

NC-SARA - Welcome

Financial Responsibility Compliance and Planning: Balance Sheets

Tuesday, February 4, 2020

Please Note:

- **The webcast will begin at the top of the hour.**
- **There is no audio being broadcast at this time.**

NC-SARA - Logistics

Welcome!

Please use the **Question and Answer** box for questions.

The webcast will be recorded.

This PowerPoint and any other resources referenced will be emailed next week to all who registered and available on our website.

Presenters

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Financial Responsibility Compliance and Planning: Balance Sheets

NC-SARA

February 4, 2020

Balance Sheet Basics

- ▶ Snapshot of a company's financial position at a single point in time
- ▶ Illustrates a business's net worth
- ▶ Reflects financial resources and obligations
- ▶ Useful in evaluating financing options

Balance Sheet Basics - Assets

- ▶ Assets are the means used to operate a company
- ▶ Current assets
 - ▶ Lifespan of one year or less
 - ▶ Can be converted easily to cash
 - ▶ Typically reflected in order of liquidity
 - ▶ Cash and cash equivalents
 - ▶ Accounts receivable due within 12 months
 - ▶ Inventory
 - ▶ Prepaid expenses

Balance Sheet Basics - Assets

- ▶ Non-Current assets
 - ▶ Lifespan of more than one year
 - ▶ Not turned into cash easily
 - ▶ Examples
 - ▶ Accounts receivable due more than 12 months in the future
 - ▶ Property and equipment, net of accumulated depreciation
 - ▶ Intangible assets
 - ▶ Goodwill
 - ▶ Tradenames
 - ▶ Accreditation

Balance Sheet Basics - Liabilities

- ▶ Financial obligations owed to outside parties
- ▶ Current liabilities
 - ▶ An obligation that will come due, or must be paid, within one year
 - ▶ Typically reflected in order of obligation
 - ▶ Accounts payable
 - ▶ Refunds payable
 - ▶ Debt payments due within one year
 - ▶ Accrued expenses
 - ▶ Deferred revenue that will be earned within one year
 - ▶ Deferred rent

Balance Sheet Basics - Liabilities

▶ Non-Current liabilities

- ▶ Debts and other non-debt financial obligations which are due after a period of at least one year
- ▶ Examples
 - ▶ Debt payments due more than 12 months in the future
 - ▶ Deferred revenue that will be earned more than 12 months in the future
 - ▶ Deferred rent or tenant improvement obligations

Balance Sheet Basics - Equity

- ▶ Total amount of assets that investors will own after payment of all debts and liabilities (Assets = Liabilities + Equity)
- ▶ Indicates the amount of funds retained in the business
- ▶ Components of Equity
 - ▶ Capital/Common stock – initial equity contributions from owners
 - ▶ Retained earnings – accumulated net income from operations retained by the company
 - ▶ Additional paid-in capital – additional capital contributions from owners

Intangible Assets

- ▶ Goodwill and other intangibles with an indefinite life (tradenames)
 - ▶ Amount the purchase price exceeded the fair value of assets and liabilities at the date of purchase
 - ▶ Must evaluate for impairment annually
 - ▶ May elect to amortize over 10 years
 - ▶ Any impairment will be an expense in the period the impairment was determined
- ▶ Intangibles with a definite life
 - ▶ Must be amortized over the estimated life
 - ▶ May be impaired

Deferred Rent and Tenant Improvement Allowances

- ▶ Deferred rent
 - ▶ Results from escalating rent and free rent periods
 - ▶ Monthly/annual rent expense calculated as total of rent payments ÷ total number of months/year in lease term, including free rent periods
 - ▶ Cumulative amount that expense exceeded cash payments
- ▶ Tenant Improvement Allowance Liabilities
 - ▶ Results from amounts received from landlord for improvements to leased space
 - ▶ Amortized over the life of the lease
 - ▶ Amortization reduces rent expense

Types of Transactions

- ▶ Equity purchase
 - ▶ Purchase of stock (transaction between owners)
 - ▶ No significant effect on the financial statements
 - ▶ Not the most common type of transaction for schools
- ▶ Asset purchase
 - ▶ Purchase of specified assets and liabilities
 - ▶ Assets and liabilities recorded at fair value
 - ▶ Goodwill recorded for the amount the purchase price exceeds the fair value of assets and liabilities purchased
 - ▶ Most common type of transaction for schools

Common Financial Ratios

- ▶ Acid test (Quick ratio)
 - ▶ $\text{Cash and AR} \div \text{current liabilities}$ (1 to 1)
 - ▶ Indicates assets that can quickly be turned into cash to meet current obligations
- ▶ Current ratio
 - ▶ $\text{Current assets} \div \text{current liabilities}$ (1 to 1)
 - ▶ Relationship of current assets to current liabilities
- ▶ Working capital
 - ▶ $\text{Current assets} - \text{current liabilities}$
 - ▶ Indicates whether the company will be able to meet its current obligations

Common Financial Ratios

- ▶ Debt-to-Equity ratio
 - ▶ Total liabilities ÷ shareholder's equity
 - ▶ Ratio of what is owed to what is owned
 - ▶ Indicates the extent of the company's dependency on debt
- ▶ Tangible positive net worth
 - ▶ Equity minus intangible assets
 - ▶ Represents total value of physical assets net of liabilities
 - ▶ Approximates liquidation value of a company
 - ▶ Department of Education also excludes unsecured related party receivables

Problem Indicators

- ▶ Current ratio of less than 1 to 1
- ▶ Acid test ratio of less than 1 to 1
- ▶ Working capital deficit
- ▶ Negative tangible net worth
- ▶ High debt to equity ratio – dependent on debt

Important Disclosures

- ▶ Description of purchase transaction
- ▶ Calculation of goodwill or other intangibles
- ▶ Future commitments
 - ▶ Lease agreements
 - ▶ Debt service
- ▶ Restricted assets

Examples

The background features abstract geometric shapes. On the right side, there are overlapping shapes in teal, gold, and light blue. A thin white line runs diagonally across the lower right portion of the image.

**ABC School
Balance Sheet
DATE**

ASSETS

Current Assets

Cash	\$ 925,000
Cash held in escrow	100,000
Accounts receivable, students, net	324,000
Employee advances	2,500
Accounts receivable, related party, unsecured	<u>125,000</u>
Total Current Assets	<u>1,476,500</u>

Property and Equipment

Furniture	30,000
Computers	31,000
Medical equipment	<u>100,000</u>
Total Property and Equipment	<u>161,000</u>

Other Assets

Security deposits	10,000
Goodwill	<u>2,950,000</u>
Total Other Assets	<u>2,960,000</u>

TOTAL ASSETS **\$ 4,597,500**

LIABILITIES AND MEMBERS' EQUITY

Current Liabilities

Accounts payable	\$ 30,000
Prepaid tuition	<u>158,000</u>
Total Current Liabilities	<u>188,000</u>

TOTAL LIABILITIES 188,000

Members' Equity

4,409,500

TOTAL LIABILITIES AND MEMBERS' EQUITY **\$ 4,597,500**

Quick ratio	6.64
Current ratio	7.85
Working capital	1,288,500
Tangible net worth	4,597,500
Debt-to-equity	0

XYZ, LLC
Balance Sheet
July 01, 2017

ASSETS				
Current Assets				
Cash	\$	316,000	Quick ratio	1.24
Accounts receivable, students		870,000	Current ratio	1.31
Inventory		47,000	Working capital	295,000
Prepaid expenses		21,000	Tangible net worth	(3,495,000)
Total Current Assets		1,254,000	Debt-to-equity	6.13
Property and Equipment				
Furniture, fixtures and equipment		189,000		
Leasehold improvements		71,000		
		260,000		
Other Assets				
Goodwill		4,100,000		
Capitalized loan costs		100,000		
Total Other Assets		4,200,000		
TOTAL ASSETS		\$ 5,714,000		
LIABILITIES AND MEMBER'S EQUITY				
Current Liabilities				
Current portion, notes payable	\$	273,000		
Unearned tuition		686,000		
Total Current Liabilities		959,000		
Noncurrent Liabilities				
Notes payable, net of current portion		4,050,000		
TOTAL LIABILITIES		5,009,000		
Member's Equity		705,000		
TOTAL LIABILITIES AND MEMBER'S EQUITY		\$ 5,714,000		

Acid test = .65 to 1
 Current ratio = .69 to 1
 Working capital = (15,088)
 Tangible net worth = 11,162
 Debt to equity = -0-

Assets	
Current assets:	
Cash	\$ 26
Restricted cash	726
Student accounts receivable, net	21,323
Other receivables	10,134
Prepaid expenses and other	1,160
Total current assets	33,369
Property and equipment, net	29,283
Intangible assets, net	9,087
Other long-term assets	213
Total assets	\$ 71,952
Liabilities and Net Assets	
Current liabilities:	
Accounts payable	\$ 5,641
Accrued liabilities	4,884
Unearned tuition	36,519
Advance payments	1,413
Total current liabilities	48,457
Other long-term liabilities	3,246
Total liabilities	51,703
Net Assets:	
Net assets without donor restrictions	20,202
Net assets with donor restrictions	47
Total net assets	20,249
Total liabilities and net assets	\$ 71,952

Balance Sheet – Example 3



Questions?

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