

M.6

Reviewing the Balance Sheet

What is a balance sheet and why should I review it?

A balance sheet is a report generated by a bookkeeping system that shows everything a business **owns**, and everything a business **owes**, and the ownership interest in the business, also known as equity.

Equity is an important measure on the balance sheet; it includes your own money you put into your business, any money you have taken from the business, (either as an owner's draw or by paying a personal expense from your business account) and the value of the what the business has earned or lost since its start.

A balance sheet is a report of what you own and owe at a specific point in time. It should be run on the last day of the month or of the year.

The bank and credit card reconciliations are done for the same date as the balance sheet, because one of their functions is to prove that the cash and credit card balances on the balance sheet are correct.

When reviewing your balance sheet you are looking for any expected or unexpected changes to your cash or equipment accounts (also called asset accounts) or to the amounts you owe (also called liabilities). You are also looking for any transactions that may have been recorded between you and your business (personal money you deposit to your business, draws you take from the business, and personal expenses that may have been paid by the business.)

One of your goals when reviewing your balance sheet should be to think about how much money you have in the bank versus how much you owe, and consider if you are paying down debts as you would like to, or if you might want to take out a loan to help with operating expenses or for equipment.

How do I review my Balance Sheet?

1. Verify the Report Date
 - a. Check the date at the top of the report. This date should be the last day of the prior month
2. Compare Cash Balances
 - a. Locate the balance(s) shown for any business bank accounts.
 - b. Compare these amounts to the balances shown on the bank reconciliation reports you just reviewed. These numbers should be the same. Action required: If they are different, there is a problem. Ask your bookkeeper to explain why the numbers do not agree.
3. Consider other amounts owed to your business
 - a. Think about whether anyone owes your business money for something other than sales of crops or services. This might be for a piece of equipment they bought from you, which would usually be shown as a "Note Receivable" on the top half or first page of your balance sheet. If such an amount is owed but not listed, talk to your bookkeeper about how to record it.
4. Review Equipment and Other Assets
 - a. Look at the numbers shown for equipment and other assets (things that benefit your business for more than one year).
 - b. Do these numbers seem about right? Do they reflect the amount of equipment and other assets you believe your business owns?
 - c. If you do not think the amounts shown accurately reflect your assets, ask your bookkeeper to provide a detailed list of the individual items that make up the balance in your equipment and other asset accounts.
 - i. Remember: Assets should be listed at purchase or acquisition costs, which may be less or more than market value.
If the amounts still don't look correct, find the FarmLink Model Asset List in the Bookkeeping Learning Center for assistance with creating an asset list.
5. Review "Liabilities" section (Amounts Owed to Others)
 - a. These are usually presented in order of how soon they are due.
 - b. If you record "Accounts Payable," you will see that balance first. Consider: Does it look like an amount you expect to see?
 - c. If you have business credit cards, you will see those next. Compare: Do the amounts shown match the amount on the credit card reconciliation you reviewed? If the credit card reconciliation and the amount shown on the

balance sheet do not match most likely they were run on a different date. Either run the reports with the correct date or ask your bookkeeper for an explanation.

6. Review Long-Term Debt

- a. The next item you will see should be any long-term business debt, such as an operating loan or an equipment loan.
- b. Reflect: Do the balances match your expectations of what you owe? Did you expect them to be smaller or larger?
- c. If you have questions, find your most recent statement from your lender and compare it to what is shown on your balance sheet.
- d. If the balances are different, ask your bookkeeper to review what they have recorded and what your lender shows.
- e. Often, the difference between what you expect to see and what you actually see is because of interest. You pay one amount each month, but part of that amount is interest (shown as an expense on your income statement) and part pays down the loan (reducing the loan balance).
- f. If you still have questions, you should ask your lender to help you understand your statement.

7. Review "Total Liabilities"

- a. Locate the subtotal on your balance sheet called "Total Liabilities." This represents all the debts of your business.
- b. Confirm: You should understand everything above this subtotal, or else have a list of questions to ask any items you do not understand.

8. Review Owner's Equity (Personal Money In/Out of Business)

- a. The last section of your balance sheet will include any amounts of your personal money you have deposited into the business, any amounts you have withdrawn from the business, and any personal expenses accidentally paid by the business.
- b. Review this detail to make sure you agree with how the bookkeeper has posted these items.
- c. If you disagree with how any of these items are posted, have a conversation with your bookkeeper to understand why they posted them the way they did and to see if you can agree on how the items should be posted.

9. Final Cash and Debt Assessment

- a. Go back to the top of your balance sheet and look at your total cash, then scan down to Accounts Payable.

- b. Consider: Do you have enough cash to pay the amounts you know will be due in the coming month? If not, what are some things you can do to ensure you will have the cash you need in time to make your payments?
- c. Consider: Have you been taking owner's draws? Can you take more money home from the business? Do you need to re-deposit some of the cash?