, 133, 142 location on balance sheet, 34 as one component of solvency, 142 presence in every transaction, 242-243 protecting in small businesses, 339-340 recordkeeping for collections, 25 seasonal ebb and flow of, 263-265 selling cycle as consumer of, 283-284 selling cycle generation of, 281 small business focus on, 335

cash burn rate, 76-77, 126, 140, 182 cash flow, defined, 1 cash flow from activities financing activities, 57, 61, 66-69 investing activities, 57, 61, 66 operating activities, 56-57, 61, 62-66 cash flow per share, 124-125 cash inflow, 1 cash management available lender for. 244-245. 246 controlling accounts, 252-254 controlling electronic-based accounting systems, 259-262 electronic transactions for, 256-259 establishing accounts, 249–252 having too much cash, 248 maximizing the cash balance, 254–256 normal cash balance, 245-249 planning for needs, 246 cash outliow, 1 cash payments. See disbursement cycle cash rules, 115, 119 cash-basis accounting, 13, 24, 28, 31–34, 228 - 229cash-flow analysis cash flow as ratio to net income, 125 cash flow compared to sales revenue momentum, 121-123 cash flow per share, 124-125 cash rules for, 115, 119 of changes in financial condition from making profit, 119-121 comparing dividends to cash flow, 125 condensed balance sheet for, 115-118, 121 earnings per share (EPS), 124 EBITDA for, 127 financial reports needed for, 113 fraud considerations, 115 free cash flow, 126 importance of, 113-114 massaging the numbers, 127-129 price-earnings ratio, 124 cash-flow scenarios break-even, 74 monitoring, 72 negative cash flow, 73, 76-77

sales growth or decline, 75-76 steady state, 73-74 cash-flow statement. See statement of cash flows checks accepting payment by, 300 advanced controls for, 261 electronic cash versus, 259 signing authority for, 252, 276 collateral, 150, 217, 219, 288-289 collection agencies, 295 collection efforts, 292-296 commissions, 325-327 common stock, 195-196 compensating balances, 254-255 computer controls, 275 concentration of receivables, 305 confidentiality agreement (CA), 317 contra accounts, 43, 64 cooking the books, 128, 271 cost of goods sold expenses, 17, 28, 96, 177 CPA (certified professional accountant), 2, 128, 129, 271. See also accountants cram down, 321 credit cards, 258, 288, 301 credit reporting agencies, 286-287 credit review and approval, 257-258, 286-289 creditors external, managing, 316--3 priority, 216 unsecured, 215, 225 critical economic drivers, 176-177, 179 cross-aging factor, 306-307 currency for payment, 303 current assets, 84, 110-111, 146 current, defined, 44 current liabilities, 85, 101-102, 214 current ratio, 95, 139 customers. See also selling cycle bankrupt, 294 data sheet for, 287 diversifying the base of, 289-290 80/20 rule for, 289-290 as liquidity sources, 153-154, 225 qualifying, 284-286 reputation risk with, 285 terms and conditions for, 289-291, 292

• /) •

days costs of goods sold outstanding in inventory, 96, 139 days sales outstanding (DSO), 86, 95, 139 debit cards, 258, 261, 301 debt and debt capital. See also lending agreements; liabilities appropriate use of, 112, 213, 216-218 from asset-based lenders, 220-221 assets securing, 213, 214-215 available lender for, 244-245, 246 on balance sheet. 36 bank refusal of roll over, 73 from banks, 218-220 basics, 214-216 business plan required for, 159, 220 cash flow irom financing activities, 67 collateral for, 150, 217, 219 cost of 51 current versus long-term, 101-102 oebt capital, defined, 194 debt, defined, 21, 30 default provisions for, 216 eligible receivables for, 304-305 equity capital compared to, 205–208 exit strategies for capital sources, 210 external capital markets, 338-339 factoring receivables for, 223-224 financial reporting required for, 30-31 finite life of debt, 30 from government programs, 223 inappropriate use of, 145-147 leasing as source of, 221-223 lending agreements, 216, 304-310 leveraging equity for, 50 liquidity issues for, 145–147 loan advances against assets, 152 long-term debt, 67-68, 85, 90, 101-102, 214 misapplying, 345-346 notes payable, 105, 112, 153 personal guarantees for, 216, 219-220 priority creditors for, 216 private equity groups' use of, 202 proactive management of, 338 pros and cons of, 155-156, 237 recording interest paid on, 21

debt and debt capital (continued) roll over, 67 rules for asset investments, 146-147 secondary repayment sources, 219-220 for small businesses, 338-339 subordinated debt, 224 subordination agreements with, 216 tax management for cash flow, 226-237 treating sources as partners, 210 from unsecured creditors, 215, 225 vendor-provided financing, 324 debt holders. See lenders debt load, 50 debt maturity, 214 debt security, 214-215 debt service coverage ratio, 139 debt-to-equity ratio, 96, 139, 205 declining sales, 75-76, 148-149 default provisions for debt, 216 deferring tax obligations, 104, 227 deposits from customers, 299-300 depreciation accounting methods for, 18, 19 accumulated, 43-44, 49, 63-64 adding to profit for cash flow calculation," avoiding, 18 as book entry, 64 book value net of accumulated, 43-44 with break-even scenario, 74 cash flow due to, 74 in expense accounting 13 historical nature of, 75 as noncash expense, 15, 18 nonrecurring write-downs of assets versus, 19 recovery of cash through, 52 with steady state scenario, 74 dilution ratio, 306 disbursement cycle accounting/financial view of, 312 approval and authorization, 315 controlling, 314-316 creating cash from inventory, 323 float strategies, 322 grading vendors and suppliers, 320-322 improving cash flows, 318-324 invoice verification, 315 JIT payment strategies, 320 leveraging employees, 324-329

managing external creditors, 316-317 negotiating with vendors, 89, 225, 318-319 payment authorization, 316 purchase-order system, 314 qualifying vendors and suppliers, 313-314 recordkeeping, 25-26 separation of duties, 315 for small businesses, 336-337 strategic view of, 312 vendor-provided financing, 324 disclosure balance sheet issues regarding, 43 of capital-raising activities, 209-210 of income statement, 53 NDA (nondisclosure agreement), 317 of terms and conditions, 291 discounts, 98, 290, 296-297 distributions of earnings, owner W-2 wages versus, 232-234 dividends, 21, 68-69, 125, 195 doctoring the numbers, 127-129 DSO (days sales outstanding), 86, 95, 139 dual bottom lines, 182 due diligence, 200, 211

• E •

earnings before income tax, 54 earnings before interest and income tax (EBIT). 54 earnings before interest, tax, depreciation, and amortization (EBITDA), 127 earnings per share (EPS), 53, 115, 124, 205, 207 earnings statement. See income statement economic drivers, critical, 176-177, 179 EFT (electronic funds transfer), 257, 288, 301 electronic payments, 257–258, 286, 288, 302 electronic-based systems, 255-262 eligible receivables, 304-305 embezzlement. See fraud and embezzlement employees allowances versus expense reports, 329 background checks for, 274 commissions and bonuses, 325-326 compensation tied to performance, 326-327 leveraging, 304, 324-329

356

as liquidity sources, 154 managing advances, 87 noncash compensation for, 327-328 staffing companies for, 319 vacations, 276, 329 whistle-blowing by, 273 worker's compensation insurance, 286 environment fees and taxes, 236 equipment. See property, plant, and equipment equity. See owner's equity equity capital accredited investors, 200 from angel investors, 200 on balance sheet, 36 capital stock issues for, 20 capital stock versus retained earnings, 50 cost of, 51, 196, 199 criteria of private sources of capital, 199 - 200debt capital compared to, 205-208 defined, 194, 195 dividends or distributions with, 195 due diligence by investors, 200, 211 equity preference, 195–196 exit strategies for capital sources, 210 from FF&CBAs, 198-199 financial reporting required for, 30-31 from founders, 197 good use of, 204-208 as long-term source. 30 management influence with, 196 for noncash compensation, 327-328 from other private groups, 202-203 from private equity groups, 201-202 public sources of, 203-204 realities of capital markets, 210-211 rules for asset investments, 146-147 seed capital, 197 tips for raising, 209-210 treating sources as partners, 210 from venture capitalists, 201 equity kicker, 203 equity preference, 195-196 equity shareholders. See investors estimated tax payments, 231-232, 264 evading taxes, 29 Example icon, 6 Excel (Microsoft) for budgeting, 174

exception reports, 260 executive summary in business plan, 161 exit strategies for capital sources, 210 expense accounting, 12-13 expense reports, 329 expenses accounting for, 12-13 on balance sheet, 47-49 capitalized start-up costs, 100 cash outflow versus, 17, 18 cash-basis accounting for tax purposes, 228 - 229critical economic drivers, 177 limits on reducing, 55 owner advances as, 100 as percentage of revenue, 14 reduced by electronic cash, 259 relationship of profit or loss to, 11 revenue more important than, 54-55 with cales decline, 75 extending the runway, 182 external capital sources. See debt and debt capital; equity capital external collection efforts, 294–296 external financial reports for creditors, 316-317 income statement for, 53 for investors and lenders, 19-20, 27, 30 - 31projections, 184-185 recordkeeping for, 31 statement of cash flows in, 19-20 for tax authorities, 27

• F •

factoring receivables, 223–224 FDIC (Federal Deposit Insurance Corporation), 251 FF&CBAs (family, friends, and close business associates), 155, 198–199 financial forecasts. *See also* budget accumulating data for, 173–174 Arm forecasting, 186 basic projection model for, 178–180 bottom-up strategy for, 175–176 broadening the use of, 191–192 combination strategy for, 176 357

financial forecasts (continued) detail in, 185 internal versus external, 184-185 key economic drivers for, 176-177, 179 low, medium, and high scenarios, 186 for management discussion, 190-191 as management tools, 183-184, 188-192 operating plan using, 190 overly optimistic, 348-349 quarterly information on, 178 recasting to avoid surprises, 183 rolling, 183-184 for small businesses, 334-335 summary format for, 179 terminology for, 181–182 top-down strategy for, 174–175 variance analysis using, 188–190 what-if analysis using, 185-187 year-end financials in first column, 178 financial reporting to capital sources, 211 defined, 29 exception reports, 260 external, 19-20, 27, 30-31, 53, 184-185 316-317 financial statements for, 29-30 flash reports, 253, 260, 266 fraudulent, 271 identifying accrual accounting in, 32-33 internal, 27, 79, 85, 184-185 to investors and lenders 19-20, 27, 30-31 knowledge presumed in reader of, 45 for lending agreements, 307-308 to managers, 27, 72, 79 for profit-sharing plans, 41 purposes of, 39 to the SEC, 41 to tax authorities, 27 types of reports, 27 unaudited versus audited statements, 85 financial statements. See also specific statements about the examples in this book, 2 availability and distribution of, 40-41 interrelated nature of, 37 need for, 38-39 periodic, for monitoring purposes, 177 primary, 29-30 for privately owned companies, 40-41

as privileged information, 40 for publicly owned companies, 40, 41 for small businesses, 334 standards for. 38 supplemental information for, 30 financial summary in business plan, 163 financing activities. See also debt and debt capital cash flow from, 57, 61, 66-69 defined. 20 on statement of cash flows, 20-21 fixed assets, 43, 52. See also long-term assets flash reports, 253, 260, 266 float, 254, 255, 322 flow-through taxable entities, 229, 230-231, 345 FLV (forced) iquidation value), 92 FOB (free on board), 290-291 forecasting. See financial forecasts founcers, equity capital from, 197 froud and embezzlement. See also internal controls accounting errors versus, 268 balance sheet masking, 44 bank account signers, 251-252, 276 cash-flow analysis uncovering, 115 financial reporting fraud, 271 fraudulent business practices, 270-271 internal controls, 268-270, 272-278 limitations of internal controls, 278-280 policy of absorbing, 279 procedure when discovered, 278 reduced by electronic cash, 259 security measures for preventing, 278 vulnerability to, 268, 269 ways of finding, 279-280 free capital, 51 free cash flow, 126 fume date, 182

• G •

general operating account, 250 gifts of capital, 225 GIGO (garbage-in, garbage-out), 94, 167 gold, payment in, 303 government programs, 223, 225, 226 grading vendors and suppliers, 320–322

grants, 225 Great Plains software, 174 Great Recession as balance-sheet driven, 83 customer credit changed by, 289 deposits, advances, and prepayments in, 299 FLV use in, 92 lessons from, 346-347 liquidity's importance in, 131 gross margins, effect on liquidity, 136-137 gross wages or gross earnings, 25 growth cash-flow scenario, 75-76 liquidity issues with, 147-148, 350 not liquidating assets needed for, 151 sustainable growth rate, 182

• H •

haircut, 321 hiding internal controls, 277 high forecast scenario, 186 *How to Read a Financial Report* (Tracy), 114, 271

•1•

icons in book margins, explained, 5-6 immaterial assets, 88 income statement benchmarks with balance sheet, 52 cash flow not shown on, 9, 14-16 defined, 30 disclosure of, 53 for external financial reports, 53 as focus before recent downturn, 83 importance of revenue on, 54-55 interest expenses on, 21 interrelation with other statements, 37 other names for, 9, 14, 30 profit or loss revealed by, 37 rounding of balances on, 52 statement of cash flows numbers versus, 16 - 18income tax payable, 65, 117 ineligible receivables, 304-305 insurance, 251, 286, 324 intellectual property, 88, 151

interest expenses, 18, 21 internal auditing, 280 internal collection efforts, 292-294 internal controls. See also fraud and embezzlement for accounting reliability, 269-270 antifraud purpose of, 270 audit trails, 273-274 checklist for, 272-276 computer controls, 275 cost effectiveness of, 277, 279 curbing indifference to, 275 defined, 268-269 to deter and detect, 269 employee background checks, 274 employee whistle-blowing, 273 fraudulent business practices, 270-271 hiding, 27for high risk areas, 272 importance of implementing, 268 job sharing, 276 key asset appraisal, 274–275 legal implications of, 276–277 limitations of, 278-280 limiting access to records, 274 periodic review of, 274 procedure after fraud discovery, 278 required for CPA audits, 271 separation of duties, 273, 276, 315 for small businesses, 275-276 surprise audits, 273 internal financial reports, 27, 79, 85, 184-185 inventory appropriate levels of, 86-87 on balance sheet, 34, 48, 86-87 converting to cash, 110-111 creating cash from, 323 days costs of goods sold outstanding in, 96 decrease in statement of cash flows, 63 defined, 26 described, 35 excessive, problems from, 144-145 in expense accounting, 12 IRS requirements for accounting, 28 LCM value for, 98 liquidating, 63, 150 liquidity issues for, 144–145 NSTOP figured using, 117 obsolescent, 342-343

Cash Flow For Dummies

inventory (continued) recordkeeping for, 26 with sales growth or decline, 75, 76 scrubbing (case study), 104 subcomponents of, 86 valuing correctly, 98–99 investing. See also equity capital bank account for, 250 in cash, 51-52 defined, 20, 57 rules for asset investments, 146-147 in soft assets, 343-344 on statement of cash flows, 20, 57, 61 types of, 66 investors accredited, 200 angel investors, 200 due diligence by, 200, 211 financial reports for, 19-20, 27, 30-31 financial statements needed for, 39 management influence of, 196 other private groups, 202-203 private, criteria of, 199-200 private equity groups, 201–202 venture capitalists, 201 invoices, 291-292, 305, 315 IRS

financial reports for, 27 requirements of, 27, 28, 32, 33–34, 228 safe harbor rules, 232

•] •

Jargon Alert icon, 6 JIT (just in time) payment strategies, 320 job sharing for internal control, 276

• K •

Key Concept icon, 5 key economic drivers, 176–177, 179 KISS principle for business plan, 169 Koo, Richard (financial expert), 83

• [•

LCM (lower of cost or market) value, 98 leases, 152–153, 221–223, 324. *See also* liabilities lenders. See also banks asset-based, 220-221 available, 244-245, 246 financial reports for, 19-20, 27, 30-31 financial statements required by, 39 as liquidity sources, 152-153 need and availability of, 93 lending agreements advance rates for, 305-306 CART invoices for, 306 concentration of receivables affecting, 305 covenants, 216, 307 cross-aging factor, 306-307 dilution ratio, 306 eligible receivables for, 304–305 getting competitive fees and bids, 309 hidden fees and charges, 308-310 proactive management of, 309–310 reporting requirements, 307-308 restrictions on borrowing, 308 leverage, defined, 50 leveraging. See also debt and debt capital; equity capital assets, 151-152 employees, 304, 324-329 equity versus debt capital for, 205, 207 the float, 255, 322 liabilities, 111-112 to manage seasonality, 303-304 payment terms, 290 professional counsel for, 151 pros and cons of, 155-156, 237 unsecured creditors, 225 vendors and suppliers, 304, 337 liabilities. See also debt and debt capital in accrual accounting, 33 on balance sheet, 34, 84, 89-91 cash flow effect of changes, 63 changes in statement of cash flows, 69-72 current, 85, 101-102, 214 evaluating, 100-102 leveraging, 111-112 off-balance-sheet, 102 offsetting, avoiding, 44 properly accounting and accruing, 101 ratios to assets, 95 as real accounts, 38 recognizing earned revenue, 102 scrubbing (case study), 104-106

line of credit, 90, 136, 146 liquidity available cash versus, 133, 142 defined, 131, 133 example illustrating, 136–137 growth leading to issues, 147-148, 350 importance during recession, 346 importance of, 131 liquidating assets, 149-151 liquidating inventory, 63, 150 measuring, 133, 136-137, 140-142 of public sources of capital, 204 solvency versus, 131, 133-137 sources of, 152-154, 225 traps to avoid, 143-149 liquidity availability analysis, 140 loans. See debt and debt capital lockboxes, 254, 255, 300 long-term assets on balance sheet, 84, 88 book value of, 43 cash flow and purchase of, 111 cash recovery through depreciation, 52 defined, 84 as fixed assets, 43 as investing activities, 20 long-term debt on balance sheet, 85, 90 classification of, 101-102 current portion of, 90 defined, 85, 214 moving line of credit borrowings to, 90 on statement of cash flows, 67-68 loss. See also fraud and embezzlement defined, 11 on income statement, 14 income statement showing, 37 negative cash flow due to, 126 noncash expenses, 74 for year, in retained earnings, 36 low forecast scenario, 186 lower of cost or market (LCM) value, 98

• M •

management accounting, 26–27 management exposure, 204 management influence, 196 management integrity and credibility, 191 management of earnings, 127–129 market assessment in business plan, 161–162, 163 market conditions, changing, 347–348 market stability, cash needs and, 247–248 massaging the numbers, 127–129 material assets, 88 MDA (management discussion and analysis), 190–191 MDOR (management discussion of operating results), 190–191 medium forecast scenario, 186 Microsoft Excel for budgeting, 174

• N •

NDA (nondisclosure agreement), 317 negative cash flow, 73, 76–77, 126 net income adjustments to arrive at cash flow, 62-65 as bottom line, 59 cash flow as ratio to, 125 cash flow from operating activities versus, 57, 61 on income statement, 54 return on investment measure using, 52 net short-term operating position (NSTOP), 116-121, 124-125 net 30, 290, 296-297, 324 net working capital, 95, 119, 139 net worth, 47 netting, 117-118 nexus, 236-237 noncash expenses amortization on intangible assets, 74 depreciation as, 15, 18, 74 employee compensation, 327-328 losses, 74 nondisclosure agreement (NDA), 317 nonroutine cash flows, 244 notes payable, 105, 112, 153

• () •

obsolescent inventory, 342–343 offsetting, 44 operating activities alternative method of reporting, 21 bank account for, 250

Cash Flow For Dummies

operating activities (continued) cash flow from, 56-57, 61, 62-66 defined, 21 multiple operating plans, 346-347 on statement of cash flows, 21 operating conditions, cash needs and, 247-248 operating margin, measuring, 54 operating plan, 190 operational overview in business plan, 162-163 operations expenses, cash outflow versus, 17 owner advances, 100 owner's equity. See also equity capital on balance sheet, 36, 85 capital stock, 50, 67-68 cash flow from financing activities, 67-69 changes in statement of cash flows, 69-72 debt-to-equity ratio, 96, 139, 205 defined, 20, 30 justifying use of, 51 owner advances against, 100 as real account, 38 retained earnings, 36, 50, 68-69 return on investment measure using, 52 scrubbing (case study), 104-106 owner's equity shareholders. See investors owners, financing by, 154-155

• p •

P&L report. See income statement partnerships, capital from, 225 password protection, 260 past-due accounts and collection, 292-296 PayPal, 288 payroll, 25, 29, 250 PEGs (private equity groups), 201–202 performance-measurement tools available current working capital, 140 for balance sheet evaluation, 93-96 benchmarks, 52, 265-266 cash as key indicator, 262-266 cash burn rate, 76-77, 126, 140 current ratio, 95, 139 day sales outstanding, 86, 95 days costs of goods sold outstanding in inventory, 96, 139 days sales outstanding, 139

debt service coverage ratio, 139 debt-to-equity ratio, 96 liquidity availability analysis, 140 liquidity measurements, 140-141 net working capital, 95, 139 quick or acid-test ratio, 95, 139 return on investment, 52 solvency measurements, 139 using after scrubbing, 106–108 personal guarantees for debt, 216, 219-220, 288-289 phantom equity, 328 plant. See property, plant, and equipment positive pay, 260-261 PP&E. See property plant, and equipment preferred stock, 195 prepaid debit cards, 261, 301 prepaid expenses, 35, 48, 63-64, 87, 117 prepayment by customers, 299-300 price increases, 177 price earnings ratio, 124–125 prority creditors, 216 private equity groups (PEGs), 201–202 private sources of capital, 199–203, 210, 211 privately owned companies, 40-41, 128 privileged information, 40 procurement, recordkeeping for, 26 profit cash flow from, 11, 15-18 cash flow versus, 16-17, 55, 333 changes in financial condition from making, 119-121 defined, 11 dividends from, 21 on income statement, 14 income statement showing, 37 as percentage of revenue, 14 statement of cash flows not showing, 22 for year, in retained earnings, 36 profit and loss statement. See income statement profit-sharing plans, 41 projections. See financial forecasts property, plant, and equipment (PP&E) accumulated depreciation deducted from. 43 on balance sheet, 43-44, 48-49, 52, 88 balance sheet reporting of, 43-44 book value of assets, 43

cash flow from investing activities, 61, 66 cash-basis accounting for items, 34 contra account for, 43 cost of land (nondepreciable) in, 43 described, 35, 88 leasing as capital source, 221–223 liquidating, 150 liquidity affected by, 145 recordkeeping for, 26 scrubbing (case study), 104 valuing correctly, 99 property taxes, 236 public sources of capital, 203–204 publicly owned companies, 40, 41, 53 purchase-order system, 314

• Q •

qualifying customers, 284–286 vendors and suppliers, 313–314 quick or acid-test ratio, 95, 139 QuickBooks software, 174

• *R* •

raising capital. See debt and debt capital; equity capital ratios. See also performance-measurement tools cash flow to net income, 125 current, 95, 139 debt service coverage, 139 debt-to-equity, 96, 139, 205 dilution, 306 performance measurement, 95, 96 price-earnings ratio, 124 quick or acid-test, 95, 139 solvency measurement, 133, 136, 139 real accounts, 38 real estate, leveraging, 151 recasting, 183 recessions, drivers for, 83. See also Great Recession recordkeeping, 23, 25-26, 31 references of customers, 287 regular taxable entities, 230-231 Remember icon, 5 reputation risk with customers, 285

restricted cash accounts, 250 retained earnings, 36, 50, 68-69 return on investment, 52, 205, 207 revenue accounting for, 11–12 accounts receivable for, 36 assets compared against, 52 on balance sheet, 47-49 book versus tax income, 191 cash flow effect of changes, 75-76 cash inflow versus, 17 cash-basis accounting for tax purposes, 228-229 critical economic drivers, 177 decline, liquidity issues with, 148-149 expenses as percentage of, 14 growth, liquidity issues with, 147–148 IRS requirements for accounting, 28 momentum, cash flow compared to, 121 123 more important than expenses, 54-55potential increase as limitless, 55 profit as percentage of, 14 relationship of profit or loss to, 11 requirements for private capital, 199 skimming (tax evasion), 29 taxable income trap, 344-345 as top line, 59 revenue and expense accounting, 11–13, 32 risk balancing reward with, 210 with debt capital, 205, 207 with discounts, 296-297 with equipment leases, 222 with equity kickers, 203 of fraud, 268, 269 internal controls for high-risk areas, 272 managing capital risks, 205 with private sources of capital, 200, 201, 203 reputation, with customers, 285 returns on, 199 for unsecured creditors, 215 rolling forecasts, 183-184 routine cash flows, 244

• 5 •

safe harbor rules, 232 sale lease-back of assets, 152–153

sales revenue. See revenue sales skimming (tax evasion), 29 sales taxes, 236 sales-driven budgets, 184-185 SALT (state and local taxation), 235-237, 264 SBA (Small Business Administration), 223 scientific wild-ass guess (SWAG), 164 scrubbing the balance sheet, 103-110 seasonality, 263-265, 303-304 secondary repayment sources. 219-220 Securities and Exchange Commission (SEC), 41 security interest or position, 215 security measures, 278 seed capital, 197 selling cycle accounting/financial view of, 282 alternative forms of payment, 300-303 CART invoices, 291-292, 305 cash generated from, 281 as consumer of cash, 283-284 creative payment terms, 297-298 credit review and approval, 286-289 deposits, advances, and prepayments. 299-300 discounts, 290, 296-297 importance of managing, 281 improving cash flows, 296-304 lending agreement management in, 304-310 past-due accounts and collection, 292-296 qualifying the customer, 284–286 seasonality in, 303-304 setting customer terms and conditions, 289-291 for small businesses, 336 strategic view of, 282-283 separation of duties, 273, 276, 315 shareholders. See investors shocks to cash resources, 244 signers for bank accounts, 251-252, 276 silver, payment in, 303 Small Business Administration (SBA), 223 Small Business Financial Management Kit For Dummies (Tracy and Tracy), 47, 79, 156

small businesses accounting adjustments in, 349 accrual accounting for, 24 balance sheet for. 338 CART information for, 340 cash-basis accounting use in, 24, 32 cash-flow management in, 333-340 creative cash generation for, 337-338 disbursement cycle for, 336-337 financial statements for, 334 focus on capital and cash, 335 internal controls for, 275-276 planning and forecasting for, 334-335 protecting cash in, 339-340 selling cycle for, 336 statement of cash flows for, 77-78 soft assets, 343-344 software for budgeting, 174 solvency cash component of, 142 defined, 133 example illustrating, 134–136 liquidity versus, 131, 133–137 measuring, 133, 136, 137-139 staffing companies, employees from, 319 staggering cash flow, 265 start-up phases capitalized start-up costs, 100 negative cash flow in, 76-77 normal cash balance for, 245-246, 248 state and local taxation (SALT), 235-237, 264 state lending programs, 223 statement of cash flows accounts payable decrease, 64-65 accounts receivable increase, 62 accrued expenses payable increase, 65 accumulated depreciation increase, 64 basic example, 60 business valuation tied to, 79 cash flow from financing activities on, 57, 61, 66-69 cash flow from investing activities on, 57.61.66 cash flow from operating activities on, 56-57, 61, 62-66 change in cash on, 21-22

changes in assets, liabilities, and owner's equity on, 69-72 comparing with balance sheet, 70-72 defined. 30 in external financial reports, 19-20 financial condition indicated by, 69-70 financing activities on, 20-21 importance of, 59, 83 income statement numbers versus, 16-18 income tax payable increase, 65 information shown by, 37 interrelation with other statements, 37 inventories decrease, 63 investing activities on, 20 mandate in reports, 55, 59 massaging the numbers, 127-129 with negative cash flow, 73, 76-77 not reconciled with balance sheet, 78-79 number of lines on, 78 operating activities on, 21 prepaid expenses increase, 63-64 profit not knowable from, 22 purposes of, 55, 69 redesigning for internal reports, 79 rounding of balances on, 55 with sales growth or decline, 75-76 for small businesses, 77-78 with steady state scenario, 73-74 strategies and policies not shown by, 78 timing and frequency of 72statement of financial condition or position. See balance sheet statement of operations. See income statement steady state cash-flow scenarios, 73-74 stop payments, 254 subchapter S corporations, 229, 230-231 subordinated debt, 224 subordination agreements with debt, 216 subsequent events, 47 suppliers. See vendors and suppliers surprise audits, 273 sustainable growth rate, 182 Sutton, Willie (bank robber), 267 SWAG (scientific wild-ass guess), 164

sweat equity, 197

sweep accounts, 255 SWOT analysis for business plan, 167–169

• 7 •

taxes accelerated deductions, 235 accounting for compliance, 28 basing economic decisions on, 227 book versus tax income, 191 cash flow impacted by, 264 complying with requirements, 227, 236 deferring obligations, 104, 227 estimated payments, 231-232, 264 evading, 29 financial reports for authorities, 27 financial statements for returns, 39 flow-through taxable entities, 229, 230 231, 345 income tax payable increase, 65 managing to improve cash flow, 226-235 owner W-2 wages versus distributions of earnings, 232-234 professional counsel for, 227 recordkeeping for, 25 regular taxable entities, 230-231 reporting income on cash basis, 228-229 specialized incentives, 235 state and local (SALT), 235-237, 264 structuring the business for, 229-231 tax credits, 234 taxable income trap, 344-345 Technical Stuff icon, 5 terms and conditions creative payment terms, 297-298 for customers, 289-291, 292 disclosure of, 291 expected payment terms, 101 for government programs, 226 negotiating with vendors, 89, 225, 318-319 vendor, liquidity affected by, 136 third-party information in business plan, 169-171 Tip icon, 5 top line, 59 top-down forecasting strategy, 174-175

Cash Flow For Dummies

top-line approach, 326–327 Tracy, John A. Accounting For Dummies, 11 How to Read a Financial Report, 114, 271 Small Business Financial Management Kit For Dummies, 47, 79, 156 Tracy, Tage C. (Small Business Financial Management Kit For Dummies), 47, 79, 156 trade payables. See accounts payable trade receivables. See accounts receivable trades, 302 treasurer, 25

• 11 •

unaudited financial statements, 85 unsecured creditors, 215, 225 use taxes, 236

• 1/ •

vacations, 276, 329 variance analysis, 188–190 VCs (venture capitalists), 201 vendors and suppliers financing provided by, 324 float strategies with, 322 grading, 320–322 JIT payment strategies for, 320 leveraging, 304, 337 liquidity affected by terms, 136 as liquidity sources, 154 negotiating terms, 89, 225, 318–319 qualifying, 313–314 resources for references on, 313 sample or trial runs from, 313 as unsecured creditors, 215, 225 using multiple like suppliers, 319 venture capitalists (VCs), 201

• W•

WAG (wild-ass guess), 164 Warning! icon, 6 what-if analyzis, 186–187 window dressing, 128 wire funds transfer, 257, 301 worker's compensation insurance, 286 World Gold Council, 170 write-downs, 19, 137 W-2 wages for owners, distributions versus, 232–234

• Z •

ZBAs (zero balance accounts), 255 zero cash balance, 10