

How to get your accounting house in order: a guide for startups

HOME // HOW TO GET YOUR ACCOUNTING HOUSE IN ORDER: A GUIDE FOR STARTUPS

* During Coronavirus, we're flagging up key articles about business planning and marketing. We hope this will help you minimise the impact of the current crisis on your business *

Building a startup can be hard work. And when you're focused on serving your customers and building a product people love, the last thing you want to worry about is accounting. But figuring out the finances and accounting setup for your startup doesn't have to be difficult. In fact, [the Tide team](#) say all you need is a basic understanding of how accounting principles work, and the willingness to find help.

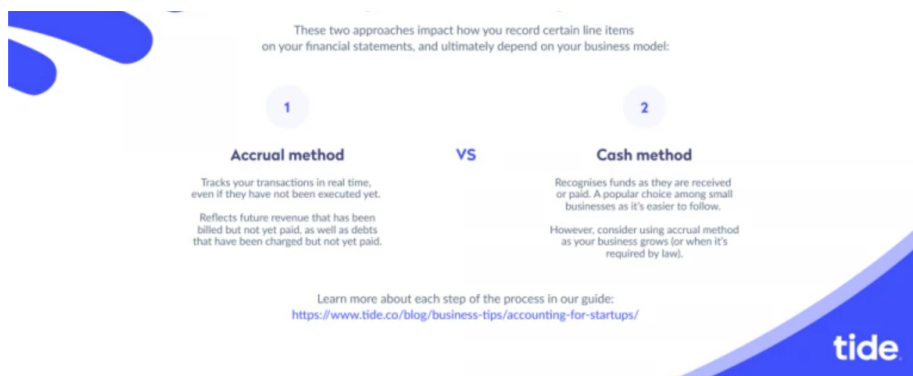


1. Select the right accounting method for your startup

First things first, you need to select an accounting method that's right for you. There are two primary accounting methods, which are:

- **Accrual method** - recognises when you bill clients or owe money to creditors. This method tracks your transactions in real-time, even if payments are yet to be actioned
- **Cash method** - recognises funds only when they are received or paid. Accounts Receivable or Accounts Payable line items don't apply.





For most new businesses and startups, we'd recommend the accrual method. Why? Because managing your finances is easier and, depending on your business model/industry, it's often mandated by law.

Not only that, but accounts receivable and accounts payable will help you keep an eye on transactions, assets and liabilities in real time.

2. Get a solid understanding of these three financial statements

With your accounting method chosen, the next step is to understand the three most common financial statements that you'll come across when running your startup: your balance sheet, income statements and cash flow statement.

Balance sheet

Your balance sheet illustrates the financial health of your business by showing your assets and liabilities.

Here's what this looks like (courtesy of [CFI](#)).

	A	B	C	E	F	G	H	I	J	K	L	M
1	© Corporate Finance Institute. All rights reserved.											
2	Financial Model			2014	2015	2016	2017	2018	2019	2020	2021	2022
77	Balance Sheet											
78												
79												
80	Assets											
81	Cash	81,210	83,715	111,069	139,550	159,474	182,573	190,511	224,399	261,248		
82	Accounts Receivable	5,904	6,567	7,117	7,539	8,179	8,997	9,896	10,758	11,650		
83	Inventory	9,601	9,825	10,531	11,342	15,267	19,343	24,191	26,894	29,772		
84	Current Assets	96,715	100,107	128,717	158,430	182,920	210,913	224,599	262,051	302,670		
85	Property & Equipment	42,350	40,145	38,602	37,521	45,017	51,013	55,811	59,649	62,719		
86	Goodwill											
87	Total Assets	139,065	140,252	167,319	195,951	227,937	261,927	280,410	321,700	365,389		
88												
89	Liabilities											
90	Short Term Debt											
91	Accounts Payable	4,800	4,912	5,265	5,671	7,061	7,952	8,951	9,951	11,016		
92	Current Liabilities	4,800	4,912	5,265	5,671	7,061	7,952	8,951	9,951	11,016		
93	Long Term Debt	50,000	30,000	30,000	30,000	30,000	30,000	10,000	10,000	10,000		
94	Total Liabilities	54,800	34,912	35,265	35,671	37,061	37,952	18,951	19,951	21,016		
95	Shareholder's Equity											
96	Equity Capital	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000	70,000		
97	Retained Earnings	14,265	35,340	62,053	90,280	120,876	153,974	191,459	231,749	274,373		
98	Shareholder's Equity	84,265	105,340	132,053	160,280	190,876	223,974	261,459	301,749	344,373		
99	Total Liabilities & Shareholder's Equity	139,065	140,252	167,319	195,951	227,937	261,927	280,410	321,700	365,389		
100												
101	Check	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000		
102												

Your balance sheet includes your:

- **assets** - items your company owns
- **liabilities** - obligations like short-term debts and taxes
- **equity** - what your business is worth

The formula to calculate balance sheet is **Assets = Liabilities + Equity**.

Income statement

Next is your income statement (also known as profit and loss statement).

It provides a financial snapshot that measures how well your startup is performing, and is considered one of the most important financial statements to keep an eye on regularly.

	A	B	C	D	E	F	G	H	I	J
1	© Corporate Finance Institute. All rights reserved.		Historical Period				Forecast Period			
2	Financial Model		2014	2015	2016	2017	2018	2019	2020	2021
60										
61	Income Statement									
62										
63	Revenue		118,086	131,345	142,341	150,772	165,849	182,434	200,678	218,739
64	Cost of Goods Sold (COGS)		48,004	49,123	52,654	56,710	69,657	78,447	88,298	98,432
65	Gross Profit		70,082	82,222	89,687	94,062	96,193	103,987	112,379	120,306
66	Expenses									
67	Marketing, Advertising & Promotor		22,658	23,872	23,002	25,245	28,194	31,014	34,115	37,186
68	General & Administrative		10,125	10,087	11,020	11,412	15,000	15,000	15,000	15,000
69	Depreciation & Amortization		18,150	17,205	16,544	16,080	7,504	9,003	10,203	11,162
70	Interest		2,500	1,500	1,500	1,500	3,000	3,000	1,000	1,000
71	Total Expenses		53,433	52,664	52,066	54,237	53,699	58,017	60,318	64,348
72	Earnings Before Tax		16,649	29,558	37,622	39,825	42,494	45,970	52,062	55,958
73										
74	Taxes		4,858	8,483	10,908	11,598	11,898	12,872	14,577	15,668
75	Net Earnings		11,791	21,075	26,713	28,227	30,596	33,099	37,484	40,290
76										

Your income statement can be calculated with the formula **Net Income = Revenue – Expenses**.

Net income is an important metric, as it illustrates your bottom line after all expenses (including taxes and cost of sales).

Cash flow statement

Finally, you'll need your cash flow statement.

This shows you how much cash is flowing in and out of your business across a specific period (eg monthly or quarterly).

© Corporate Finance Institute. All rights reserved.		Startup year							Terminal year
		2016	2017	2018	2019	2020	2021	2022	
Balance Sheet Check		OK	OK	OK	OK	OK	OK	OK	
Cash Flow Statement									
Cash from Operations									
	Net Income	(2,573,040)	(1,340,320)	42,855	925,320	2,086,560	3,706,200	4,303,920	
	Depreciation	100,000	120,000	140,000	250,000	300,000	420,000	520,000	
	Changes in non cash working capital								
	Accounts Receivable	52,529	23,456	45,022	68,373	72,976	105,363	68,813	
	Inventory	900,493	154,849	396,740	733,068	786,356	1,084,438	755,290	
	Accounts Payable	880,708	(111,228)	7,108	69,245	285,394	383,178	298,961	
1	Total	(2,545,354)	(1,509,854)	(251,799)	443,124	1,812,621	3,319,576	4,256,808	
Cash Invested									
	Capital Expenditures	500,000	100,000	100,000	550,000	250,000	1,100,000	600,000	
	Acquisitions	0	0	0	0	0	0	0	
2	Total	500,000	100,000	100,000	550,000	250,000	1,100,000	600,000	
Cash from Financing									
	Increase (decrease) in Debt	0	0	0	0	0	0	0	
	Equity Issued (repurchased)	8,000,000	0	0	0	0	0	0	
	Dividends Paid	0	0	0	0	0	0	0	
3	Total	8,000,000	0	0	0	0	0	0	
	Total Cash	4,954,646	(1,809,854)	(351,799)	(106,876)	1,562,621	2,219,576	3,656,808	
	Opening balance	0	4,954,646	3,344,792	2,992,993	2,886,117	4,448,738	6,668,315	
	Increase (Decrease)	4,954,646	(1,809,854)	(351,799)	(106,876)	1,562,621	2,219,576	3,656,808	
4	Closing balance	4,954,646	3,344,792	2,992,993	2,886,117	4,448,738	6,668,315	10,325,123	

Typically, cash flow statements are segmented into three categories:

- **Operations** - activities that contribute to the day-to-day running of your startup
- **Investing** - items and activities that contribute to the growth of your startup
- **Financing** - these are broken down into debt and equity, which highlight activities related to raising investment

Each of these three statements are related, as demonstrated by this illustration from CFI.

Income Statement								
Revenue	102,007	118,086	131,345	142,341	150,772	158,311	165,435	172,052
Cost of Goods Sold (COGS)	39,023	48,004	49,123	53,254	57,310	58,575	61,211	61,939
Gross Profit	62,984	70,082	82,222	89,087	93,462	99,736	104,224	110,113
Expenses								
Salaries and Benefits	26,427	22,658	23,872	23,002	25,245	25,000	25,000	25,000
Rent and Overhead	10,963	10,125	10,087	11,020	11,412	10,000	10,000	10,000
Depreciation & Amortization	19,500	18,150	17,205	16,544	16,080	15,008	15,005	13,003
Interest	2,500	2,500	1,500	900	900	900	900	900
Total Expenses	59,390	53,433	52,664	51,466	53,637	50,908	50,905	48,903
Earnings Before Tax	3,594	16,649	29,558	37,622	39,825	48,827	53,319	61,210
Taxes	1,120	4,858	8,483	10,908	11,598	13,672	14,929	17,139
Net Earnings	2,474	11,791	21,075	26,713	28,227	35,156	38,389	44,071
Balance Sheet								
Assets								
Cash	167,971	181,210	183,715	211,069	239,550	274,339	317,122	328,798
Accounts Receivable	5,100	5,904	6,567	7,117	7,539	7,807	8,158	8,485
Inventory	7,805	9,601	9,825	10,531	11,342	11,715	12,242	12,388
Property & Equipment	45,500	42,350	40,145	38,602	37,521	37,513	32,508	44,505
Total Assets	226,376	239,065	240,252	267,319	295,951	331,374	370,030	394,175
Liabilities								
Accounts Payable	3,902	4,800	4,912	5,265	5,671	5,938	6,205	6,279
Debt	50,000	50,000	30,000	30,000	30,000	30,000	30,000	10,000
Total Liabilities	53,902	54,800	34,912	35,265	35,671	35,938	36,205	16,279
Shareholder's Equity								
Equity Capital	170,000	170,000	170,000	170,000	170,000	170,000	170,000	170,000
Retained Earnings	2,474	14,265	35,340	62,053	90,280	125,436	163,825	207,897
Shareholder's Equity	172,474	184,265	205,340	232,053	260,280	295,436	333,825	377,897
Total Liabilities & Shareholder's Equity	226,376	239,065	240,252	267,319	295,951	331,374	370,030	394,175
Check	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Cash Flow Statement								
Operating Cash Flow								
Net Earnings	2,474	11,791	21,075	26,713	28,227	35,156	38,389	44,071
Plus: Depreciation & Amortization	19,500	18,150	17,205	16,544	16,080	15,008	15,005	13,003
Less: Changes in Working Capital	9,003	1,702	775	903	827	375	611	398
Cash from Operations	12,971	28,239	37,505	42,354	43,480	49,789	52,783	56,676
Investing Cash Flow								
Investments in Property & Equipment	15,000	15,000	15,000	15,000	15,000	15,000	10,000	25,000
Cash from Investing	15,000	15,000	15,000	15,000	15,000	15,000	10,000	25,000

As you can see, the three statements are linked together by specific values:

- the net income line on the income statement is linked to both the balance sheet and the cash flow statement
- the net income line from the balance sheet then feeds into retained earnings for the owner's equity
- finally, on the cash flow statement, the top line for the cash is linked from the operations section

Knowing how each statement connects, as well as the important line items on each statement, will help you measure the financial health of your startup. In turn, you're more likely to make decisions that make you profitable, faster.

3. Hiring an accountant, bookkeeper or both?

No matter where your cash is coming from, you still need to ensure it's contributing to the growth of your startup.

It's important to have a solid grip on the basics of accounting. But as a startup founder, you're already focusing on so many things: creating a great product, hiring the best talent and raising funding.

Which is why it's important to get help, especially in the early days. By recruiting the help of a chartered accountant or bookkeeper, you'll have an expert set of eyes glancing over your accounts.

The question is, should you hire an accountant, bookkeeper or both?

First, let's look at the difference between the two:

- An **accountant** has an extensive knowledge in tax law and financial statements. They can help guide you through complex topics and advise you on key financial decisions.
- A **bookkeeper** takes care of basic financial tasks. These include managing income, expenses and bank reconciliation.

Our recommendation? Seek to find someone who can do both.

These days, many agencies and accounting services will take care of both accounting and bookkeeping tasks, and don't have to cost an arm and a leg.

Getting help early on can save you a host of tax and accounting-related headaches later down the line. At the very least, find someone you can talk to and get advice, no matter where on the fence you sit.

When it comes to startup accounts, using the right technology can also make your life easier. Like a business account that connects with your accounting software and automates many manual tasks. Sound good? [Join Tide today](#) and enjoy your first 100 transactions with zero fees.

ABOUT THE AUTHOR: LAURA WHITE



Laura W is a PR consultant and a trainee Counsellor. An experienced journalist, she interviews entrepreneurs and senior leaders about their business journeys and collaborates with designers, filmmakers, photographers, and marketers to share stories that inspire a reaction.

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Transmit Startups
Northern Design Centre
Abbotts Hill
Baltic Business Quarter
Gateshead, NE8 3DF

✉ info@transmitstartups.co.uk



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