THE GOOD NEWS:
Your business is growing by leaps and bounds!

THE BAD NEWS:
Your business is growing by leaps and bounds!

THE LESSON:
Speed kills!

The comments at the left are the key messages that NASE business expert Gene Fairbrother delivers about rapid business growth.

“While the first thing that comes to mind when a business closes its doors is that they didn’t have the customers to generate enough revenue to survive, there is another edge to the sword,” says Fairbrother. “Failure can also occur when a business grows too fast and the company can’t handle it.”
“The inexperienced business owner is the most susceptible to growing too fast,” he warns. They might not have industry or management experience and all they see is the dollar signs. The attitude is, “If I can pay my bills, I must be making money.” But this not necessarily true. The common denominator seen in almost all of these cases is the failure of the small business owner to produce and understand financial statements. Most small businesses find out if they made a profit once a year when they prepare their taxes. Financial statements should be produced at least quarterly, although Fairbrother recommends monthly statements.

Today’s financial accounting programs such as Quickbooks can generate balance sheets and profit/loss statements from the information that you input during the month. If you don’t have this software or don’t understand the financial statements produced, then it is money well spent to speak with an expert. The NASE has a team of experts who can help members with these matters.

So what are the warning signs that your business is growing too fast? Fairbrother says knowing you financial position will help you see the signs. “If you have lots of revenue, but small profits or even losses or you can’t pay providers on time, you may be taking on too much, too fast,” he says. “Also look for severe highs and lows in cash flows.”

Fairbrother recommends looking at customer satisfaction as a monitor as well. He warns: “If customer complaints are on the rise because you are promising products or services you can’t deliver, it may be that growth has exceeded the capacity of your staff and ability to pay providers.” That equals growth that is too rapid and can result in lost customers and providers, as well.

Another sign that the business is growing too quickly is employee burnout. Is your staff becoming over-stretched because you are trying to do too much with too few employees? Also look to see how you feel about your business. Have things gotten so overwhelming and busy at the office that you dread going in? Maybe it is time to realize that things are growing too quickly.
PREPARE FOR THE BEST AND THE WORST
The best way to avoid the disaster of rapid growth is to plan for it. Most small businesses live in the “here and now” and do not have a growth strategy written down. It is very important for all business to think 12-18 months into the future so they can plan their growth and anticipate their needs at that time.

KNOW YOUR FINANCES
Knowing your financial situation at any given moment is the easiest way to prepare for growth. This will let you know what your working capital is, what profit/losses are, and how much cash is available. This information is also very important to lenders. “It is important to establish financial relationships and sufficient lines of credit before

KNOW YOUR FINANCIAL STATEMENTS
There are three main financial statements for small businesses. They are: (1) balance sheets, (2) income statements, and (3) cash flow statements. Balance sheets show what a company owns and what it owes at a fixed point in time. Income statements show how much money a company made and spent over a period of time. Cash flow statements show the exchange of money between a company and the outside world also over a period of time.

The most important financial statements for most small business owners are the balance sheet and the income statements.

BALANCE SHEET
A balance sheet provides detailed information about a company’s assets, liabilities and owners’ equity.

Assets are things that a company owns that have value. This typically means they can either be sold or used by the company to make products or provide services that can be sold. Assets include physical property, such as plants, trucks, equipment and inventory. It also includes things that can’t be touched but nevertheless exist and have value, such as trademarks and patents. And cash itself is an asset. So are investments a company makes.

Liabilities are amounts of money that a company owes to others. This can include all types of obligations, such as money borrowed from a bank to launch a new product, rent for use of a building, money owed to suppliers for materials, payroll a company owes to its employees, environmental cleanup costs, or taxes owed to the government. Liabilities also include obligations to provide goods or services to customers in the future.

Owners’ equity is sometimes called capital or net worth. It’s the money that would be left if a company sold all of its assets and paid off all of its liabilities. This leftover money belongs to the owners of the company.

INCOME STATEMENT
An income statement, also called a profit and loss statement, is the most common and important financial report a business can produce and should be done monthly to show not only that particular month’s profit picture, but also its year-to-date profit picture. It is a report that shows how much revenue a company earned over a specific time period. An income statement also shows the costs and expenses associated with earning that revenue. The literal “bottom line” of the statement usually shows the company’s net earnings or losses. This tells you how much the company earned or lost over the period.

If total expenses exceed total revenues, a net loss is reported. Revenues are not necessarily the same as collections from customers and expenses are not necessarily the same as payments to suppliers. As a result, net income normally does not equal the net cash generated by operations. The cash a company has is noted in the cash flow statement.

These statements need not be difficult to produce or interpret. Many accounting software programs automatically generate them. If you are not sure how to interpret them, it is a worthwhile investment to speak with a professional who can guide you.
you need them,” says Fairbrother. Once the line of credit is established it will revolve as the company borrows and repays it.

As growth happens, some other financial questions to answer include: Is our pricing on target? Do we understand the true cost of each sale? What products and clients are most profitable (and which ones are actually losing money)? How will new investments affect future cash flows?

Finally, watch your money carefully. Rapid growth is a precarious balance of making and spending money, and using it wisely. Now is probably not the time to take a luxury vacation or buy a new house. You need to find a balance of spending on the company (not yourself), but you don’t want to bring in a ton of fresh capital only to sit on it. Use a portion of it to provide the tools and resources to your employees to aid in the growth process.

PEOPLE POWER

One of the most important aspects to manage for your business and for growth is the people. Establishing the culture of your business and then hiring people who buy into your culture will help during growth periods.

Human productivity is at the heart of business growth, so you want employees who fit into your business’s culture so that during times of turmoil, such as rapid growth, everyone is grounded in the culture. Many business experts agree that it is more important to hire people who fit the culture than it is to hire the candidate with the most impressive resume.

Once you have hired the right people for the culture, be sure to reinforce it by orienting new employees in a consistent engaging way, positively reinforcing behavior that exemplifies the desired values, over-communicating company values, and holding people accountable for behaviors that are out of sync with core values.

If rapid growth sneaks up on your business, don’t keep it a secret. Communicate with your staff. Fairbrother recommends holding weekly production and management meetings. Your staff is likely to respond more favorably if you inform them what is going on and what new or added roles they may have to take on during this period. They may also be able to provide feedback and ideas that can help the business navigate through the growing pains.

RESOURCE PLANNING

During rapid growth, a company may realize that portions of its infrastructure are no longer adequate to handle the task. Telephone systems, computers, software, and other office equipment may not be able to handle the increased capacity. Websites may not be able to keep up to date or handle increased traffic and sales. It may be necessary to upgrade these systems to keep the business running smoothly.

Resources should also be made available to staff. During a tumultuous time of growth it is important that staff is supported. If they have bought into the company culture, then they want to be there, so don’t let them get burned out during growth. Bonuses or overtime pay can help ease the burden for employees.

Temporary help may also be necessary to get through a period of rapid growth. Fairbrother says, “Outsource to trained resources instead of trying to fast-track tasks in-house that may be outside the skill or comfort zone of current employees, such as accounting and marketing.” The more you can assist your staff, the more likely they are to handle the growth.
FOCUS ON CUSTOMER SERVICE
You are in business because of customers, so it is critical to stay customer focused. What they experience when they do business with you determines if they become a repeat customer. When operations are overwhelmed by waves of new business, remember that a positive customer experience is at the heart of every healthy venture. Invest resources—capital, people, technology, training, etc.—to be sure you deliver on your promises.

It may be tempting to court only the new customers during a rapid growth period, but don’t forget to pay attention to established clients. They may be the first to notice a decline in customer service and complain about the lack of service and support. Any complaints from customers should be addressed immediately and employees trained to prevent further issues.

As hard as it may be at the time, sometimes it is also necessary to say no to new customers to slow growth to controllable levels. Saying no now to an order that you cannot deliver may disappoint a customer, but it will be far less disappointing to them than if you could not fulfill a promise.

GROWTH AHEAD
Growth should be the goal of small businesses. Having a solid grasp of the company’s financial situation should be the first step preparing for it. All businesses should create a quarterly business and growth plan and then review and revise the plans as each quarter passes. With that, there is a way to measure if goals are being met and the proper finances and resources are in place. If you are uncertain of how to formulate a plan or work through the finances, get outside professional help, such as the NASE business consultants, in building a plan to meet growth.

Sallie Hyman writes on small business issues and owns and operates her own small business in Purcellville, Virginia.
Ask The Experts

Determining Reasonable Salaries for an S Corporation

Q: My wife and I own a limited liability corporation. We just elected to be treated as an S corporation. We are trying to determine salary levels, and I read something about how the owner’s salary must be greater than employee’s for S corporations to minimize the chance of an IRS audit. What criteria should we use to establish our salaries.

A: The key for the S corporation and the audit issues are not that an owner’s salary must be higher than an employee or any other ratio type analysis but only that the wages be “reasonable” in connection with the services provided. The underlying economics of the situation will always be the key factor in the reasonableness of the wage payments.

When we talk about reasonable compensation, most of us think of the big New York bankers or investment brokers and we talk about how much they make and think that it is unreasonable because the wages are so high. The S corporation issue is the reverse. The concern in the eyes of the IRS is that the wages are too low and therefore intentionally avoiding payroll taxes, FICA, Medicare, etc.

You should find some third-party support for the wages you pay yourself for the work you and your wife do. For example, is that an hourly wage that is common for people who do what you do? Is there a trade association or membership for your industry that does a salary survey of your type of job? Are there other people in other companies doing what you do and, if so, what do they earn? Providing some third-party support for the wage you choose is the key to answering the IRS question if they ever actually ask it of you.

Keep in mind that there is no process or decision or safe harbor that will prevent or even materially decrease your chances of being audited. So concentrate on the underlying economics of your situation, always consider the support for “reasonable” salaries, document your decisions, and then just be successful and let everything else take care of itself.

Keith Hall, NASE Tax Expert
Gary Gygi is president of Gygi Capital Management, an investment advisory firm in Cedar Hills, Utah that he founded in 2003. The company caters to high net worth individuals, corporations and institutions. He has been managing money since 1989 and before starting his company he spent 15 years as an investment advisor and management executive for Morgan Stanley. He is also the mayor of Cedar Hills and has been a NASE member since 2003.

What inspired you to start your business?
I come from a very entrepreneurial family so being an entrepreneur came naturally to me. I am doing the same type of work now as I was when I worked for Morgan Stanley, but I have taken the next step and I can now make strategic and financial decisions for myself and I am free of certain limitations that I had while working for a Fortune 500 company.

Sometimes people may find themselves self-employed because they are forced there but most of us do it by choice. Many of my friends are happy with their regular jobs and that is great for them. But it’s not great for me. I want to be compensated for how hard I work. People who are entrepreneurial thrive on going out and creating their own destiny.

What key lessons did you learn during your time at Morgan Stanley that helped you in setting up your business?
I learned a lot of lessons in terms of how our business operates. When you go out on your own you will always make mistakes. The experience I had at a large company helped minimize the number of mistakes.

What differentiates your company from other investment advisory firms?
Most investment firms want to put you in a box and their investment strategies are set up that way. They have already determined what type of box they want you to have. We try to develop an investment strategy based on each person’s goals and needs. No one likes to be put into a box, so I think that is the biggest difference.

How do you market your business?
There are several ways. One is by word of mouth – I use my clients for referrals. I have also developed “centers of influence” and contacts such as accountants and attorneys, and we refer business to each other.
I also have more media exposure than any investment advisor in Utah. That has helped my business a lot. When talking with corporations, institutions or high net worth individuals there is better than a 50 percent chance they have seen me on TV or heard me on the radio and are comfortable about how I think and what I do, so that has helped a lot.

To gain this exposure, entrepreneurs need to develop relationships with people in the media. The media needs to fill time and they need to write stories on financial topics. If you have developed a relationship and make yourself accessible and give good interviews, they will come to you directly. It takes time to develop those relationships but it does help.

My company is also very active in social media but we are careful to not be overly promotional. We want to be perceived as credible. I have a blog and I also make comments on LinkedIn, Facebook, and Twitter. I comment on the economy and the markets and deliver information that is helpful. It enhances your credibility when you deliver valuable information.

**What challenges have you faced in your business? How have you overcome them?**

You have to wear a lot of hats. You have to be really good at time management. I spend time on a number of activities such as research, portfolio management, compliance, sales, marketing, etc. We are going to expand and hire people to take on some of those responsibilities. I am really disciplined about things that I have to do. There are reports that need to be done. Not procrastinating is a big deal. You have to make little bits of time to do things every day so when you get to the end of the week or the month you are not so burdened with a project that you should have been doing a little bit at a time all the way along.

In addition to running your business you are also the mayor of Cedar Hills, Utah. How does your experience as a self-employed person help you in this position?

Being in the private sector adds a skill set not often found in the public sector, which is a motivation to turn a profit if possible. The private sector is all about turning a profit and the public sector is more about providing services so my private sector experience helps me take care of taxpayer dollars entrusted to me.

**What’s the best thing about being self-employed?**

Everything. The flexibility of being able to create your own schedule is a big thing. I can go see my son in a baseball game or watch my daughter do a performance. You always know you have to get things done, but if you are entrepreneur you are going to be motivated.

**What’s the best compliment you’ve ever received from a client?**

We have helped a lot of clients and a lot of them are appreciative and say thank you. But one client made a point of coming to me and said, “You changed my life. There were things we didn’t think we would be able to do but you helped us with our finances and now we can do them.”

**Which NASE member benefit is most important to you?**

The ability to be able to go to professionals in the organization for legal and accounting advice. I use them as a resource on questions such as how to structure my business. It makes it easy for someone just getting started in a business to dash off an email and get an email back in a couple days that helps them make a good decision.
In early May 2014, the District of Columbia (DC) City Council unanimously supported PR20-0744 — Health Benefit Exchange Authority Financial Sustainability Emergency Declaration Resolution of 2014, enacting a 1 percent tax on all health-insurance carriers with gross receipts of $50,000 or more within the District of Columbia.

Since the passage of the Affordable Care Act (ACA), the NASE has proactively engaged in its implementation in order to ensure that our members — and the millions of self-employed and micro-businesses nationwide — have access to comprehensive and affordable health care coverage. However, we believe the decision by the DC City Council is counterproductive and ultimately hurts those individuals who would benefit the most from being able to access comprehensive and affordable health care coverage.

The request by the DC Health Benefit Exchange Authority for the city to find revenue to ensure the solvency of the Exchange undermines the purpose of the state-based exchange model. On several occasions the NASE, along with many other organizations, expressed concern to District and Exchange officials that the city did not have the demographics to support a state-based exchange. This fact became evident when the Exchange Authority put forth rules (which received approval from the DC City Council) that would require every DC-based small business with 50 or fewer employees to purchase their health care in the Exchange.

NASE does not believe it is unreasonable to assume this 1 percent tax on health-insurance carriers will be immediately tacked on to the premium costs paid by the policyholder. Given the estimated fluid nature of the health insurance premium marketplace and continued concerns and efforts by the self-employed and micro-business community to contain costs, this additional tax is unwelcome and counterproductive to achieving the Authority’s goals.

We also believe that the decision to tax “all health insurance carriers” and not just those operating within the DC Exchange could be in violation of the law and could result in a costly lawsuit that the District of Columbia will have to defend.

The NASE supports the proactive nature of the Council to be good stewards of the District’s fiscal health while balancing the commitment to the DC Health Benefit Exchange Authority. However, the NASE will hopes that the DC City Council will engage in a thoughtful process to address our concerns and ensure that no business owner is unfairly taxed out of operating within the District of Columbia.

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