September 2022

Introduction - Business Finance Essentials

By James Allen

Abstract

Learn the basics of managing finances for your business, including start-up costs, budgeting and record keeping.

Getting Started

Understanding key finance and accounting concepts and language is critical for managers and professionals at every level. This practical and engaging pdf will help you understand the essentials of finance to interpret financial reports and make more informed business decisions.

<u>SET UP YOUR FINANCES</u>

I. Plan your business finances

Setting up and managing finances is essential to the success of your small business. You can learn about basic financial processes, planning for good financial management and discover what financial policies you need to be aware of.

Basic financial requirements

Start-up costs

- Work out how much it will cost to set up your business. It is better to overestimate than underestimate.
- Plan how you will fund your business.
- Research other businesses to understand your potential costs by benchmarking your business.

Pricing for products and services

- Research your competitors to find out what they are charging for similar products or services.
- Review competitors' websites and online promotions.
- Learn more about what to charge for your products or services.

Income and profit

- Calculate key figures such as break-even point, gross profit and net profit. This will help you estimate the level of sales you need to cover costs and make a profit.
- Know your potential profitability.
- If you need to borrow money, develop a business plan for your lenders or investors, and a cash flow projection. There will also be lending criteria to follow.
- Estimate how long your business can survive without making a profit. Consider factors such as interest rates and your ability to borrow more money.
- Develop a budget to manage your money until your business starts earning income.
- Engage an accountant or financial adviser to help you prepare cash flow forecasts and develop record-keeping processes.
- Find out about your tax obligations.

Managing your own finances

You can learn basic skills as a small business owner to give you confidence to manage your own finances. These skills will help you:

- understand accounting basics
- be confident in financial terms
- interpret financial statements
- identify how cash flows through a business
- understand cost of goods sold
- use financial information to make business decisions.

Skills such as budgeting, calculating taxes, setting price points and setting revenue and success rates will give you control over your own financial decisions.

Create a budget

Putting together a budget can be as simple as creating a spreadsheet. At the end of every month, compare your actual spending to your budget. If it doesn't match, review where your money was spent and make adjustments for next month.

Understand your expenses

Expenses are things you have to pay for to run your business, such as overheads (e.g. rent, electricity) and employee salaries.

Understanding your expenses can save you money when applying for a loan or negotiating deals with suppliers.

Understand your cash flow

Cash flow is how money moves in and out of your business. You can track your cash flow on a simple spreadsheet or in your accounting software. Small businesses starting out may have dramatic changes in income and expenses each month.

Record every purchase, withdrawal, cost and sale in your spreadsheet or accounting software. This will help you understand:

- where your money is going
- your highest expenses
- your most profitable products
- high revenue months or periods
- what an average month looks like.

Borrowing money

Before borrowing money, compare terms, interest and fees from multiple lenders using an online comparison service or a broker. Read the fine print and understand the loan's limitations and requirements.

Improve your financial knowledge

Grow your financial knowledge to help you better understand how to run your business. You could:

- review and research business books and online resources
- subscribe to finance newspapers, magazines, newsletter and blogs
- listen to business podcasts
- attend business events, including workshops and webinars
- consider enrolling in further training, including vocational education and training or tertiary education
- participate in financial education programs, events or webinars offered by business associations (such as the Chamber of Commerce and Industry in Queensland) or professional bodies (such as CPA Australia).

Financial policies and procedures

Financial policies set out the 'rules' for how you will manage your business's finances. They should reflect the core values and culture of your business.

Clear financial policies and procedures will ensure:

- staff are aware of their obligations
- financial decisions are consistent and reliable
- client or employee disputes are less likely
- professional operating standards are in place.

Types of financial policies and procedures

Your policies and procedures will depend on the nature of your business. Think about your preferences for:

- who you will authorise to complete specific tasks
- cash handling and managing your business's day-to-day finances, such as petty cash and invoicing
- how you will choose and work with new suppliers

- buying and purchasing processes such as stocktake and purchase orders
- overdue invoices or accounts payable (creditors)
- sales and accounts receivable (debtors)
- engaging and managing customers or clients
- processing wages, sick leave and overtime
- business insurance and risk management.

Creating financial policies

Financial policies should:

- align with your business plan and goals
- reflect the values and the culture of your business
- explain why policies have been put in place
- be easily understood by everyone in your business.

Creating financial procedures

Financial procedures set out clear instructions under a policy and should:

- be factual, informative and detailed
- be presented simply using clear instructions and visual supports such as flow charts, images and checklists
- include references and links to forms.

When writing your financial policies and procedures:

- highlight your objectives
- involve your employees in the decisions
- write and review each day, or as you complete tasks, to keep manageable.

II. Costs to start and run your business

Learn about common start-up costs and how to determine these costs for your business.

Understand start-up costs

Knowing your start-up costs and creating a realistic budget in the early stages of starting a business is key to starting in the right way. One of the most common reasons a new business will fail is not having enough money to cover expenses, especially in the first 6–12 months. You are more likely to succeed if you plan for expenses early on.

Pay close attention to your initial costs such as fixtures, equipment, office supplies, leasing/tenancy bonds, insurance and accounting or legal fees. Consider including a safety buffer of 10% when calculating your costs.

Common start-up costs

Some of the costs associated with starting a business include:

- market research
- preliminary financial advice or general business advice
- compliance expenses such as the cost of any licences or registrations required
- tenancy or leasing bond, transfer (stamp) duty and lease agreement advice
- telephone and internet
- insurance
- power connection and bond
- marketing and website development
- equipment, fixtures and fittings
- staffing and wages
- initial materials and stock purchases.

Your exact start-up costs will depend on your type of business and industry. For example, a bakery will need to own or lease a shop, while an online business will have website set-up costs.

How to calculate your start-up costs

Check financial statements

Look up financial statements of publicly listed businesses in your industry, especially competitors and market leaders.

Compare businesses that are a similar size to yours. Remember that larger businesses will often have the advantage of stronger buying power. That means they will be able to negotiate lower prices for goods because they can buy more of them.

Talk to industry associations and networks

Before you start:

- talk to other businesses
- join industry associations
- visit websites designed for new business owners and entrepreneurs
- seek advice from mentors or financial advisers.

Calculate ongoing and one-off costs

Consider any ongoing costs that recur annually, weekly, monthly, quarterly or every couple of years. For example, your rent and power are ongoing costs.

You also need to budget for one-off costs (e.g. your tenancy bond).

Get support and advice

Get support for your new business by:

- applying for government grants, tax incentives for early stage investors and for research and development
- visiting Australian Business Licence and Information Service (ABLIS) for licences, regulations, approvals and compliance advice
- using the Business Launchpad for licences, permits and regulatory information in your local government area
- attending business events and seminars in your local area
- watching our free business webinars
- speaking to an accountant or financial adviser.

Set realistic expectations

Consider how long it will take to open your business and start making a profit. Set realistic expectations and have a contingency plan if this changes. Make sure your business goals are achievable and your budget aligns with your goals.

For example, a new social media business may set:

- a realistic goal to break-even for the first 2 years before achieving profitability in year 3
- an unrealistic goal to have more customers than Facebook in 3 years.

Overestimate costs

It's better to overestimate then underestimate costs. Experts recommend adding 10% on top of your total costs as a safety buffer.

III. Working with accountants and financial advisers

An accountant or financial adviser can manage a range of financial activities for your business. Learn about what to look for and the key questions to ask for when engaging a professional to help you with your tax and financial requirements.

An accountant can give you advice about:

- starting, buying, growing or ending a business

- tax, including goods and services tax (GST) and business activity statements (BAS)
- reporting obligations
- income, deductions and concessions
- obligations to employees (including PAYG and superannuation)
- managing records.

When to engage an accountant

Accountants can support you and your business and guide you to make the right financial decisions.

Consider contacting an accountant:

- before you start, buy or sell a business
- before you buy or change property, plant or other assets
- to plan before the end of financial year (between January and June 30 each year) if you're planning to grow your business
- if you have concerns with creditors, debtors, finance, expenses or stock.

Aim to speak with your accountant at least every quarter or when the BAS is due.

If you're not sure if you can afford the services of an accountant, consider how long it would take you to complete each step without their help or advice, and the quality of success you will achieve on your own. You may find that you only need a couple of hours of their time.

Questions to ask a potential accountant or financial adviser

a. **What are your qualifications?**
- Confirm their specific accounting qualifications.
- Ask if they are a certified or chartered accountant.
- Check if they are a member of an accounting body.

b. **How long have you been practising?**
- Ask how long they have been a practising accountant (if they haven't practised in many years you may wish to go with someone with more up-to-date experience).
- Check how long their business has been operating or how long they have been with the business. Choosing an established accountant or firm may be more reliable than one which has just started.

c. **Who is your typical client?**

- Find out who their clients are, and what type of client needs they have experience dealing with.
- Ask for client referrals so you can talk to a current or previous client.

d. What is the scope of your services?

- Ask about the scope of their services, so you can decide if 1 accountant can handle all of your needs (e.g. if you need broad business advice which not only covers tax, but also business and strategic planning, budgeting, and cash flow).
- Review if they can provide advice on management accounting (e.g. can they help you set up a chart of accounts or a management reporting framework).

e. Who will be my main point of contact?

If you are hiring an accounting firm, ask if you will have 1 accountant dedicated to handling your business, or if you'll be dealing with multiple contacts. It's often far more streamlined, and easier for you to develop trust with your accountant, if you have the same person managing your accounts, rather than your finances being passed through multiple people.

f. How can you save my business money?

- Find out if they are proactive about saving your business money, rather than simply filing your paperwork and doing the bare minimum.

g. How much notice do you need and how long will you take to complete work?

- Find an accountant who you can rely on to communicate effectively, and complete work promptly within your timeframes.

h. What accounting software are you familiar with?

- Ask if they know how to use the accounting software your business uses.
- If they're not familiar with your systems, ask them how information should be shared.

i. What is your preferred way to communicate?

- Check if they prefer to communicate through email, mail, or phone.

j. How do you handle billing?

- Find out what their fees and charges are, and what their fee structure is (e.g. monthly retainer, charge by the hour).
- Ask what you'll be billed for (e.g. if you're charged for every email they open, every phone call they make, or for travelling time).

- Check how you can make payments (cash, cheque, credit card, online banking). Don't be afraid to negotiate on any of these points.

IV. Business tax requirements

Managing your tax affairs and obligations is an integral part of your business, particularly if you have employees. Your business's tax requirements will vary according to the type of business you run, the number of employees you have and the legal structure of your business. Tax is a complex area. Outsourcing your tax to a professional or employing an experienced accountant can help you to avoid legal and financial problems.

Tax basics

- You will need to register your business for tax—there are different types of tax which you may need to pay.
- You may need to pay tax to the Australian Taxation Office (ATO), or Queensland Revenue Office (QRO).
- You will need to lodge business activity statements (BAS).
- You will need to lodge an income tax return each year.
- You must keep good records for tax purposes.
- You may be able to reduce the amount of tax you pay through deductions.

Help with your tax

You may be tempted to manage your business's tax yourself to keep costs down, but this can be risky. Outsourcing your tax to a professional or employing an accountant can help things run smoothly, and possibly save you money (and potential financial penalties) in the long run.

They can explain tax considerations such as:

- legal structure and the need for a tax file number (for businesses other than sole traders)
- Australian business number (ABN)
- goods and services tax (GST)
- business activity stream (BAS)
- pay as you go (PAYG)—withholding and instalments
- superannuation
- fringe benefits tax (FBT)
- payroll tax.

Taxes if you employ people

As an employer, you must be aware of your tax obligations when paying staff, including PAYG withholding tax and superannuation. Depending on the size of your business, you may also need to pay payroll tax.

The ATO provides tax information for employers about paying staff, including:

- tax rates
- paying superannuation
- employee termination payments
- redundancy pay
- paying contractors
- forms, calculators and tools to make sure you withhold the correct amount of tax.

Payroll tax

You must register even if you think that you will pay less than $1.3 million in Australian taxable wages in a year.

Payroll tax is imposed by each state and territory, not by the ATO.

Superannuation guarantee obligations

As an employer, you can either pay a set minimum level of superannuation for each of your eligible employees, or pay a charge to the ATO.

You must use SuperStream to pay employee superannuation guarantee contributions to super funds. All employers should be SuperStream compliant.

If you have 19 or fewer employees, use the ATO's Small Business Superannuation Clearing House—a free online superannuation payments services that helps small businesses meet their superannuation obligations.

V. Financial record keeping

Keeping accurate and up-to-date records is vital to the success of your business. Good records help you to minimise losses, manage cash, meet any legal, regulatory and taxation authority requirements and improve financial analytics. Your accountant can help you set up a record-keeping system.

Understanding financial record keeping

Record keeping is how you log, store and dispose of important financial information for your business.

Records are:

- source documents, both physical and electronic, that show transaction dates and amounts
- contracts and other legal documents
- private customer and business details.

You may need to access your records at different times of the year (e.g. for end of financial year) or on request (e.g. by the Australian Taxation Office).

Benefits of good financial record keeping

Good financial record keeping can help you:

- protect your business
- measure your performance
- maximise profits
- plan and work more efficiently
- generate meaningful reports
- meet legal and tax requirements
- protect your rights
- manage potential risks.

How to keep financial records

There are certain record-keeping requirements for businesses in Queensland, and there may be specific laws and requirements related to your industry sector.

You can keep records using either an electronic or manual system. You also need to make sure your records are secure, private, backed up and can be easily reported on if needed.

The Australian Taxation Office (ATO) recommends that businesses use an electronic record-keeping system. The same record-keeping principles apply to both electronic and manual records.

Assess your record-keeping skills

Use the ATO record-keeping evaluation tool to identify what records you need to keep and review how well your business is keeping records.

Electronic record keeping

An electronic record-keeping system, such as accounting software, makes it easier to capture information, generate reports, and meet tax and legal reporting requirements.

Advantages

- Easily record business transactions, including income and expenses, payments to workers, and stock and asset details
- Efficiently keep financial records and requires less storage space

- Provides the option of recording a sale when you raise an invoice, not when you receive a cash payment from a client
- Easily generate orders, invoices, debtor reports, financial statements, employee pay records, inventory reports
- Automatically tallies amounts and provides reporting functions
- Keeps up with the latest tax rates, tax laws and rulings
- Emails invoices to clients, orders to suppliers, or business activity statement (BAS) returns to the Australian Taxation Office (ATO)
- Backs up records and keep them in a safe place in case of fire or theft

Manual record keeping

You may prefer to use a simple, paper-based record-keeping system.

Advantages

- Less expensive to set up
- May be easier to use for correcting errors, as opposed to computerised ones that can leave complicated audit trails.
- Lower risk of corrupted data
- Less of a risk of data loss, particularly if records are stored in a fire-proof environment
- Problems with duplicate copies of the same records are generally avoided
- Familiarity with how accounting software calculates and treats your information isn't needed

How long to keep records

You must keep your records for a certain period. The length of time will depend on the type of record and your business type or industry.

Legal information

There are legal requirements for how long you keep some records. These include:

income tax and other financial records—at least 5 years

personnel records—at least 7 years

formal company documents (e.g. resolutions)—indefinitely.

Keeping your records secure and private

Legal information

If you collect and keep customer records, you'll need to protect and respect your customers' privacy. You may have to comply with the Privacy Act 1988.

Read the Office of the Australian Information Commissioner's guide to privacy for small business to help you apply the national privacy principles.

New technologies make it easier to access, transmit and misuse personal information. You will need to pay particular attention to securing online and electronic records. You should develop a privacy policy and train staff to implement it.

Reporting on your records

If you use an electronic record-keeping system, you must be able to produce a hard copy of a record if the ATO or Australian Securities and Investments Commission (ASIC) request it.

Backing up records

Set up a secure electronic backup system to ensure records are safely stored and regularly backed up. Daily backups are recommended, particularly for important records.

Online (or 'in the cloud') backup services allow you to access records from anywhere, at any time. They are generally inexpensive and offer benefits for flexible work and business continuity. Make sure any online system protects the privacy and security of your business and customers.

Cheap backup options include memory sticks and external hard drives.

Make sure any physical backup copies are stored in a separate location to your business in case of fire, theft or a natural disaster.

VI. Fund your business

Understanding the basics of raising capital is a vital business skill. You will need money whether you're looking to start a new business or grow your existing business.

When exploring funding options, consider:

- the amount of finance required
- the nature of your project
- your stage of business development (i.e. a start-up or an established business).

Potential sources of funding

There are 3 basic sources of funding:

- equity finance—investing your own or other stakeholders' funds into your business in exchange for partial ownership (e.g. venture capital)
- debt finance—borrowing funds that you pay back with interest within agreed time frames (e.g. bank loans)
- other—raising funds through other sources that may not need repayment or to provide an ownership stake in your business (e.g. crowdfunding).

Your business may need to be more mature to access some of these types of funding.

Create a funding plan

The first step in securing funding is to draft a business plan. Whether you are starting a business or looking to grow your existing business, your business plan is the key document that guides your future operations. It also makes your business goals clear to potential investors or lenders and explains how you are going to spend your invested or borrowed money (i.e. your financial strategy).

Your business plan should include a detailed funding plan and 12-month cash flow budget that explains:

- how much money will be required
- when the money will be required

- where the money will be sourced
- what the money will be used for
- when debts will be paid back
- when investors can expect to see returns.

Try to identify all the likely costs involved in your business:

- start-up capital (e.g. office equipment, plant and machinery, building costs, shop fittings, licences, permits, insurance, bond or premises costs)
- operating capital (e.g. salaries/wages, rent, expenses, supplies, utilities, advertising/marketing, interest repayments, depreciation)
- contingency funds—to survive rough periods until your business becomes profitable or during periods of low cash flow.

How To Secure Funding For A Small Business?

Capital is the quintessential requirement that propels a business forward and allows it to achieve its target. Every company has its unique funding requirements that help it to stay afloat, maintain its cash reserves and reinvest in its processes. Thus, entrepreneurs need to identify how cash much is enough to run their venture successfully.

Small businesses need to be more careful with their capital as they need bigger amounts to grow and establish a substantial customer base. So, whether it is seed investment or funding for expansion, companies need a constant flow of funds to maintain their momentum.

Thus, entrepreneurs looking for businesses for sale in Perth must know about various sources of funding to maintain a positive cash flow and expand. However, they should keep their debts in check when taking out loans, or they can quickly translate into cash deficits. So here is how small businesses can secure funding to keep progressing in the best way possible.

1. Self-Fund Your Business

Bootstrapping is the most common funding method that involves financing your business through your personal savings. It does not require lending from a third party and there is no paperwork or collateral required. Many entrepreneurs also get funding from their family and friends, who can lend the amount at a much lower interest rate. It proves beneficial because there is no hassle or legwork, and you get immediate access to funds.

Small business owners in Perth usually prefer bootstrapping in the initial stages of the business because of the ease of getting the money. However, it may not prove helpful when the business is growing because it needs a higher amount. Also, some friends and relatives may only lend money in exchange for equity and there is the risk of relations turning sour if ideologies do not match in the long run and lead to disputes and litigations.

2. Accelerators or Business Incubators

The accelerator or incubator program is for start-ups who need support from the introduction stage of the business lifecycle. The initiative offers several advantages to start-ups, including business capital, co-working spaces, introduction and meetings with investors, business management training, etc.

Corporate partners work for these incubators to help start-ups find footing in the marketplace. They are dedicated to creating high-growth entities, and the start-up can stay with the incubator depending on its needs. The acceptance to the program is through an application process. If the business incubator finds the business scalable and viable, they provide all the support for growth, including funds.

3. Find Venture Capitalists

Businesses that are operating in a high-growth or risky sector usually get seed funding through venture capital. It is a pool of funds created by savvy investors who get equity in the business, which promises long-term growth. Most venture capitalists are interested in high-tech companies in the IT and biotechnology sector because of their high growth prospects.

Thus, entrepreneurs who wish to get funded by venture capitalists must know that they will want to generate a high return on investment and will demand returns. While seeking the funding, you need to look for venture capitalists and get them acquainted with your business plan to get the desired capital.

4. Liaise with Angel Investors

Angel investors are high-net-worth individuals who have operated in the same field in which they invest. They are like mentors for small businesses that need funding and valuable business advice to grow with their tutelage and financial help. These investors work alone and invest in several small businesses to earn a considerable return on investment. They also need equity in the business in exchange for the funding.

Small business owners must look for investors who have helped in the growth of other businesses in the past and have surplus cash for investment. However, the amount provided by angel investors is lower than what can be received from venture capitalists. The reason behind this is that angel investors work alone while venture capital offers a sum of the funds of several wealthy investors.

5. Government Grants

The state and territory governments in Australia provide grants, funds and support programs to small businesses. There are more than 700 grants and programs across the country that can be accessed through the government website and chosen based on the industry, location, business type, etc.

Businesses can submit their applications and get the funds needed to grow. Some of these grants include the Entrepreneur's Program, which offers funding of up to $1 million to support small entities. Besides funds, this program also offers incentives and expert advice to innovate and grow in the field. Similarly, the Accelerating Commercialisation program also provides project funding of up to $1 million to help small businesses create a new product or service. Check the criteria for getting the grant and submit your application to make the most of it.

6. Small Business Loans

Most entrepreneurs rely on small business loans to secure funds for their companies. There are a variety of loan types provided by banks, such as loans with interest payments, loans with additional charges, etc. Entrepreneurs become liable to tax and GST implications when they borrow money to fund their businesses.

It is advisable to ask your accountant to find a business loan that matches your requirements and does not burden you with the repayment and interest rates. Some of the loans that business owners in Australia can access include a line of credit, commercial bill, rent to buy, chattel mortgage, invoice finance, overdraft facility, fully drawn advance, commercial hire-purchase and factoring.

7. Crowdfunding

Crowd-sourced funding involves securing funding for the business through donations, loans and getting cash in exchange for shares in the business. It is done online when the entrepreneur posts the business idea on the website and asks people to contribute funds for the business. The entrepreneur can put a cap on the amount required for the growth or start-up.

Crowdfunding allows the entrepreneur to interact with the contributors and get suggestions and ideas from them. Since it takes place online, it becomes easier to spread the word around about the funding requirement through social media. Also, if you are unable to achieve success, you would not be badgered as there will be no stakeholders.

Funding is a common requirement for entrepreneurs who wish to purchase a business for sale in Perth or launch their own start-up. They can utilise any of the methods listed above to secure financing for their business and make it grow. However, they must understand the terms and conditions and the impact of the funding on their cash flow before going ahead.

References

Business And Finance | Job & Skills WA, Retrieved September 26, 2022 From

https://www.jobsandskills.wa.gov.au/business-and-finance

Business Finance And Loans | Small Business Development Corporation, Retrieved September 26, 2022 From

https://www.smallbusiness.wa.gov.au/finance/business-finance-loans

Business Finance Essentials | Business- Australian Government, Retrieved September 26, 2022 From

https://www.business.qld.gov.au/running-business/finance/essentials

By Liam Walker. (2022) | How To Secure Funding For A Small Business? | Business2sell, Retrieved September 27, 2022 From

https://www.business2sell.com.au/blogs/strategy/how-to-secure-funding-for-a-small-business