FINANCE, MODULE 1

Reading your numbers

After this module you can read a profit and loss statement and a balance sheet, explain why the bank balance and the profit never match, and say why your books are kept the way they are.

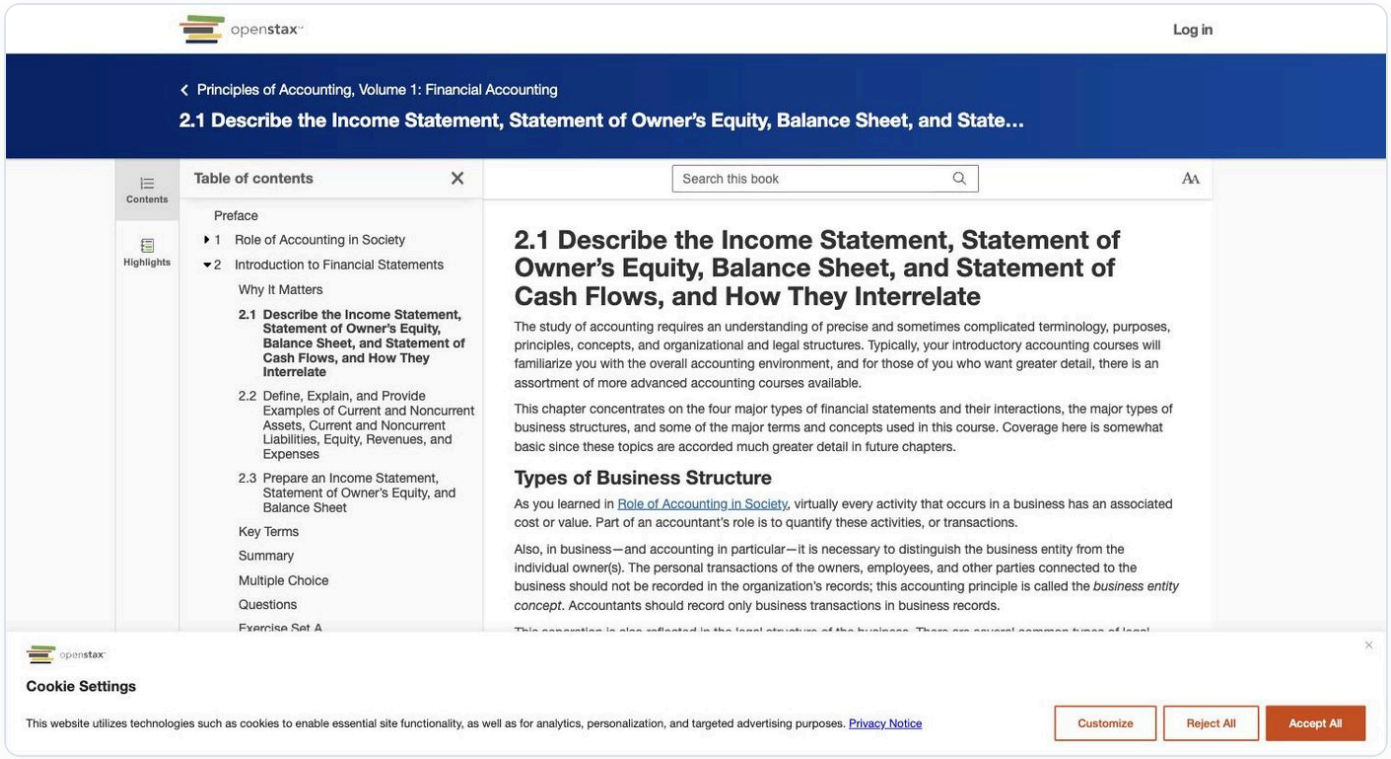
One question, every month

Did the business get richer or poorer? Accounting is a system for answering that in a way a stranger can check. Everything else, the reports, the software, the terms, is machinery for that one job.

Two reports you will read every month

Report	Question it answers	Think of it as
Profit and loss (P&L)	Did we make money this month?	A video of the month
Balance sheet	What do we own, what do we owe, and what is left over?	A photograph taken at midnight on the last day

There is a third, the cash flow statement, that explains why the bank balance moved even though profit said something different. You will see it when it matters. The first two are enough to run a clinic.



Source OpenStax, Principles of Accounting, Volume 1, section 2.1. A free college textbook. Chapter 2 is the best 40 minutes you can spend after this module.

A month at Harbor Aesthetics

Read the P&L top to bottom: what came in, what it cost to deliver, what it cost to run the place, what was left.

Harbor Aesthetics, Profit and Loss, September	Amount
Revenue (services delivered and retail sold this month)	125,000
Injectables (neurotoxin, filler)	69,000
Laser, light and skin treatments	33,500
Membership revenue earned this month	15,000
Retail products	7,500
Cost of services (the product used up to deliver that revenue)	28,400
Gross profit	**96,600**
Operating expenses (the cost of running the clinic whether or not anyone walks in)	85,400

Provider wages and commissions	30,000
Front desk and admin wages	9,200
Owner salary	12,500
Payroll taxes and benefits	5,000
Rent	8,000
Marketing	8,300
Equipment lease, software, insurance, utilities, other	12,400
Earnings before depreciation and interest (EBITDA, Advanced 4)	**11,200**
Depreciation (the laser wearing out, spread over its life)	5,000
Interest on the equipment loan	1,800
Net income (profit before tax)	**4,400**

> **Read it like this.** Of every dollar a patient paid, about 23 cents went to product, 68 cents went to running the clinic, 5 cents to the equipment wearing out and the loan, and about 3.5 cents was left. Small on purpose: this is a first year clinic paying a full owner salary and a loan. Notice that payroll in all its forms (providers, desk, owner, taxes) is 45 cents of the dollar. That is why Finance 6 starts with payroll.

Now the photograph at midnight on September 30. It always balances: what you own equals what you owe plus what belongs to you.

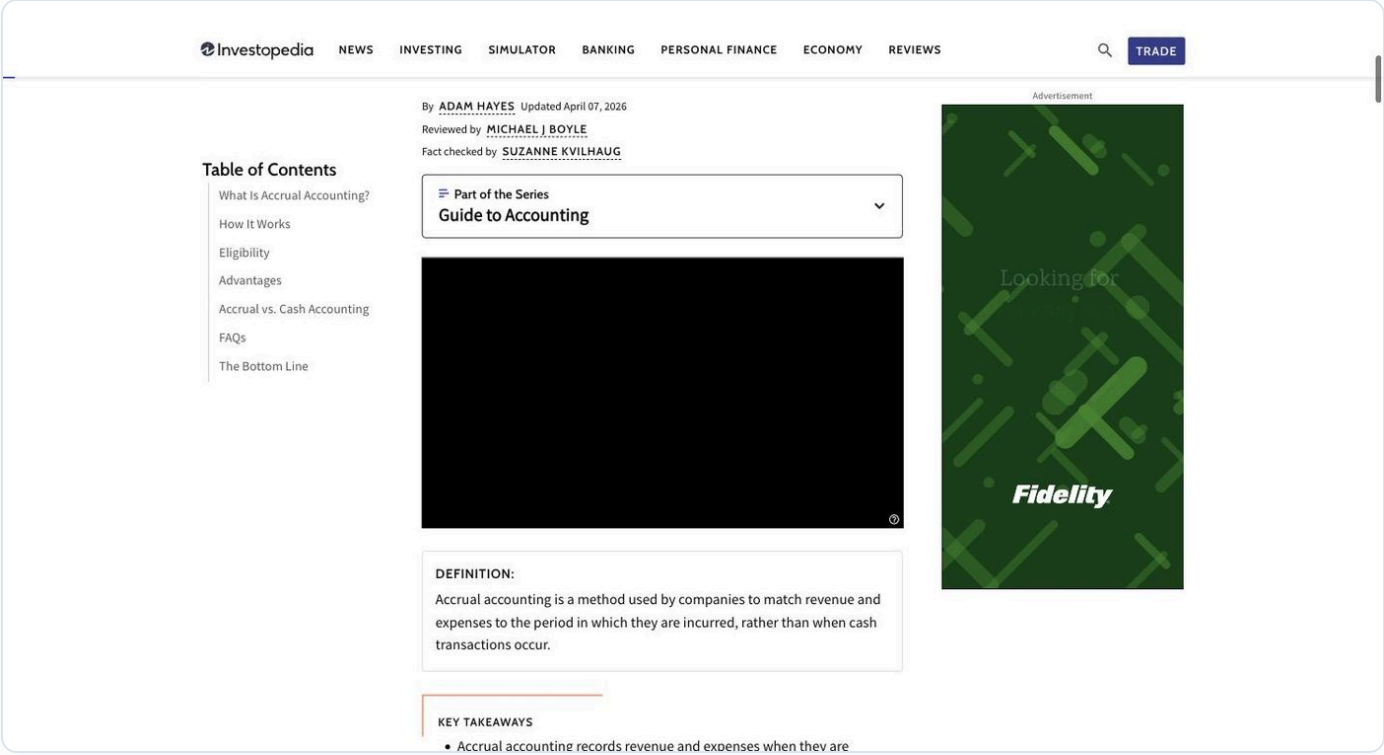
Harbor Aesthetics, Balance Sheet, September 30	Amount
What we own (assets)	
Cash in the operating account	61,000
Card processor deposits in transit	9,800
Injectables on the shelf (inventory)	22,000
Prepaid insurance	6,500
Equipment, net of depreciation	238,000
Lease security deposit	16,000
Total assets	**353,300**

What we owe (liabilities)	
Credit card balance	7,400
Payroll taxes and wages owed	11,900
Sales tax collected, not yet sent in	1,200
Packages and memberships sold, visits not yet delivered	41,000
Gift cards outstanding	6,800
Equipment loan	176,000
Total liabilities	**244,300**
What is left for the owner (equity)	109,000
Total liabilities and equity	**353,300**

> **Two things to notice.** First, $41,000 of packages and memberships that patients already paid for sits here as a debt, not as revenue. The clinic still owes those visits. Second, the cash balance ($61,000) and the profit ($4,400) have almost nothing to do with each other. Cash went up more than profit this month because patients prepaid; it will go down more than profit next month when the loan payment and the quarterly insurance hit. That gap is why you get both reports.

Cash basis and accrual basis: the one habit

There are two ways to decide *when* to count a sale. On the **cash basis** you count it when the money lands. On the **accrual basis** you count it when you earned it, meaning you delivered the service. A patient buys a six visit laser package for $2,400 in January and comes once a month. On a cash basis January looks wonderful and the next five months look worse than they were. On the accrual basis each month shows $400, which is what happened. Your books are kept on accrual so the P&L tells the truth month to month, and the bank balance is read separately.



Source Investopedia, Accrual Accounting. The definition to remember: match revenue and expenses to the period they belong to, not to when cash moved.

Going deeper, if you want to

Every transaction touches two places. Buy $3,000 of neurotoxin on the company card: inventory goes up $3,000 and the card balance goes up $3,000. Use $600 of it on patients: inventory goes down $600 and cost of services goes up $600. Accountants call the two sides debits and credits. You do not need to know which is which. You need to know that when a report looks wrong, the other side of the entry is usually where the mistake lives.

Account numbers tell you where a line lands. Accounts starting with 1 are things you own, 2 are things you owe, 3 is what belongs to you, 4 is revenue, 5 is cost of services, 6 and up are operating expenses. Revenue accounts and cost accounts are set up in pairs (neurotoxin revenue next to neurotoxin product cost) so you can see whether each service is priced right. That pairing is what makes Finance 6 and Operations 3 possible.

> **Where Benchmark comes in.** We keep the books on accrual, split revenue and cost by service line, and hand you both reports closed and reconciled on business day ten (Finance 4). You read them; the questions are included.

Try it yourself

- [ ] Open your P&L for last month and find gross profit. Divide it by revenue. That is your gross margin; a medspa usually lands between 60 and 80 percent.

- [ ] Open the balance sheet and find deferred revenue and gift cards. Say out loud what those numbers mean: visits and products you still owe.
- [ ] Add up every payroll line on the P&L, including your own salary, and divide by revenue. Write the percentage down; you will need it in Finance 6.

Check yourself: Finance 1

A patient pays $2,400 in January for six laser sessions. On the accrual basis, how much revenue is recorded in January?

- $2,400, because the money arrived in January
- $400, one session's worth, and the rest waits on the balance sheet
- $0 until all six sessions are done

Revenue is earned as each session is delivered. The other $2,000 sits in deferred revenue, a liability, until the visits happen.

Which report answers "what do we own and owe as of today"?

- Profit and loss
- Balance sheet
- The bank statement

The balance sheet is a snapshot of a single day. The P&L covers a period.

Profit was $4,400 but cash went up $18,000. The most likely reason?

- The bookkeeper made an error
- Patients prepaid for packages, which is cash in but not yet revenue
- Profit and cash are always the same

Prepaid packages raise cash and raise deferred revenue. They do not touch profit until the visits are delivered.

Gross profit is

- Revenue less every expense
- Revenue less the product used to deliver it
- The bank balance

Gross profit is what is left after cost of services, before the cost of running the clinic.

Why are revenue and cost accounts set up in matching pairs by service?

QuickBooks requires it

So you can see whether each service is priced right

To make the chart longer

Neurotoxin revenue next to neurotoxin product cost tells you the margin on that service. One lumped supplies account cannot.

Pick an answer for each question.

Want this done, not just explained?

The 10-Day Sprint finds the leaks for $1,000, one time. After that, on the plan, the scorecard keeps coming and at least one growth initiative is executed with you every month. Plans from $2,299 a month. Everything in this module is part of that work.

See the sprint and pricing | Text Nate

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