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lives or dies by its balance sheets, so it's important for business owners to understand basic finances. Business owners don't need to have an MBA in accounting, but they ...

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Owning a small business can be rewarding; you control your own destiny, set your working hours, choose the employees you want to work with, and feel proud of building something of your own.

But owning a business carries many responsibilities. Business owners must keep

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## How Financially Literate Are Small Business Owners?

A recent study of small business owners conducted by Intuit uncovered surprising results. The study found that **40% of small business owners** consider themselves to be financially illiterate. At the same time, 81% of them are doing their business' finances themselves.

Let's break these numbers down. If 40% are financially illiterate, and 81% are handling their own finances, this means that 32.4% of those handling their own finances are ill-equipped to do so. The number of small businesses operating in 2010 **was 27.9 million**. Therefore, a total of about 5.9 million businesses are operating without a strong financial rudder.

## Why is Financial Literacy Important?

Understanding your business's finances helps ensure you can withstand downturns. It will allow you to take advantage of opportunities that arise and increase the business's chances of succeeding. On the other hand, if you are financially illiterate, your business will eventually run into problems, such as allowing expenses to increase to a point where profits are minimal. In some circumstances, business owners fail to include the correct amount of taxes on their profit and loss statement.

These are a few areas that can cause your company to run aground if you are unprepared:

### Taxes

Failure to understand federal and state tax requirements or to keep accurate records

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not always be the best strategy because a lower price can deteriorate your brand and make it difficult to increase prices in the future.

## Anticipating Cash Flow

At the start of a business' lifecycle, suppliers want fast payment for inventory. If your products are sold on credit, it **can be months** between the time of making a sale and getting paid. Failure to plan for this scenario can jeopardize your company.

## Which Areas of Finance Does a Business Owner Need to Understand?

There are three financial reports that everyone who owns a business should be able to understand:

### 1. Profit and Loss Statement

This financial statement details the amount of profit or loss over a specific time period, commonly a fiscal quarter or a year. The statement details the company's revenues, expenses, gains, and losses. Net income is the difference between the revenues and gains and the expenses and losses. A positive balance equates to net income, while a negative balance is a net loss. A company can use this information to determine whether it can generate profit by increasing revenue and/or reducing costs. If the organization is losing money, the owner should investigate where to cut expenses. Tax preparers rely heavily on a profit and loss statement to prepare a tax return.

### 2. Balance Sheet

A balance sheet is a financial statement that reports the company's assets and

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amount of cash that enters the company from its operations and external investment sources, as well as the amount of cash that exits the company to pay for business activities and investments. Publicly traded companies [must disclose their cash flow statements](#) to the U.S. Securities and Exchange Commission (SEC) and the information must be made public.

While an understanding of these financial reports will go a long way in running a business, it's also essential for a business owner to know their limits. If something seems too complicated or volatile for you to handle on your own, the best course of action is always to ask for help. In fact, knowing when to ask for help is just as important as knowing *who* to ask, so be sure to use the services of a trusted financial specialist and a tax attorney.

## How Can I Become More Financially Literate?

There are many [free financial literacy resources](#) small business owners can take advantage of to up their game. Here are a few:

### Small Business Development Center Program

[Small Business Development Centers](#) (SBDCs) offer technical assistance to small businesses and aspiring entrepreneurs. Administered by the U.S. Small Business Administration (SBA), and with more than 900 locations across the country, the SBDC program delivers financial literacy tools that can be accessed online. The SBDC also offers workshops, business counseling and business finance training.

### FDIC Money Smart for Small Business

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**SCORE** is a nonprofit organization that counsels, trains, and provides mentors for entrepreneurs and future small business owners. SCORE's website features online tools and information that cover a wide array of topics on starting and running a small business. The Finance and Money section of the website contains articles and help on finance and financial planning. Local workshops and mentors are available.

## 360 Degrees of Financial Literacy

**360 Degrees of Financial Literacy** is a free resource provided by the American Institute of Certified Public Accountants (AICPA), with the goal of providing financial information to individuals. The website contains a section for small business owners that includes topics such as budgeting, business formation, and debt and business valuation. Financial tools and calculators are also available.

## SME Toolkit

This free resource is provided by IBM and the International Finance Corporation (IFC), a subsidiary of the World Bank. The website is geared toward small and medium enterprises (SMEs). While the **SME Toolkit** focuses on minority, women and veteran entrepreneurs, most of the information provided is useful for any small business owner.

## Improving Your Financial Knowledge

No matter how you look at it, if you own a small business, you have nothing to lose and everything to gain by increasing your financial literacy. At the very least, it will help you communicate more effectively with your accountant and could **save your business from financial ruin**.

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John Milikowsky represents U.S. and foreign businesses and individuals in

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