

Table of Contents

Introduction	1
About This Book	1
Conventions Used in This Book.....	2
What You're Not to Read.....	3
Foolish Assumptions.....	3
How This Book Is Organized	4
Part I: Fitting Cash Flow into the Big Picture of Running a Business	4
Part II: Using Financial Statements to Assess Cash Health.....	4
Part III: Getting Intimate with Your Company's Cash Flow Needs.....	4
Part IV: Managing Your Business with Cash Flow in Mind	5
Part V: The Part of Tens	5
Icons Used in This Book	5
Where to Go from Here.....	6
Part I: Fitting Cash Flow into the Big Picture of Running a Business.....	7
Chapter 1: Getting in Sync with the Rhythm of Cash	9
Not Letting the Well Run Dry	10
Outlining Profit Accounting Basics	11
Reviewing revenue accounting	11
Examining expense accounting.....	12
Contrasting cash- and accrual-basis accounting	13
Seeing Why Profit and Cash Flow Are Different Bottom Lines	14
Considering what the income statement doesn't say about cash flow	14
Exploring cash flow from profit	15
Identifying and Reporting Basic Types of Cash Activities	19
Cash flow from investing activities.....	20
Cash flow from financing activities.....	20
Cash flow from operating (profit-making) activities	21
Putting cash-flow activities together.....	21

Chapter 2: Why Accrual Accounting Is Essential	23
Finding Out the Four Functions of Accounting.....	24
Keeping records (Bookkeeping)	25
Giving company management the information it needs.....	26
Complying with tax laws	28
Reporting financial information	29
Examining the Nature of Accrual Accounting.....	31
Uncovering the inadequacy of cash-basis accounting.....	32
Recognizing accrual accounting in financial reports	32
Reporting Assets and Liabilities in the Balance Sheet.....	34
Chapter 3: The Big Three Financial Statements	37
Why Financial Statements Are Essential	38
Who gets financial statements and why	40
Who doesn't get financial statements and why	41
Facing Off: The Balance Sheet.....	42
Strolling through the balance sheet	42
Putting accounts in their right places.....	44
Dealing with the limitations of the balance sheet	45
Tracing revenue and expenses in the balance sheet	47
Managing capital.....	49
Making Profit: The Income Statement.....	52
Moving from the revenue top line to the profit bottom line	54
Deciding which is more important: Revenue or expenses	54
Summarizing Cash Flows: The Statement of Cash Flows	55
Showing cash flow from operating (profit-seeking) activities	56
Listing other sources and uses of cash.....	57
Chapter 4: Getting a Grip on the Statement of Cash Flows	59
Distinguishing Cash Flows.....	60
Adjusting your way to cash flow from operating activities.....	62
Cogitating on cash flow from investing activities.....	66
Considering cash flow from financing activities	66
Getting to Know the Dual Personality of the Statement of Cash Flows	69
Spotting changes in financial condition.....	69
Building the year-end balance sheet	70
Comparing Cash-Flow Scenarios	72
Starting with cash flow in a steady state	73
Assessing cash-flow effects of growth and of decline	75
Understanding negative cash flow.....	76
Recognizing Problems with the Statement of Cash Flows	77
Getting skipped by small businesses	77
Providing too much or too little information.....	78

Part II: Using Financial Statements to Assess Cash Health..... 81**Chapter 5: Mining the Balance Sheet for Cash..... 83**

Reading the Balance Sheet from a Cash-Flow Perspective	84
How assets are listed in the balance sheet	
in relation to generating cash.....	85
How liabilities are listed in the balance sheet	
in relation to consuming cash	89
What the balance sheet doesn't disclose about cash flows.....	91
Giving the Balance Sheet a More Thorough Examination.....	93
Using key balance sheet performance-measurement tools.....	93
Evaluating your assets	96
Taking a closer look at your liabilities	100
Scrubbing the Balance Sheet Clean for Its Users	103
A case study: Scrubbing the balance	
sheet of ACME Distribution, Inc.	103
Aiding internal business management	109
Providing confidence to outsiders	109
Unlocking Hidden Cash from the Balance Sheet	110
Turning over current assets.....	110
Investing in long-term assets.....	111
Leveraging your current liability friends.....	111
Using notes payable, loans, and leases appropriately.....	112

Chapter 6: Digging Deeper into Cash Flow 113

Tying Up Cash Flow in a Neat Bundle	113
Presenting financial statements for analyzing cash flows	114
Cutting the balance sheet down to size	115
Reviewing sources and uses of cash	119
Zeroing in on changes in financial	
condition from making profit.....	119
Developing Benchmarks for Cash Flow	121
Comparing cash flow with sales revenue momentum	121
Using other tools for cash-flow analysis	124
Massaging Cash-Flow Numbers	127

Chapter 7: Understanding Liquidity versus Available Cash 131

Defining Business Solvency and Liquidity	
(Hint: Not the Same Thing)	132
Applying Business-Solvency and Liquidity Measurement Tools.....	137
Measuring and monitoring solvency	137
Keeping tabs on liquidity	140

Avoiding Liquidity Traps	143
Tying up cash in company assets.....	143
Using debt inappropriately.....	145
Assuming that business growth is always good.....	147
Assuming that a shrinking business always represents trouble	148
Discovering Untapped Sources of Liquidity	149
Liquidating assets.....	149
Leveraging assets.....	151
Relying on available lending sources	152
Approaching creditors, customers, and other partners	153
Using equity and off-balance-sheet sources of capital.....	154
Financial Leverage: The Good, the Bad, and the Downright Ugly.....	155
The good	155
The bad	156
The downright ugly	156

Part III: Getting Intimate with Your Company's Cash Flow Needs..... **157**

Chapter 8: Creating a Business Plan to Secure Cash **159**

Outlining the Basic Business Plan.....	160
The executive summary.....	161
The market assessment	161
The operational overview.....	162
The financial summary: Performance and required capital (Cash).....	163
Developing a Business Plan.....	163
Outlining your plan by using BOTE, WAG, and SWAG	164
Getting the process going.....	165
Using two simple but powerful tools: SWOT and KISS.....	167
Incorporating Third-Party Information into Your Plan.....	169
Gathering the info	170
Using only reliable info	170
Riding the CART Concept: Complete, Accurate, Reliable, and Timely	171

Chapter 9: Building Best-in-Class Projection Models to Manage Cash **173**

Rounding Up Resources to Build Financial Forecasts	173
Planning with the Big Picture in Mind	174
Deciding on a top-down versus bottom-up projection strategy	174
Identifying your critical business economic drivers.....	176
Building the Basic Projection Model.....	178

Making the Most of Your Projections	181
Getting familiar with some useful terms	181
Treating forecasts as living, breathing management tools	183
Understanding the difference between internal versus external projections	184
Preparing multiple projection scenarios: The what-if analysis	185
Integrating forecasts into the active management of your business.....	188
Broadening the use of projections even further.....	191
Chapter 10: Identifying and Securing External Sources of Capital	193
Getting a Grip on the Capital Concept	194
Understanding the Basics of Equity Capital.....	195
Equity preference	195
Equity and management influence	196
Starting to Look for Capital	196
Looking in the mirror	197
Turning to family, friends, and close business associates	198
Seeking Equity Sources of Capital	199
Angel investors.....	200
Venture capitalists (VCs).....	201
Private equity groups (PEGs).....	201
Other private investment groups	202
Accessing Public Sources of Capital	203
Putting Your Capital to Good Use	204
Looking at the Reality of the Current Capital Markets	209
Ten tips for raising capital.....	209
Five realities of the current capital markets	210
Chapter 11: Knowing When to Use Debt to Finance Your Business	213
Understanding the Basics of Debt Capital.....	214
Debt maturity	214
Debt security	214
Other debt attributes	216
Determining When Debt Is Most Appropriate	216
When you can offer security or collateral	217
When business is stable.....	217
When you have financial strength	218
Using Loans, Leases, and Other Sources of Debt	218
Borrowing from banks.....	218
Making friends with asset-based lenders.....	220
Leasing as a source of capital	221
Tapping government programs and the SBA	223
Using other sources of debt-based capital	223

Getting Creative with Capital	224
Generating internal cash flow	224
Leveraging unsecured creditors	225
Going after government aid, gifts, and grants	225
Partnering up.....	226
Leveraging Uncle Sam for Cash	226
Four government-endorsed strategies to help improve cash flow.....	227
Don't forget the SALT: State and local taxation	235

**Part IV: Managing Your Business with
Cash Flow in Mind.....** **239**

Chapter 12: Covering the Basics of Cash and Cash Activity **241**

Managing the Unique Characteristics of Cash.....	242
Understanding that cash ends up being one side of almost every transaction	242
Tuning in to the constant cash hum.....	244
Deciding what a normal cash balance should be	245
Implementing Fundamental Cash Management Practices	249
Establishing cash and bank accounts	249
Controlling cash and bank accounts	252
Maximizing your business's cash	254
Understanding Cash in the Digital Age	255
Moving and processing cash transactions electronically	256
Establishing cash controls in electronic-based accounting systems	259
Working with Cash as a Key Business Indicator	262
Knowing the seasonal ebb and flow of cash.....	263
Setting periodic cash level benchmarks	265

**Chapter 13: Preventing Cash Losses from
Embezzlement and Fraud** **267**

Setting the Stage for Protection.....	268
Preventing loss with internal controls	268
Recognizing the dual purpose of internal accounting controls	269
Struggling with fraud committed by the business.....	270
Putting Internal Controls to Work	272
Going down the internal controls checklist	272
Considering some important details of internal control	276

Recognizing Limitations of Internal Controls	278
Keeping internal controls under control	279
Finding fraud that slips through the net.....	279
Chapter 14: Managing the Selling Cycle to Improve Cash Flows . . .281	
Understanding the Entire Selling Cycle: Start to Finish.....	282
The accounting/financial view	282
The strategic view.....	282
Why the sales cycle is the biggest consumer of cash.....	283
Implementing Basic Controls in the Selling	
Process to Manage Cash	284
Qualifying the customer.....	284
Being prudent with credit review and approval.....	286
Setting proper terms and conditions	289
Supplying CART — complete, accurate, reliable, and timely — invoices	291
Managing past-due accounts and collection efforts.....	292
Getting Creative to Improve Sales-Related Cash Flows	296
Using discounts: The double-edged sword	296
Offering creative payment terms	297
Using deposits, advances, and prepayments	299
Accepting alternative forms of payment	300
Managing seasonality in the selling cycle.....	303
Managing the Lending Agreement in Relation to Your Sales Cycle	304
Defining eligible receivables.....	304
Understanding advance rates and dilution	305
Watching for hidden time bombs in your lending agreement	306
Driving a lending agreement to improve liquidity and access to cash	309
Chapter 15: Managing the Disbursement Cycle to Improve Cash Flows.....311	
Tracing the Entire Disbursement Cycle.....	311
Taking Critical Steps in the Disbursement Cycle to Manage Cash.....	313
Qualifying suppliers and vendors.....	313
Establishing proper disbursement cycle controls	314
Managing external creditors	316
Getting Creative to Improve Cash Flows from the Disbursement Cycle.....	318
Leaning on vendors and suppliers	318
Using JI'T payment strategies	320
Grading your vendors and suppliers.....	320
Floating along	322
Creating cash from inventory.....	323
Tapping vendor-provided financing.....	324

Leveraging Your Employees for Cash	324
Timing commissions and bonuses	325
Connecting compensation to performance.....	326
Utilizing noncash forms of equity compensation for employees	327
Checking out other benefit strategies and ideas	328
Part V: The Part of Tens	331
Chapter 16: Ten Keys to Managing Cash Flows in a Small Business	333
Respect and Understand Financial Statements	334
Plan, Do Projections, and Plan Some More	334
Focus on Capital and Cash: The Lifeblood of Any Business	335
Understand Your Selling Cycle	336
Manage Your Disbursements Cycle	336
Be Creative to Generate Cash	337
Balance the Balance Sheet	338
Understand External Capital Markets.....	338
Protect Cash at All Times	339
Always Think of CART.....	340
Chapter 17: Ten Tales of Cash-Flow Woes	341
Misunderstanding Trade Account Receivables	341
Letting Good Inventory Go Bad	342
Improperly Investing in Soft Assets	343
Falling into the Taxable Income Trap	344
Misapplying Available Debt-Based Capital.....	345
Failing to Prepare for the Economic Hard Landing	346
Getting Left in the Cold by Changing Market Conditions.....	347
Making Overly Optimistic Sales Forecasts	348
Robbing Peter to Pay Paul.....	349
Growing Yourself Out of Business.....	350
Index	351