

Dressing Up Your Financial Statements - by Dan Sautner

There are times when you have to provide financial information to outside parties. Generally speaking, you will only do this when you have no choice (i.e., the government) or when you want something.

In the case of government reporting we suggest the minimum. As with all contact with the government, give them what they can legally ask for and ignore the rest. This is a perfect example of not "gilding the lily." Too much information is worse than too little information.

The other times you provide information, you are trying get something. You may be trying to establish new or additional lines of credit, enticing new ownership contributions or simply showing that you are capable of handling a lease commitment. In each of these cases you want the party reading these financial statements to be as impressed as possible. This article suggests some ideas that you can adopt.

Currently your monthly information should have mostly management value. You need information to run a better business. You need the details of each area of importance. In the case of new projects you want to be able to determine the financial impact, so you may need more information. All of these "details" are important in the use of your financial statements. The details in this format are not necessarily good for you when you want to impress other people.

There are two main statements that you need to concern yourself with. The first is the income statement. Here you show the revenues and expenses of your operation. Second is the balance sheet, where you show the assets of the company along with what the company owes outside parties. Finally, this statement will show how much the ownership has in the company. First we shall deal with income statements.

INCOME STATEMENTS

Reduce Details

First and foremost, reduce the detail in your information. As much as possible, consolidate the operating or income statement. The key numbers here are sales, gross profit, inventory, wages, rents and other operating-type numbers. There is no need, for instance, to separate all of the different levels of payroll such as ownership and management. These numbers can be provided separately, if needed. Another example is to reduce the number of lines of sales. Consolidate this to one line. You want to show that you have a viable operation, not to invite comment on a sideline sales category.

Separate Core Activities

In the above paragraph it's suggested that you consolidate wherever possible, but sometimes you'll need to separate items. The point here is that few businesses work on one idea at a time. They often mix different activities into the same operation. Examples of this include sub-leasing, renting signs,

wholesale activity and sideline activities. When these are combined with the core activity of, say, a hair salon, you hide the true operational results of the main business. The other readers are not interested in these sidelines -they are interested in the manner in which you make your money. Sometimes these little adventures cost us money, or are still in the development stages. This being the case, they are making the core business look bad when, in fact, it is doing well enough to support these outside activities. You need to show the reader of the income statement how well you are doing with the main business and how much it contributes to bottom-line expenses. You can show these other activities below the line called income from operations.

Use Comparative Information

Many readers are trying to determine the trends in your business. Show growth rates and management accomplishments. Commonly, companies show the prior year in their statements. There is nothing wrong with the consolidation of a number of years on one page. Here you can see how the company has grown and the cost controlling measures that you may have put in. It is impressive to see sales increasing by ten percent and expenses only by eight percent.

BALANCE SHEETS

Not all of the same rules apply for the balance sheet. Here some additional detail can be useful, but do not try to overwhelm the reader with too many details.

Detailing

Make sure you show the various assets you actually have. Show the key current items such as inventory, accounts receivable and cash. This will show your reader how liquid you are. Show your payables split among remittances required by governments and those to outside trade suppliers. If any money is due to the principals of the company, show these separately.

Reduce details in the fixed asset area to the main categories of land, building, equipment and leasehold improvements. Group all of the accumulated depreciation and amortization together.

The reader should be able to easily extract how much you own and the general categories in to which it falls. They should be able to see how much you owe to outsiders and what type of outsiders they are, and finally they should be easily able to determine how much you have in the business.

In the balance sheet there is a delicate line of too much information and too little. Help the reader understand where your business is without trying to show them where every piece of stock is located.

Some Don'ts

It is tempting to inflate sales and income to impress someone. Never do this. First, the numbers will stop making sense to a skilled reader, and second, by exaggerating, you might be opening yourself

up to litigation, possibly even jail time. Certainly you are permanently losing all credibility with your reader. Avoid this at all costs.

Next, while non-cash expenses such as depreciation is tempting to exclude (after all, it does not result in cash,) resist it. A skilled reader knows it should be there, and in its absence, will make assumptions that are not in your favor.

Resist the transfer of expenses from the income statement to the balance sheet. There are accounting rules with respect to what expenses can be capitalized, but readers on the whole are looking for the "hard" assets. Certainly set up a legitimate prepaid expense (where the value of the expense extends into future periods,) but do not over do it. Readers catch on.

Conclusion

A skilled accountant can easily prepare these statements for you, but that does not change your involvement. Read your own statements and see if they are telling the story you want told.