Co-funded by the European Union

#womenBOSSproject

BOSS

WOMEN IN FAMILY BUSINESSES

Heritage Business Strategies for Sustainable Development

Work package 3

Training Programme For Leader Women in Europe Family Businesses

2022-1-SE01-KA220-ADU-000087596

This project has been funded with support from the European Commission. Its content and material reflects only the views of the authors, and the Commission cannot be held responsible for any use which may be made of the information contained therein. Project number: 2020-1-SE01-KA202-077922

CC BY NC

FINANCE

&

ACCOUNTING

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

Content:

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

1. Introduction

In this module, participants will acquire valuable knowledge about entrepreneurship through a first approach to the world of finance and accounting. The contents covered within this module offer a basic introduction to the fundamental aspects of accounting and some financial aspects such as risk management. These are essential prerequisites for understanding more advanced topics. In addition, essential terminology is acquired during this module.

Finance refers to the management of money and the allocation of financial resources. It encompasses activities related to the acquisition, utilization, and management of funds, as well as the analysis and evaluation of financial decisions. Finance involves making decisions about how individuals, businesses, and organizations raise and invest money. It encompasses various aspects, including personal finance, corporate finance, and public finance. It is a broad field with applications in personal finance, business finance, and the overall functioning of the global economy.

Focusing now on **financial management**, this plays a crucial role in the success and growth of small businesses. Understanding the principles of finance is essential for entrepreneurs and business owners **to make informed decisions and effectively manage their financial resources**. Therefore, in this introduction to the world of finance, we will explore the fundamental concepts and practices of financial management that are specifically relevant to small businesses.

At its core, financial management involves the strategic planning, organizing, controlling, and monitoring of financial resources to achieve the organization's objectives. For small businesses, these objectives may include maximizing profits, ensuring liquidity, managing cash flow, securing funding, and optimizing resource allocation.

One of the key aspects is financial planning. This involves creating a comprehensive roadmap that outlines the business's financial goals and strategies to achieve them. It includes forecasting revenues, estimating expenses, and developing budgets to guide financial decision-making. Effective financial planning enables small businesses to allocate resources efficiently and set realistic targets for growth and profitability.

Another critical area of financial management is financial analysis. Business owners need to assess their financial performance regularly to identify strengths, weaknesses, and areas for improvement. Financial analysis involves examining financial statements, such as income statements, balance sheets, and cash flow statements, to gain insights into the business's

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

financial health. By analyzing key financial ratios and trends, business owners can make informed decisions to enhance profitability, manage costs, and optimize their capital structure.

Managing cash flow is a vital aspect. Cash flow refers to the movement of money in and out of the business, including cash inflows from sales, investments, and loans, and cash outflows for expenses, inventory, and debt repayments. Maintaining a healthy cash flow is crucial to meet short-term obligations, fund operations, and seize growth opportunities. Effective cash flow management involves implementing strategies to accelerate cash inflows, delay cash outflows when possible, and maintain adequate reserves to handle unforeseen expenses.

Additionally, financial management encompasses risk management. Small businesses face various financial risks, such as market volatility, credit risk, and operational risk. It is essential for business owners to identify, assess, and mitigate these risks to protect their financial stability and sustainability. This may involve implementing risk management strategies, such as diversifying revenue streams, maintaining insurance coverage, and establishing contingency plans.

Finally, financial management includes making informed investment and financing decisions. Small businesses often require funding for growth, expansion, or working capital. Understanding different financing options, such as bank loans, equity investments, or government grants, and evaluating their costs and benefits is crucial. Furthermore, assessing investment opportunities and evaluating the return on investment (ROI) helps small business owners allocate their resources effectively and make sound investment decisions.

To navigate the world of finance, **it is also necessary to understand five fundamental elements: assets, liabilities, equity, revenue, and expenses**. These play a significant role in assessing the financial health and performance of a business. In the following sections, we will delve deeper into these concepts to provide you with a comprehensive understanding of financial management in the context of small businesses.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

2. Skills & Knowledge Table

The content in this module is linked to the BOSS Competences Framework (WP2) and will offer you introductory information and tools to develop the following skills and knowledge:

CONTENT	LEARNING OUTCOMES	
	SKILLS FOR TARGET GROUP	KNOWLEDGE FOR TARGET GROUP
What is an asset, types of assets, debt to asset ratio, ROA,	Give a definition and distinguish between asset and liability; Know how these two elements relate; Distinguish the different types of assets and liabilities; Know where these two elements fit into the balance sheet; Have a basic knowledge of important ratios in business economics and accounting.	To have knowledge about assets
What are liabilities, Assets vs. Liabilities		To have knowledge about liabilities
Types of equity, Money vs. Capital	Give a definition of equity and know the difference between equity and terms that are misused as synonyms in everyday life	To have knowledge about equity
Type of revenues	Distinguish between different types of costs; Understand revenue streams; Know what is the relation between costs/revenues and how you calculate profit/loss	To have knowledge about revenues
Type of costs, Relationship between Cost and Revenue		To have knowledge about expenses
Accounting and balance sheets		To have a basic knowledge about how works a balnce sheet
Risk management, Risk analysis and assessment, Risk reduction strategies	Risk management	To understand how to manage risks, through systematic activities such as identification, measurement, assessment, treatment of risk.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

3. Finance & Accounting

3.1. Assets Liabilities

At the end of the session, participants will be able to

- give a definition and distinguish between asset and liability;
- Know how these two elements relate;
- Distinguish the different types of assets and liabilities;
- Know where these two elements fit into the balance sheet;
- Have a basic knowledge of important ratios in business economics and accounting.

3.1.1 Assets

What Is an Asset?

An asset is a resource with economic value that an individual, corporation, or country owns or controls with the expectation that it will provide a future benefit. Assets are reported on a company's balance sheet. They're classified as *current, fixed, financial,* and *intangible*. They are bought or created to increase a firm's value or benefit the firm's operations.

Calculating assets is a simple way for a small business owner to know if they can repay their debts while also giving an idea of the organization's overall health. At the same time, a potential lender would also look into what assets in accounting a company has. The lender looks at these assets to know if they can be used as leverage or guarantee for a new loan.

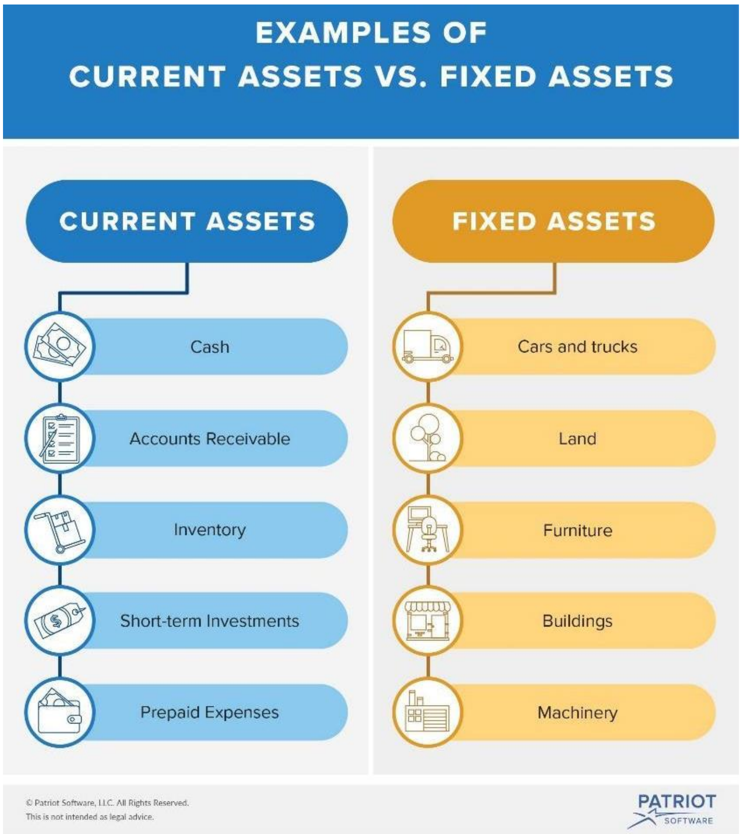
Types of Assets

Assets can be broadly categorized into different types based on their characteristics and nature:

- Current Assets: are short-term economic resources that are expected to be converted into cash or consumed within one year. Current assets include cash and cash equivalents, accounts receivable, inventory, and various prepaid expenses.
- Fixed assets: also known as property, plant, and equipment (PP&E), are resources with an expected life of greater than a year and are not intended for resale. Examples include land, buildings, machinery, vehicles, and furniture. An accounting adjustment called depreciation is made for fixed assets as they age. It allocates the cost of the asset over time.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596



- Financial assets: are intangible assets that derive their value from a contractual claim or ownership right. They represent a legal or ownership interest in an entity and can be traded in financial markets. Financial assets include stocks, sovereign and corporate bonds, preferred equity, and other, hybrid securities. Financial assets are valued according to the underlying security and market supply and demand.
- Intangible assets: are economic resources that have no physical presence. They include intellectual property, brand names, patents, copyrights, trademarks, goodwill, and software. These assets often contribute to a company's competitive advantage and can generate long-term economic benefits. Accounting for intangible assets differs depending on the type of asset. They can be either amortized or tested for impairment each year.

3.1.2 Focus 1: Debt to asset ratio

The debt-to-asset ratio is a financial metric that measures the proportion of a company's total debt to its total assets. It is a figure that provides insight into the level of leverage or indebtedness of a company and indicates the extent to which its assets are financed by debt. The ratio is a sort of percentage. A higher rate of debt to asset ratio means that a more significant number of an organization's assets are purchased through debts. This could be

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

problematic for a business. This can cause the company to be at a higher risk of filing bankruptcy or insolvency. On the other hand, a lower ratio indicates a lower level of debt relative to the company's assets, which may signify a more conservative financial position. However, it is always crucial to consider other financial indicators and conduct a comprehensive analysis before making conclusions or investment decisions based solely on this ratio.

The formula to calculate its ratio is:

$$\textbf{Debt-to-Asset Ratio} = \frac{\boldsymbol{Total\ Debt}}{\boldsymbol{Total\ Assets}}$$

Where:

- Total Debt: This represents the sum of all the company's outstanding debts, including short-term and long-term liabilities. It includes items such as bank loans, bonds, lines of credit, and any other forms of borrowing.
- Total Assets: This refers to the sum of all the company's assets, which can include current assets (such as cash, inventory, and accounts receivable) and fixed assets (such as property, plant, and equipment), as well as intangible assets (such as patents or trademarks).

Example 1: A small business organization has total liabilities of €2000 and total assets of €4000
€2000 / €4000 = 0.5 or 50%.
This means that the organization has a debt to asset ratio of 50 percent.

Example 2: Let's consider a fictional company called ABC Inc.
ABC Inc. Financials: Total Assets: €1,000,000 and Total Liabilities: €400,000

Debt-to-AssetRatio=0.4 or 40%

The debt-to-asset ratio for ABC Inc. is 40%, indicating that 40% of the company's assets are financed by debt. This ratio is a measure of financial leverage, and in this case, it suggests that a significant portion of ABC Inc.'s assets is funded by liabilities.Furthermore, a debt-to-asset ratio of 40% means that, for every euro of assets, ABC Inc. has €0.40 in debt.

3.1.3 Focus 2: Return on assets (ROA)

ROA is a financial ratio that measures a company's profitability relative to its total assets. It provides an indication of how efficiently a company is utilizing its assets to generate profits. ROA is calculated by dividing the net income (typically obtained from the company's income statement) of a company by its total assets.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

The ROA formula tells how much profit is generated after tax for each euro held in assets. ROA can be calculated as it follows:

$$\textbf{ROA} = \frac{\textbf{\textit{Net Income}}}{\textbf{\textit{Total Assets}}}$$

The result is usually expressed as a percentage. A higher ROA indicates that a company is generating more profits per unit of assets, which suggests efficient asset utilization and better profitability. Conversely, a lower ROA implies lower profitability or less effective utilization of assets.

Note that ROA should be interpreted in conjunction with other financial ratios and factors to gain a comprehensive understanding of a company's financial health and performance.

Example: If a company has a net income of €75000 and the average assets are worth €400,000, then the ROA will be €75000 / €400,000. This is 0.18 or 18%.

3.2 Liabilities

What are liabilities?

In accounting and finance, a liability refers to an obligation or debt owed by an individual, company, or organization to another party. It represents a present or future sacrifice of economic resources that is expected to result in an outflow of assets or settlement of a financial obligation.

The most common type of corporate and small business liability is monetary debt. Recorded on the right side of the balance sheet, liabilities include loans, accounts payable, mortgages, deferred revenues, bonds, and accrued expenses.

While liabilities generally have a negative connotation since they involve debts or obligations, they are a normal and necessary part of business operations and financing.

Liabilities are a vital aspect of a company because they are used to finance operations and pay for large expansions. They can also make transactions between businesses more efficient.

Liabilities are typically classified as current liabilities or non-current liabilities based on their expected repayment timeframe. Current liabilities are usually considered short-term (which must be paid within 12 months) and non-current liabilities are long-term (which are due in more than one year's time). There also are contingent liabilities which only need to be paid under certain circumstances.

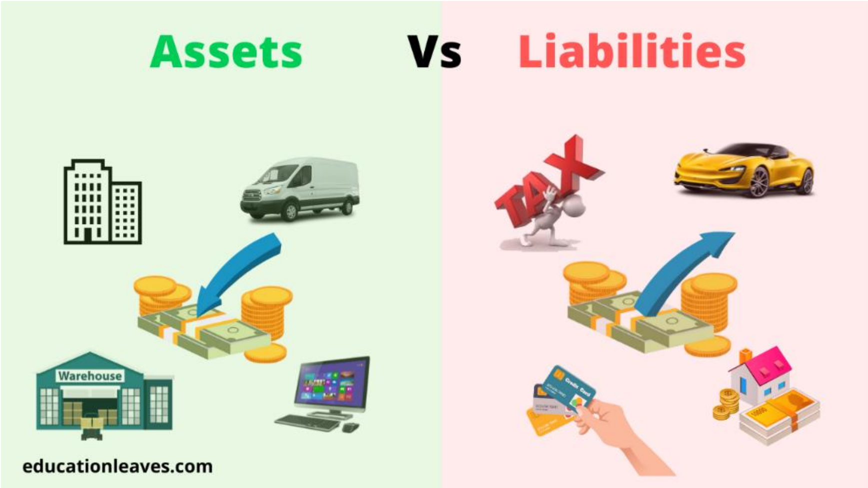
Examples of current liabilities include accounts payable (amounts owed to suppliers), short-term loans, accrued expenses (e.g., wages, taxes), and current portion of long-term debt;

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

while examples of non-current ones include long-term loans, bonds payable, lease obligations, and deferred tax liabilities.

3.2.1 Assets vs. Liabilities: How Do They Relate?



Liabilities refer to things that you owe or have borrowed; assets are things that you own or are owed. Assets represent a net gain in value, while liabilities represent a net loss in value. A standard accounting equation pits the total assets of a company against its total liabilities, and investors use this ratio of assets vs. liabilities to place a valuation on the company. Assets and Liabilities are recorded on the balance sheet, which is one of the financial statements that provides a snapshot of a company's financial position at a specific point in time. On a standard balance sheet, total assets are listed on the left side of the page. Depending on accounting procedures, this list of assets may include both current assets and long-term assets. The right side of the page contains different types of liabilities, both short-term and long-term.

3.3 Equity

At the end of the session, participants will be able to:

- know the meaning of equity
- know the difference between equity and terms that are misused as synonyms in everyday life

Equity, which can be found on a company's balance sheet, holds several key meanings and implications. Firstly, it signifies the value that would be distributed to shareholders if the company's assets were sold off and all debts were settled during a liquidation event. In the context of an acquisition, equity refers to the sales value of the company minus any

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

liabilities that were not transferred with the sale. Moreover, equity can also represent the book value of a company and is a fundamental piece of information utilized by analysts to evaluate the overall financial health of a business.
Equity can also help you assess the overall value of a business. The equity equation (assets minus liabilities) provides a clear and easily comprehensible representation of the company's financial situation for investors and analysts alike. Equity is considered a long-term source of funding for businesses and it serves as the capital raised by a company, which is subsequently used for asset acquisition, project investments, and operational funding. Companies typically raise capital by issuing debt (such as loans or bonds) or equity (by selling stocks). Investors are generally attracted to equity investments because of the greater possibility of participating in the company's profits and growth.
In the context of a company, equity holds significance because it denotes the value of an investor's ownership stake in a company, which is determined by the proportion of shares held. Owning stock in a company gives shareholders the potential for capital gains and dividends. Additionally, equity ownership provides shareholders with the right to participate in voting on corporate actions and board of director elections. These ownership benefits foster ongoing interest and engagement from shareholders. Thus, equity can determine the value of each individual share in a company, which helps shareholders decide whether to invest in a company.

Equity is important because it helps determine whether a company is financially stable. In fact, shareholder equity can either be positive or negative. A positive value indicates that the company possesses sufficient assets to cover its liabilities. Conversely, a negative value signifies that the company's liabilities surpass its assets, which, if sustained over time, is regarded as balance sheet insolvency. Typically, investors perceive companies with negative shareholder equity as risky or unsafe investments. However, it is important to note that shareholder equity alone does not offer a definitive measure of a company's financial health. When used in conjunction with other tools and metrics, it enables investors to accurately assess the organization's overall financial condition.

3.3.1 Types of equity

There are two common types of equity used by businesses: Owner's equity and Shareholder's equity. The first one refers to the company owner's control in the company. Sole proprietors and business partners commonly use this type of equity. Owner's equity can highlight how much available capital a business has. Shareholder's equity, also called stockholder's equity, refers to the number of assets shareholders have in a company after deducting all liabilities. Businesses structured as corporations often use this type of equity.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

Shareholder's equity can show you how much money is available for shareholder distribution.

3.3.2 Equity vs Capital vs Money

We have just learnt what equity is, but we need to learn more about the difference with capital and money, equally important concepts for finance and economics, each however with distinct characteristics and roles.
While equity and capital have some similarities, there are key differences between these two terms that are important for successful business owners to know to ensure financial success for their companies. Instead of focusing on the overall value of a company as equity does, capital focuses on the financial resources available to conduct daily business operations. In fact, capital is a broader term that refers to financial **resources currently available** and used to generate income or wealth. It encompasses both equity and debt. In the context of a business, capital represents the **total funds** invested in the company, which can be used for various purposes such as purchasing assets, financing operations, and expanding the business. Capital can come from multiple sources, including equity investments from shareholders and debt financing from loans or bonds. Capital is crucial for businesses to generate profit and foster growth. While equity plays a role in determining a company's long-term financial stability, capital is instrumental in assessing whether a company can cover the immediate costs associated with the production of goods and services.

Much confusion in economics results from the common practice of referring to money as capital. Money is a medium of exchange, a unit of account, and a store of value. It is a widely accepted form of payment for goods, services, and debts. Money facilitates transactions and serves as a measure of economic value. It can exist in various forms, such as physical cash (coins and banknotes) and digital money (bank account balances, electronic transfers). Money is typically issued by governments or central banks and is regulated by monetary policies. Unlike equity and capital, money does not represent ownership in an asset or a company but rather serves as a means of facilitating economic activities.

In summary, equity represents ownership in an asset or a company, capital refers to the financial resources used to generate income, and money serves as a medium of exchange in economic transactions. While equity and capital are closely related and often used interchangeably in the context of business financing, money plays a distinct role as a universal medium of exchange in the economy.

3.4 Cost And Revenues

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

By the end of the session participants will:

- Distinguish between different types of costs
- Understand revenue streams
- Know what is the relation between costs/revenues and how you calculate profit/loss

My favorite things in life don't cost any money. Its rally clear that most precious resource we all have is time. As it is, I pay a price by not having much of a personal life.
Steve Jobs, 1985

Cost and revenue are key financial elements that play a crucial role in determining the profitability and financial performance of a business. Let's explore the relationship between cost and revenue. In production, research, retail and accounting, a **cost** is the value of money that has been used up to produce something, and hence is not available for use anymore.

3.4.1 Different types of costs:

- Manufacturing Costs vs. Non-manufacturing Costs

  Manufacturing Costs are those costs that are directly involved in manufacturing of products/services. Examples of manufacturing costs include raw materials costs and charges related to workers. Manufacturing cost are usually divided into: cost of material, labor cost, manufacturing cost. Non-manufacturing Costs are those costs that are not directly incurred in manufacturing a products/services. Examples of such costs are salary of sales personnel and marketing expenses. Generally non-manufacturing costs are classified into Selling and distribution costs, administrative costs.

- Direct costs vs. Indirect costs

  A direct cost is the material, labor, expense or distribution cost associated with producing a product. It can be accurately and easily traced to a product, department or project. For example, suppose a worker spends eight hours building a car for a car manufacturing company. The direct costs associated with the car are the wages paid to the worker and the parts used to build the car. On the other hand, an indirect cost is an expense unrelated to producing a good or service. An indirect cost cannot be easily traced to a product, department, activity or project. For example, a semiconductor company rents office space in a building and produces microchips. The wages paid to the workers and the materials used to produce the microchips are direct costs. However,

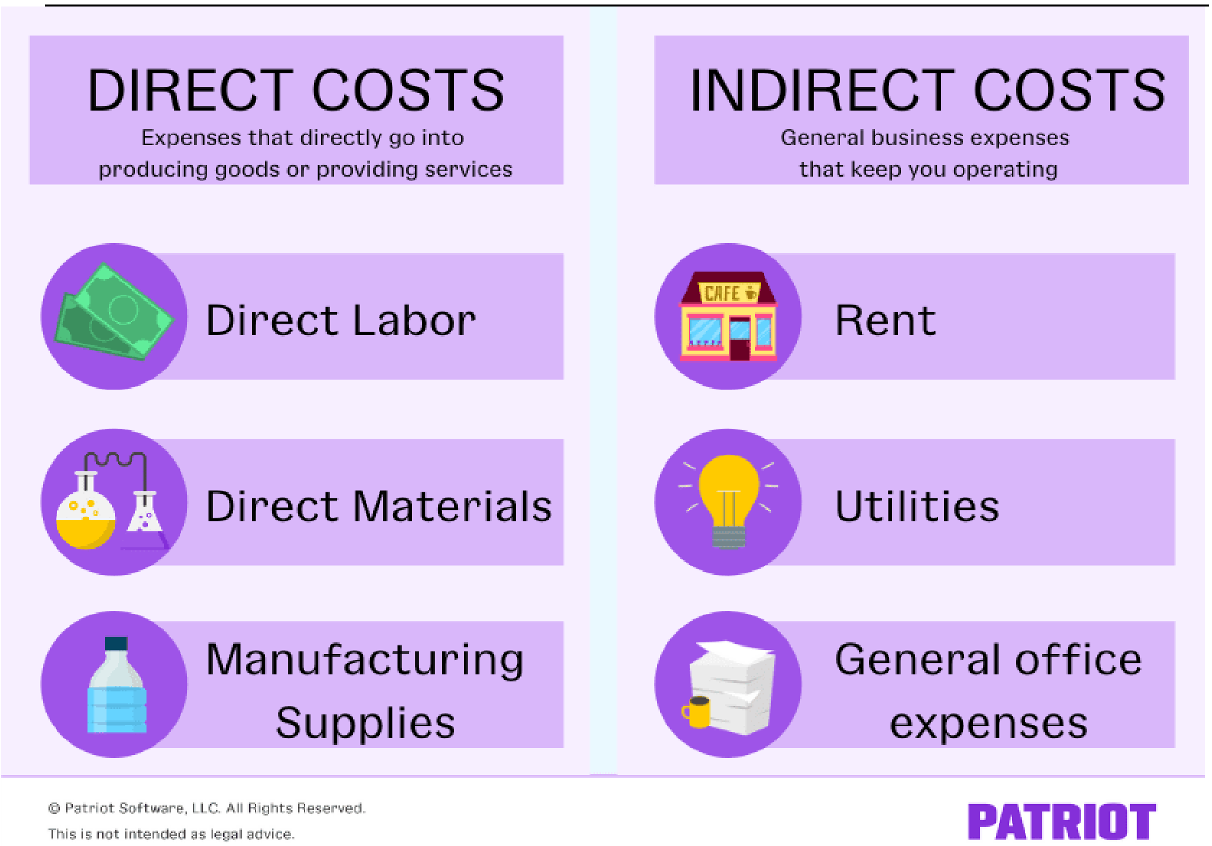
Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

the electricity used to power the entire building is considered an indirect cost because it appears on one bill and is difficult to trace back to the semiconductor company.

- Variable costs vs. Fixed costs

A fixed cost does not vary with the number of goods or services a company produces. For example, suppose a company leases a machine for production for two years. The company has to pay €2,000 per month to cover the cost of the lease. The lease payment the company pays per month is considered a fixed cost. Contrary to a fixed cost, variable cost fluctuates as the level of production output changes. This type of cost varies depending on the number of products a company produces. A variable cost increases as the production volume increases, and it falls as the production volume decreases. For example, a toy manufacturer must package its toys before shipping products out to stores. This is considered a type of variable cost because, as the manufacturer produces more toys, its packaging costs increase. However, if the toy manufacturer's production level is decreasing, the variable cost associated with the packaging decreases.



Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

3.4.2 Revenues

Revenue is the amount of money that is brought into a company by its business activities. In the case of government, revenue is the money received from taxation, fees, fines, inter-governmental grants or transfers, securities sales, mineral rights and resource rights, as well as any sales that are made. Revenue represents the income generated by a business from its primary operations, such as the sale of goods or services. It is the total amount of money received or receivable by a company from its customers. Key components of revenue include:

- Sales Revenue: This is the primary source of revenue for most businesses and represents the income from the sale of goods or services.
- Other Revenue: This includes income from secondary sources, such as interest earned, rent received from property leases, licensing fees, or royalties.

Revenue is a crucial indicator of a business's financial performance. By analyzing revenue trends and patterns, businesses can evaluate their market position, customer preferences, and the effectiveness of their sales and marketing strategies.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

A **revenue stream** is one form of revenue. Revenue streams refer specifically to the individual methods by which money comes into a company.

Investopedia, 2015

Common classification of revenues is on: Operating revenue and Non- Operating revenue. Operating revenue is any revenue derived from the company's main business, such as the sale or service of its products. Royalty revenue, money received from licensing rights the company grants, is also commonly considered as being part of operating revenue. Non-operating revenue is revenue that does not originate from the company's operation of its primary business activity, but from some secondary income source.

3.4.3 Relationship between Cost and Revenue

The relationship between cost and revenue directly impacts the profitability of a business. The objective is to generate revenue that exceeds the associated costs, resulting in a profit. Understanding this relationship is vital for effective financial management. Here are a few scenarios:

- Profit: When revenue exceeds the total cost incurred (including both fixed and variable costs), the business generates a profit. This is the desired outcome for sustainable operations.
- Breakeven: Breakeven occurs when revenue matches the total costs, resulting in zero profit or loss. It represents the point at which a business covers all its expenses without making a profit.
- Loss: If the cost exceeds the revenue, the business incurs a loss. This situation indicates that adjustments may be needed, such as reducing costs, increasing prices, or improving operational efficiency. By analyzing the relationship between cost and revenue, businesses can identify areas where costs can be optimized, revenue can be increased, or pricing strategies can be adjusted to enhance profitability.

Overall, businesses need to carefully manage their costs and optimize revenue generation to ensure financial sustainability and long-term success. Regular monitoring, analysis, and strategic decision-making are essential to maintain a healthy balance between cost and revenue.

3.4.3 Exercise

Try to calculate what are your total transportation costs of coming to the school/office/meeting? Once you get the final amount then find out who has the highest and who the lowest. Make a plan that the total transportation cost for the next meeting will be lower than those from today.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

3.5 Basic Accounting

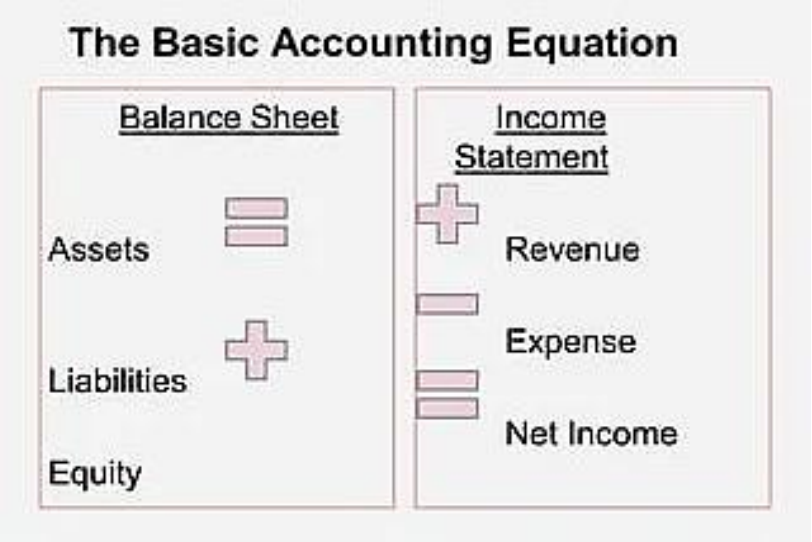
Basic accounting refers to the fundamental principles and concepts used to record, summarize, and report financial transactions of a business or organization. It involves the process of identifying, measuring, analyzing, and communicating financial information to stakeholders.

A balance sheet is a financial statement that provides a snapshot of a company's financial position at a specific point in time. It presents the company's assets, liabilities, and shareholders' equity, also known as net assets or owner's equity. The balance sheet follows the fundamental accounting equation:

- **Assets = Liabilities + Shareholders' Equity**

An income statement, also known as a profit and loss statement or P&L statement, is a financial statement that summarizes the revenues, expenses, and net income or loss of a company over a specific period. It provides a snapshot of the company's financial performance and indicates whether the company has generated a profit or incurred a loss.

The income statement provides valuable insights into a company's revenue generation, cost structure, and profitability. It helps assess the financial performance of a company over a specific period and is often analyzed in conjunction with other financial statements, such as the balance sheet and cash flow statement, to gain a comprehensive understanding of the company's financial health.



Here are some tips for basic accounting that can help you understand and manage your financial records effectively:

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

- Understand Basic Accounting Concepts: Familiarize yourself with the fundamental accounting concepts, such as the double-entry system, debits and credits, accrual accounting, and the basic financial statements. This knowledge will provide a solid foundation for your accounting practices.
- Establish a Chart of Accounts: Create a chart of accounts specific to your business. It should include relevant categories and accounts to properly classify and track your financial transactions. This will help you organize and maintain accurate records.
- Maintain Proper Documentation: Keep all relevant source documents, such as invoices, receipts, bank statements, and financial contracts. This documentation serves as evidence for your financial transactions and helps ensure accuracy and transparency in your records.
- Implement a Consistent Recording System: Establish a regular schedule for recording your financial transactions. This can be done daily, weekly, or monthly, depending on the volume and complexity of your business activities. Consistency in recording transactions helps maintain up-to-date and accurate financial records.
- Separate Personal and Business Finances: It's crucial to keep your personal and business finances separate. Maintain separate bank accounts and credit cards for your business transactions. This separation simplifies accounting and provides a clear picture of your business's financial performance.
- Check your Bank Statements: Regularly reconcile your bank statements with your accounting records. This process ensures that all transactions are accurately recorded, identifies any discrepancies or errors, and helps maintain the integrity of your financial data.
- Monitor Cash Flow: Keep a close eye on your cash flow by tracking your incoming and outgoing funds. This helps you understand your business's liquidity and enables you to manage your cash effectively.
- Find an accountant and/or use accounting software: Consider using accounting software to streamline your accounting processes. These tools automate many tasks, such as recording transactions, generating financial statements, and facilitating financial analysis. Choose software that is suitable for your business size and needs.
- Seek Professional Assistance: If you're unfamiliar with accounting or have complex financial requirements, consider consulting with an accountant or bookkeeper. They can provide valuable guidance, assist with complex transactions, and ensure compliance with accounting standards and regulations.
- Continuously Educate Yourself: Accounting practices and regulations can evolve over time. Stay updated with accounting principles, tax laws, and financial reporting standards relevant to your business. Attend workshops, seminars, or online courses to enhance your accounting knowledge.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

Remember, while these tips can be helpful, it's essential to consult with a professional accountant or bookkeeper to ensure accurate financial records and compliance with applicable laws and regulations.

Useful tools

Here are some user-friendly apps/tools in English designed to simplify the process of compiling financial statements, even for users with limited accounting knowledge.

QuickBooks: a widely used accounting software that simplifies financial management for small to medium-sized businesses.

Website: QuickBooks

Xero: a cloud-based accounting solution known for its user-friendly interface, offering features like invoicing, expense tracking, and budgeting.

Website: Xero

FreshBooks: a cloud-based accounting software designed for small businesses and freelancers, with intuitive features for invoicing and expense management.

Website: FreshBooks

Wave: a free online accounting software that is easy to use and suitable for small businesses. It includes basic features for invoicing and financial tracking.

Website: Wave

Zoho Books: a comprehensive online accounting solution with user-friendly features for managing transactions, invoicing, and financial reporting.

Website: Zoho Books

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

3.6 Risk Management

"In a world that's changing so quickly, the biggest risk you can take is not taking any risk."

Peter Thiel, entrepreneur/venture capitalist, 2004

Risk management is the process of identifying, assessing, and prioritizing risks to minimize the negative impact they may have on an organization or project. It involves analyzing potential risks, determining their likelihood and potential consequences, and developing strategies to mitigate or handle them effectively.

Entrepreneurs take risks because they're necessary to start and grow a business. Some of the risks an entrepreneur might face include:

- Leaving a full-time job and steady paycheck
- Using personal savings with no guarantee of a return on investment
- Misjudging interest in a product or service
- Putting trust in coworkers
- Giving away time, energy, sleep, the ability to enjoy personal interests, etc.

It's important to note that while entrepreneurs are willing to take risks, they also engage in risk management strategies to mitigate potential downsides and increase the likelihood of success. They conduct market research, develop business plans, seek expert advice, and continuously evaluate and adapt their strategies to minimize risks while maximizing opportunities.

Entrepreneurs take risks for several reasons, as risk-taking is often inherent to the entrepreneurial mindset and the pursuit of business opportunities. Here are some key reasons why entrepreneurs are willing to take risks:

- Pursuit of Innovation and Opportunity: Entrepreneurs are often driven by the desire to create something new, innovative, and valuable. They identify opportunities in the market, gaps in existing products or services, or emerging trends and are willing to take risks to capitalize on these opportunities.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

- Potential for High Rewards: Risk and reward are closely linked. Entrepreneurs understand that taking calculated risks can lead to significant rewards, both in terms of financial gains and personal satisfaction. They are willing to step outside their comfort zones and invest resources, time, and effort in the hopes of achieving substantial returns.
- Autonomy and Independence: Many entrepreneurs are motivated by the desire for autonomy and independence. They want to be their own boss, set their own direction, and have control over their destiny. Starting a business and taking risks allows them to pursue their own vision and build something that aligns with their values and goals.
- Personal Growth and Learning: Entrepreneurs often view risk-taking as a means of personal growth and learning. By taking risks, they expose themselves to new challenges, experiences, and opportunities for learning. Even if they encounter failures or setbacks, these experiences contribute to their personal and professional development.
- Competitive Advantage: Taking risks can provide entrepreneurs with a competitive advantage in the marketplace. By being willing to venture into unexplored territories or embrace disruptive ideas, entrepreneurs can differentiate themselves from competitors and position themselves as industry leaders.
- Overcoming Fear and Uncertainty: Successful entrepreneurs are not paralyzed by fear or the fear of failure. Instead, they embrace uncertainty and view it as an opportunity for growth and success. They understand that risk is an inherent part of business and are willing to face the unknown to achieve their goals.
- Impact and Legacy: Entrepreneurs often have a strong desire to make a positive impact and leave a lasting legacy. They believe in their ideas and their ability to create change. By taking risks, they aim to build businesses that can transform industries, solve societal problems, or improve the lives of others.

Risks can be classified as:

1. Competitive risk: losing business to similar service or product providers
2. Credibility risk: getting consumers to trust and be interested in a product or service with no brand recognition
3. Financial risk: having the cash flow needed to stay in operations
4. Market risk: knowing whether or not a product or service is what the market demands
5. Technology risk: facing business operations interruptions due to technology failure, or choosing a technology that is not the best for the busines

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

3.6.1 Risk analysis and assessment

Risk analysis: Identify the causes of each identified risk and assess the consequences of its materialization.
Risk assessment: The most widely used risk assessment method: measuring the likelihood of a risky event occurring, and the possible impact it might have on the organization.

The probability (P) of the occurrence of the risk varies (impossibility - certainty), being expressed on a scale with five levels: Very low - it is unlikely to happen for a long time (3-5 years); has not happened so far; Low - is unlikely to happen for a long time (3-5 years); has happened very few times so far; Medium - it's likely to happen for an average time (1-3 years); has happened several times over the last 3 years; High - is likely to happen over a short period of time (<1 year); has happened several times in the last year; Very high - it is very likely to happen over a short period of time (<1 year); has happened many times in the last year.

Impact (I): the consequences that the risk may have if it materializes; is expressed on a scale of five values: Insignificant - with very low impact on activities and objectives and/ or without financial impact; Minor - with low impact on activities and objectives and/ or with very low financial impact; Moderate - with medium impact on activities and objectives and/ or with medium financial impact; Major - major impact on major activities and objectives and/ or major financial impact; Critical - with significant impact on activities and objectives and/ or with significant financial impact.

Risk Index: used for risk assessment; resulting in the probability of materializing a risk, and its impact:

Risk Index = Probability x Impact (also Risk level)

The risk index takes values between 1 - 25. The value of the Risk Index is then represented on the Risk Matrix. The first step is to assign a numeric value from 1 to 5, 1 being the lowest, for each of the categories under Probability and Impact. Then, use the formula of multiplying the value of the Probability to the value of Impact to determine the Risk Level.

- **1-4: Acceptable** – no further action may be needed and maintaining control measures is encouraged
- **5-9: Adequate** – may be considered for further analysis
- **10-16: Tolerable** – must be reviewed in a timely manner to carry out improvement strategies

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

- **17-25: Unacceptable** – must implement cease in activities and endorse for immediate action

5x5 Risk Matrix Example

Impact
How severe would the outcomes be if the risk occurred?

Probability
What is the probability the risk will happen?

	Insignificant 1	Minor 2	Significant 3	Major 4	Severe 5
5 Almost Certain	Medium 5	High 10	Very high 15	Extreme 20	Extreme 25
4 Likely	Medium 4	Medium 8	High 12	Very high 16	Extreme 20
3 Moderate	Low 3	Medium 6	Medium 9	High 12	Very high 15
2 Unlikely	Very low 2	Low 4	Medium 6	Medium 8	High 10
1 Rare	Very low 1	Very low 2	Low 3	Medium 4	Medium 5

SafetyCulture

3.6.2 Risk reduction strategies

Risk reduction strategies are proactive measures taken by individuals, entrepreneurs or organizations to mitigate potential risks and minimize the negative impact they can have.

- Risk Avoidance: Risk avoidance involves completely avoiding activities or situations that pose significant risks. This strategy is applicable when the potential risks outweigh the potential benefits, and it aims to eliminate the possibility of negative outcomes. For example, a company may choose not to enter a high-risk market or discontinue a product or service with a high liability risk.
- Risk Transfer: Risk transfer involves shifting the financial burden or responsibility of potential risks to another party. This can be achieved through insurance policies, contracts, or outsourcing. By transferring risk, individuals or organizations limit their exposure to potential losses. For instance, purchasing liability insurance can transfer the risk of potential legal claims to an insurance provider.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

- Risk Reduction:Risk reduction strategies aim to minimize the likelihood or severity of potential risks. This can be done through various means, such as implementing safety protocols, improving security measures, conducting regular maintenance and inspections, or implementing quality control processes. By reducing risks, individuals or organizations decrease the probability of adverse events occurring.

It's important to note that risk reduction strategies should be tailored to specific contexts and risks faced by individuals, businesses, or organizations. A comprehensive risk management approach involves assessing risks, prioritizing mitigation efforts, and implementing a combination of appropriate strategies to address potential threats effectively.

Risk assessment tools - app

https://www.capterra.com/sem-compare/risk-management-software/

4. Suggestions for solo-entrepreneur (self employed and small business)

Effectively managing finances in a solo-entrepreneur or small business involves establishing clear financial boundaries. Start by utilizing a dedicated business bank account and credit card to separate personal and business expenses. Create a realistic budget, updating it regularly to reflect changes and ensure financial stability. Prioritize tax planning by setting aside a portion of income for taxes and seeking advice from a tax professional. Building a three to six months' emergency fund acts as a financial cushion for unexpected expenses. Ensure timely invoicing, offer discounts for early payments, and diligently follow up on late payments to maintain a healthy cash flow. Regularly monitor cash flow, anticipating and planning for seasonal or market fluctuations. Seek professional advice from an accountant or financial advisor regularly to stay informed about best practices and make informed financial decisions for the sustained success of your solo business.

Key points:

- **Separate Finances:** Use a dedicated business bank account and credit card.
- **Budgeting:** Create and regularly update a realistic budget.
- **Tax Planning:** Set aside funds for taxes; consult with a tax professional.
- **Emergency Fund:** Build a three to six months' emergency fund.
- **Invoice Management:** Invoice promptly, offer discounts, and follow up on payments.
- **Cash Flow Monitoring:** Regularly review cash flow and plan for fluctuations.

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

- **Professional Advice:** Consult with an accountant or financial advisor regularly.

5. More Materials

5. 1 Videos

https://www.youtube.com/watch?v=bgp_AAxUJpQ
https://www.youtube.com/watch?v=tRaEOYvmBmA

5.2 Further readings

Books:

1. Osterwalder, A., Pigneur, Y., & Clark, T. (2010). Business model generation: a handbook for visionaries, game changers, and challengers. Hoboken, USA: Wiley.
2. Nagy, T., Tacer, B. (2018) Teaching entrepreneurship in schools : an experiential approach. Ljubljana: STEP Institute.
3. Aven, T., & Renn, O. (2009). On risk defined as an event where the outcome is uncertain. Journal of Risk Research, 12, pp. 1–11.
4. Bandle, T. (2007). Tolerability of risk: The regulator's story, in F. Boulder, D. Slavin, R. Lofstedt (Eds.), The tolerability of risk: A new framework for risk management, London, Earthscan.
5. Campbell, S. (2005). Determining overall risk. Journal of Risk Research, 8, pp. 569–581.
6. Hopkin, P. (2010). Fundamentals of risk management, Kogan Page.
7. HSE. (2001). Reducing risk protecting people, London, Health and Safety Executive.
8. ISO. Risk management vocabulary. ISO/IEC Guide 73.
9. Kaplan, S.; Garrick, B. J. (1981). On the quantitative definition of risk. Risk Analysis, 1(1), 11–27.
10. Project Management Institute (2000). A Guide to the Project Management Body of Knowledge, Newton Square, USA.

Pages:

http://www.investopedia.com/ask/answers/041415/what-are-different-types-costs-cost-accounting.asp

http://www.investopedia.com/ask/answers/010915/what-types-revenue-are-taxable.asp

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

https://online.wharton.upenn.edu/blog/is-risk-taking-behavior-key-to-entrepreneurial-spirit/

https://www.investopedia.com/ask/answers/040615/what-risks-does-entrepreneur-face.asp

https://entrepreneurscan.com/blog/risk-taking-in-business/

How to Prepare a Balance Sheet: 5 Steps | HBS Online

How to Read & Understand a Balance Sheet | HBS Online

Learning to Read Balance Sheets | Article – HSBC Business Go

6. Conclusion

In conclusion, this module has provided participants with a foundation in the realm of entrepreneurship and its intersection with finance and accounting. It has equipped learners with essential knowledge to navigate the intricate world of finance, setting the stage for deeper exploration into more advanced topics.

The module has introduced the crucial concepts of assets, liabilities, equity, revenue, and expenses, providing a fundamental framework for assessing the financial health and performance of a business. These elements will serve as building blocks for further exploration in the subsequent sections of this course. Lastly, the discussion of risk management has shed light on the need for business owners to proactively identify, assess, and mitigate various financial risks. This proactive approach helps protect the long-term stability and sustainability of their ventures.

In essence, participants have gained a fundamental understanding of finance and accounting as essential tools for entrepreneurial success. Armed with this knowledge, they are well-prepared to delve deeper into the intricacies of financial management and make informed decisions that will drive the growth and prosperity of their small businesses. This module marks the first step on their journey toward financial expertise and entrepreneurial excellence.

7. Bibliography

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

Assets In Accounting, Identification, Types and Learning How To Calculate Them (deskera.com)

What Is an Asset? Definition, Types, and Examples (investopedia.com)

Assets vs. Liabilities: Examples of Assets and Liabilities - 2023 - MasterClass

Liability: Definition, Types, Example, and Assets vs. Liabilities (investopedia.com)

Equity Definition: What it is, How It Works and How to Calculate It (investopedia.com)

Equity vs. Capital: What's the Difference? | Indeed.com

The Difference Between Money and Capital in the American Economy (mic.com)

Direct vs. Indirect Costs | Breakdown, Examples, & Why it Matters

Direct Costs and Indirect Costs , Cost Classification - projectcubicle

https://www.slideshare.net/MaMaMoore/basic-accounting-explained-pdf

https://safetyculture.com/topics/risk-assessment/5x5-risk-matrix/;

https://en.wikipedia.org/wiki/Risk_matrix

Funded by the European Union. Views and opinions expressed are however those of the author(s) only and do not necessarily reflect those of the European Union or the European Education and Culture Executive Agency (EACEA). Neither the European Union nor EACEA can be held responsible for them.

2022-1-SE01-KA220-ADU-000087596

Co-funded by
the European Union

BOSS

WOMEN IN FAMILY BUSINESSES

HERITAGE BUSINESS STRATEGIES FOR SUSTAINABLE DEVELOPMENT

https://bossproject.eu/

This project has been funded with support from the European Commission. Its content and material reflects only the views of the authors, and the Commission cannot be held responsible for any use which may be made of the information contained therein. Project number: 2020-1-SE01-KA202-077922

BY NC