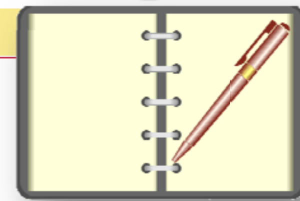


Balance Sheets

So, now that you understand the key terms associated with your P&L, it's time to learn about your balance sheet. This statement reports the amount of your assets, liabilities, and capital (equity) in the business at a given point in time.

The fundamental math of a balance sheet is: Assets = Liabilities + Equity.

Your balance sheet shows your assets in the business (cash, inventory, etc.) versus how they are funded—through debt, like accounts payable (money you owe someone) or through vendor credit, loans, shareholder investment, or retained earnings.

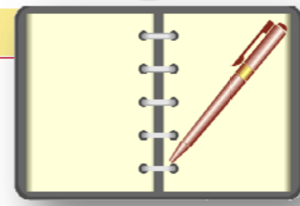
Before we go deeper into illustrating a balance sheet with our lemonade stand example, there are some definitions you need to know:

- ✓ **Current asset:** Asset in a business that can be converted to cash in one year or less. These include cash, inventory, accounts receivable, and prepaid expenses.
- ✓ **Fixed asset:** Tangible asset such as facility improvements, equipment, and land, which is intended for long-term use. (These won't be converted to cash within a normal year.)
- ✓ **Intangible asset:** Things that have value for your company, but that you cannot touch, such as your reputation, patents, and goodwill.
- ✓ **Current liabilities:** Obligations of the business due within one year. These include accounts payable to suppliers, accrued expenses and taxes, and the portion of long-term debt that is due in the next 12 months.
- ✓ **Long-term debt:** Obligations of the business that are not due for at least one year.
- ✓ **Stockholders' equity:** The amount invested by stockholders, plus the accumulated profit of the business. Includes retained earnings, paid in capital, and stock.

Let's move on to our lemonade stand. A balance sheet is presented below. It reflects the results from the income statement (P&L) plus a few other numbers, such as how the business was funded and what assets were purchased to support the business.

Let's start with inventory. On my first day of business I bought some supplies in bulk to achieve lower costs. We will assume for our example that I bought what I project to be sales of 10 cups per day, for seven days' worth of nonperishable supplies such as cups ($0. 50) and sugar ($0.25), at a total cost of $5.25 ($0.25 + $0.50 = $0.75 times 7 = $5.25). I also purchased one of my perishables (lemons at $0.50 and ice at $0.75 for a total of $1.25). I would record $6.50 ($5.25 + $1.25) for these purchases into the inventory account. I would then deduct the cost of goods sold from the inventory account each day based on the amount used (assuming you use an equal amount each day, you would deduct $2 each day, as discussed earlier (see line 2 on balance sheet below).

My supplier of nonperishable items gives me credit terms for my purchases, with the $5.25 cost resulting in an accounts-payable to that vendor (line 4 below), to be paid in 30 days. My perishables vendor requires cash on delivery, so I must pay for those purchases ($1.25) right away in cash. I also negotiated credit terms from my supply vendor on the $3 marketing costs (line 4 below), which is recorded in accounts payable as well.



Next, taxes are due on my income (I pay them quarterly). As a result, I will record (or “accrue,” in accounting lingo) the tax liability in an accrued taxes payable account on the balance sheet.

Lastly, my profit (what is left after paying my liabilities in line 6 from my assets in line 3) is recorded in the retained earnings account in the equity section of the balance sheet (line 7 below).

Note on taxes: If you sell to consumers, you must collect and remit sales taxes. You will have federal and state tax on your income. Although some states don’t have income tax, some cities and school districts do. Check with your local tax advisor.

Balance Sheet

As of January 1, 2007

Assets	
Current Assets	
(1) Cash	$8.75 ($1.25 of my original $10 was spent on perishable supplies)
(2) Inventory	$4.50 ($6.50 of purchases from vendors less $2 cost of goods sold)
(3) Total Assets	$13.25
Liabilities	
(4) Accounts Payable	$8.25 ($5.25 of supplies and $3 marketing)
(5) Accrued Taxes	$0.75
(6) Total Liabilities	$9.00
Equity	
(7) Retained Earnings	$4.25
(8) Total Liabilities and Equity	$13.25 (Liabilities $9 + Equity $4.25 = Assets $13.25)