

## Mind Your Own Business

In our last article we discussed the *Balance Sheet*. If you remember, the *Balance Sheet* is one of the three most important financial documents in a business. We learned that the *Balance Sheet* only reflects what your business owns and what it owes on the day it is generated. It tells you how you ended up or where you are right now. The *Balance Sheet* as an individual financial document can tell you some interesting and important facts about your horse business.

- Is your business solvent – are your assets at least equal to your liabilities?
- Is your business sufficiently liquid – does it have enough Cash?
- What assets do you have in your business?
- Who has claims on your business assets?

The other two important financial documents are the *Income Statement* and the *Cash Flow Statement*. The *Cash Flow Statement* is my personal favorite – ‘**Profit is an accounting opinion, cash is fact**’. In this article we are going to discuss the *Income Statement*. The *Income Statement* is sometimes called the *Statement of Earnings*, the *Profit-and-Loss Statement*, the *Statement of Operations*, or just the *P&L*. For the purpose of this article we are going to refer to it as the *Income Statement*. The *Income Statement* is the financial document that shows you if your horse business was profitable over a given period of time.

Although many businesses hold up their *Income Statement* as a mark of success when they are profitable, the *Income Statement* can be a double edge sword if you are not careful. It can be tremendously useful, but can also be tremendously dangerous because it can be misleading. If you look at only your *Income Statement* you can think you have money to spend when you don't. Remember my warning in the last article about the perils associated with ‘Checkbook Accounting’. You can think everything in your horse business is financially healthy when some parts are not healthy at all. If you remember from the last article, most business transactions consist of two parts – this is where the danger lies. *First are the promise and the agreement*. You purchase some feed from the feed store and you have the feed store put the cost of the feed on your account (*promise to pay*). You sell a horse to a customer with monthly payments and the customer *promises to pay*. *Next is the settlement when the bills are paid and cash actually changes hands*. Virtually all horse businesses have these two part transactions – even cash based businesses don't usually pay for everything in cash.

Strange as it might sound, the *Income Statement* tracks only the *promise and agreement* part of a business's transactions. An *Income Statement* is not about cash. That is why the third

financial document, the *Cash Flow Statement* is so important. The *Income Statement* doesn't show the money coming in and out of your bank account. The *Net Profit* at the bottom of your *Income Statement* is not cash you can spend. A fair observation right now might be: 'if the *Income Statement* doesn't show me what I have to spend, I don't see how it can help me manage my business.' The fact is an *Income Statement* is indispensable to a business. The reason is, the *Income Statement* answers an important question –

*If you take the value of all the goods or services you delivered during any given period of time, whether or not you have been paid for them. Then you figure out what it cost you to provide those goods or services, regardless if you actually wrote checks for those costs. NOW: are you making money or are you losing money from the delivery of those goods or services?*

You can see that an answer to this question will tell you a lot about how you are doing! By-the-way, a good *Horse Business Management System* like *equineGenie* does all the work for you and provides the answer. You might not be satisfied with the answer and *equineGenie* is not responsible for the answer, but *equineGenie* will help you solve problems and improve your business – bad to good, good to better, better to best.

The *Income Statement* is divided into two sections: the operating and non-operating sections. The operating section provides information about the goods or services you delivered and expenses associated with those goods or services that are a direct result of your regular business operations. For example, if your business is a horse training business, then the operating section of your *Income Statement* will contain information on the services and expenses involved with providing the training. The non-operating section would provide income and expense information about activities that are not tied directly to your business's regular operation. For example, if your horse training business sold a tractor and some other old equipment, then the associated income and/or expense would be in the non-operating section.

Non-operating income and expense vary depending on the type of business. If your horse business sells into foreign countries, currency exchange is a non-operating activity and could be a gain (income) or loss (expense). If payment is by a bank transfer then the bank transfer cost would be a non-operating expense. The most common types of non-operating expense relate to interest charges or other costs of borrowing. Another non-operating expense example is if you do not manage your *Supplies On Hand (Inventory)* properly and end up throwing some away due to spoilage (Feed) or expiration (Vaccines). A good *Horse Business Management System* like *equineGenie* helps prevent *Inventory* waste. The *Predictive Modeling* and *Resource Optimization* intelligence in *equineGenie's* software logic makes sure you never have too much on hand, but always enough and no waste. This not only influences your profitability, but

conserves your *Cash* – ‘*Cash is King*’ in a horse business. A business may or may not have non-operating income or expense in every *Income Statement* reporting period.

The *Income Statement* is structured to be read in a step-down manner, like walking down stairs.

- *Sales Revenue* – When you provide goods or services to your customers, whether or not you get paid, you record a sale. When all the sales are added up for a given period of time, they are listed as *Sales* on the top line of your *Income Statement*. *Sales Revenue* is net, which means all discounts off list price, returns, and any other deductions are included prior to arriving at your sales revenue. *Sales taxes or any other sales related taxes are not included. Sales revenue is the amount your business should receive to cover its expenses and to provide a profit.*
- *Cost of Goods Sold Expense* – *Cost of Goods Sold (COGS)* are the costs that go into producing the products a company sells. For example, the *COGS* for an automaker would include the material costs for the parts that go into making the car along with the labor costs used to put the car together. The cost of sending the cars to dealerships and the cost of the labor used to sell the car would be excluded. The *COGS* calculation can be complicated and subjective, and is really not necessary in a horse business. Therefore, I would not include *COGS* on a horse business *Income Statement*.
- *Operating Expenses* – When you incur cost to deliver goods or services to your customers, whether or not you have paid yet, you record an expense. When all the expenses are added up for a given period of time, they are listed as *Expenses* below the *Sales* line on your *Income Statement*. *Operating Expense* includes every expense other than *Interest* and *Income Tax*. *Depreciation* is even included in the *Operating Expenses* albeit not a cash outlay. *Depreciation Expense* is a portion of the original cost of a long term asset charged to the *Income Statement* during its reporting period.
- *Interest Expense* – *Interest Expense* is the amount of *Interest* paid on interest bearing liabilities during the *Income Statement* reporting period. Other types of financing charges may be included such as loan origination fees.
- *Income Tax Expense* – *Income Tax Expense* is the total amount of *Tax* due the government (federal and/or state) on the taxable income of a business.

A good *Horse Business Management System* like *equineGenie* will automatically create your *Income Statement*. *equineGenie* uses the *Income* and *Expense Accounts*, and their respective *Subaccounts* identified when the *Chart of Accounts* was setup. The *Sales* and *Expense* associated with delivering your goods or services will be automatically recorded in the correct *Accounts* and *Subaccounts* during the operation of your business. The *equineGenie* system

provides several *Income Statement* reports which include: Year-to-Date; Monthly; last 30 days; Quarterly; last 90 days; Semi-Annually; last 180 days. All formats are provided with or without *Subaccount* detail.

**YDT Income Statement Example without Subaccount detail**

2012 Income Statement YTD					
Category	Description	Subaccount Total	Account Total	Total	% of Net Sales
<b>Revenue</b>					
<b>Sales</b>				\$ 33,199.00	
	4000 - Boarding Income		\$ 14,900.00		
	4100 - Training Income		\$ 7,800.00		
	4250 - Event Income		\$ 200.00		
	4400 - Lesson Income		\$ 3,510.00		
	4500 - Horse Hauling Income		\$ 3,729.00		
	4550 - Farrier Income		\$ 3,060.00		
	<b>Net Sales</b>			\$ 33,199.00	100.00%
<b>Gross Profit</b>				\$ 33,199.00	
<b>Expenses</b>					
<b>Horse Expense</b>				\$ 11,800.43	35.55%
	5350 - Farrier		\$ 2,740.00		
	5500 - Horse, Bedding		\$ 1,068.47		
	5510 - Horse, Grain		\$ 1,134.32		
	5520 - Horse, Forage (Hay)		\$ 6,400.00		
	5630 - Horse, Supplements		\$ 457.64		
<b>Labor Expense</b>				\$ 9,220.00	27.77%
	5140 - Contract Labor		\$ 9,220.00		
<b>Vehicle Expense</b>				\$ 1,886.15	5.68%
	5390 - Fuel, Gasoline		\$ 156.91		
	5400 - Fuel, Diesel Fuel		\$ 750.50		
	5950 - Maintenance, Vehicles		\$ 270.90		
	6330 - Tires		\$ 707.84		
<b>Depreciation</b>				\$ 4,000.00	12.05%
	5180 - Depreciation, Vehicles		\$ 4,000.00		
<b>Total Expense</b>				\$ 26,906.58	
<b>Operating Profit</b>				\$ 6,292.42	18.95%
<b>Non Operating Expenses</b>					
<b>Interest</b>				\$ 2,449.18	7.38%
	5810 - Interest, Mortgage		\$ 2,449.18		
<b>Taxable Income</b>				\$ 3,843.24	11.58%
<b>Income Tax</b>				\$ 576.49	1.72%
	5700 - Income Tax, Federal		\$ 576.49		
<b>Net Profit</b>				\$ 3,266.75	9.84%



### Income Statement Section Example with Subaccount detail

Category	Description	Subaccount Total	Account Total	Total	% of Net Sales
<b>Expenses</b>					
<b>Horse Expense</b>				<b>\$ 11,800.43</b>	<b>35.55%</b>
	<b>5350 - Farrier</b>		<b>\$ 2,740.00</b>		
	5350.001 - Full Set of Shoes	\$ 2190.00			
	5350.002 - Trim	\$ 475.00			
	5350.003 - Front Shoes	\$ 75.00			
	<b>5500 - Horse, Bedding</b>		<b>\$ 1,068.47</b>		
	5500.001 - Pine Shavings - Bales	\$ 1068.47			
	<b>5510 - Horse, Grain</b>		<b>\$ 1,134.32</b>		
	5510.001 - Purina - Omolene 200	\$ 1013.00			
	5510.002 - Purina - Omolene 300	\$ 121.32			
	<b>5520 - Horse, Forage (Hay)</b>		<b>\$ 6,400.00</b>		
	5520.001 - Grass Hay - Elk Mountain	\$ 2100.00			
	5520.002 - Alfalfa Hay - Local	\$ 4300.00			
	<b>5630 - Horse, Supplements</b>		<b>\$ 457.64</b>		
	5630.001 - Dr's Choice Equishine	\$ 147.74			
	5630.002 - Omega Grande	\$ 309.90			
<b>Labor Expense</b>				<b>\$ 9,220.00</b>	<b>27.77%</b>
	<b>5140 - Contract Labor</b>		<b>\$ 9,220.00</b>		
	5140.001 - Barn Cleaners	\$ 6000.00			
	5140.002 - Groomers	\$ 3220.00			
<b>Vehicle Expense</b>				<b>\$ 1,886.15</b>	<b>5.68%</b>
	<b>5390 - Fuel, Gasoline</b>		<b>\$ 156.91</b>		
	<b>5400 - Fuel, Diesel Fuel</b>		<b>\$ 750.50</b>		
	5400.001 - GMC 3500 Truck	\$ 750.50			
	<b>5950 - Maintenance, Vehicles</b>		<b>\$ 270.90</b>		
	5950.001 - Oil Change	\$ 74.95			
	5950.002 - Pack Wheel Bearings	\$ 195.95			
	<b>6330 - Tires</b>		<b>\$ 707.84</b>		
	6330.001 - Truck Tires	\$ 707.84			
<b>Depreciation</b>				<b>\$ 4,000.00</b>	<b>12.05%</b>
	<b>5180 - Depreciation, Vehicles</b>		<b>\$ 4,000.00</b>		
	5180.001 - GMC 3500 Truck	\$ 1000.00			
<b>Total Expense</b>				<b>\$ 26,906.58</b>	

The *Income Statement Section Example with Subaccount Detail* illustrates why it is so important to define your *Chart of Accounts* to match the way you want to track, measure and manage your horse business. For example, just measuring your horse forage would not tell you how much you are spending to feed your horses alfalfa or grass hay. Using *equineGenie* for your *Horse Business Management System* allows you to track, manage and measure how much you are spending on your different feed types, from who you are purchasing your feed, what are you spending with each supplier, what is your supplier's quality and delivery performance, and how much does it cost you to feed each horse on a daily, monthly and annual basis. If you have a Training, Lesson, or Boarding Facility or charge to care for some else's horses, you need this information to know if you are making money or how you can make more money.

However, no matter what your *Income Statement* looks like, remember: It has very little to do with the *Cash* actually coming in and going out of your horse business. The fact is, your *Income Statement* is an abstraction. It's a useful abstraction because it answers the question: Are you making money on the goods or services you provide once you have taken all your costs and expenses into account? But, it isn't real. It doesn't show you how much *Cash* you put in your bank account or how much *Cash* you spent. In fact, if your horse business is a new business or you are expanding your current business, you may be building up Inventory, purchasing new equipment, buying more horses, and in general spending a lot more *Cash* than you are generating. Your income Statement may show you that your business is highly profitable – and all the time you might be running out of *Cash*! Remember the *Cash Ratio (Horsemen's Ratio)* discussed in the first article – '*In an Equine Business Cash is KING*' and '***Profit is an accounting opinion, Cash is fact***'.

This brings us to our next subject, the third important financial document – *Cash Flow*. In my next article we will discuss the *Cash Flow Statement* and how the *Balance Sheet*, *Income Statement* and *Cash Flow Statement* all work together to help us measure and manage the financial performance of our horse business.

To be successful in a horse business does not require a finance education, but it does require an understanding of what your financials are telling you. This understanding will enable you to make better business decisions. A good *Horse Business Management System* will do the calculations for you and analyze and report the results with comments or suggestions. A good *Horse Business Management System* will save you valuable time you can then use to improve your business.



*Think – plan – organize – execute – make/save money.*

Bob Valentine, Ph.D.  
President  
GenieCo, Inc.  
636 E. Eisenhower Blvd., Suite 100  
Loveland, CO 80537  
1.888.678.4364 or 970.231.1455  
bob@genieatwork.com  
[www.equinegenie.com](http://www.equinegenie.com)

*Dr. Valentine taught Equine Business Management to graduating seniors in the Equine Science Department at Colorado State University. He has been involved in the horse business for too long. If you have any questions, you can reach Bob at bob@genieatwork.com, or call him at 1.888.678.4364 or 970.231.1455*