

Create a Balance Sheet and Income Statement



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- The information in this material is not intended as tax or legal advice. Please consult legal or tax professionals for specific information regarding your individual situation.
- The content herein was developed from sources believed to be providing accurate information.
- All investing is subject to risk, including the possible loss of the money you invest.
- All final investment and planning decisions are the discretion of the client.

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Course Pre-Requisites

This is the first course recommended among the Personal Financial Planning Education offerings.

Introduction

Balance Sheets and Income Statements, in conjunction with Budgets, are key tools to assess your current financial situation.

I always recommend the establishment of up-to-date Balance Sheets and Income Statements as early steps when building a Financial Plan.

These tools will be the basis for your financial plan and will be crucial to help you understand your plan's outlook and to make informed decisions when analyzing “what-if” scenarios.

Discussion Topics

1. Terms and Definitions
2. Balance Sheet and Income Statement Uses
3. Interesting Facts
4. Balance Sheet Example
5. Income Statement Example
6. Balance Sheet and Income Statement Maintenance
7. Resources
8. Questions / Discussion

Terms and Definitions

1. Balance Sheet: for an individual or family, this document summarizes assets, liabilities, and net worth at a specific point in time. Along with an income statement and budget, the balance sheet is one of the three core financial reports used to assess an individual's or family's financial standing. This document is also referred to as a Statement of Financial Position or Net Worth Statement.
2. Income Statement: for an individual or family, this document summarizes income, expenses and net cash flow for a past period (typically a month, 3 months or 12 months). Similar in structure to a budget, the income statement is based on income and expenses that have already occurred.
3. Budget: a spending plan defining projected income and expenses. Similar in structure to an Income Statement, a budget is based on projections of FUTURE income and expenses and the resultant FUTURE cash flow.
4. Asset: something containing financial value or future benefit. Examples include cash, CDs, money market accounts, stocks and bonds, mutual funds, pensions and annuities, life insurance cash values, personal property (home, car, RV, jewelry), retirement accounts, rental properties.
 - A. Liquid Asset: an asset that is easily traded, such as cash, mutual funds, most stocks, bonds.
 - B. Illiquid Asset: an asset that may require time (or a penalty) to exchange for cash value, such as a house, collectibles, retirement plan savings, etc..
5. Liability: debts and financial obligations. Examples include loan balances (home, auto, student, other), lines of credit, lease obligations, accrued (unpaid) taxes, credit card balances.

Terms and Definitions

- 6. Net Worth: the amount of assets minus the amount of liabilities.
- 7. Income: money received for labor or as a return on an investment. We tend to use three general categories of income, aligned with taxation factors:
 - A. Earned income: salary, wages, tips, commission, bonuses.
 - B. Portfolio income: dividends and capital gains earned on invested assets.
 - C. Passive income: interest income, royalties, rent and certain types of owner's equity.
- 8. Expenses: services and products that you pay for. Examples include rent, utilities, daycare, insurance, monthly mortgage payments, monthly car payments, food and entertainment, clothing, taxes, transportation (gas, maintenance, parking, tolls), travel and recreation, subscriptions, gifts, etc.
- 9. Cash Flow: this is calculated by subtracting expenses for a given period from income for that same period.

A **positive** cash flow denotes a surplus of money exists at the end of the measured period of time; a **negative** cash flow indicates that more money is being spent than is being earned during the measured period of time.

A **positive** cash flow can be used to INCREASE net worth; a **negative** cash flow will DECREASE net worth.

Balance Sheet / Income Statement Uses

Balance Sheet

1. Assess your overall financial health. Key metric: is your Net Worth growing over time?
2. The basis for your financial plan. Understand asset utilization and allocation, and manage debt.
3. Typically required for a loan application or certain types of investments (partnerships, etc.).
4. Used to analyze life, disability and liability insurance needs.
5. Key tool for estate and tax planning.

Income Statement

1. Assess your near-term financial health. Key metric: do you have a positive cash flow?
2. Used as the basis for forward-looking budgets.
3. Typically required for a loan or certain types of investments (partnerships, etc.).
4. Define how much you can allocate towards savings and investing.
5. Analyze tax planning and retirement savings allocations.
6. Used to assess life and disability insurance needs.

Interesting Facts

1. 30% of US households have a long-term financial plan. 32% of American adults have a budget.
2. 28% of Americans are financially healthy, meaning they are able to cover their expenses, invest in their retirement plans, and contribute to their savings.
3. 60% of American households live paycheck to paycheck.
4. 65% of Americans don't know how much money they spent last month.
5. 39% of Americans can afford a \$500 emergency expense.
6. 20-30% of Americans don't save any part of their income. This value varies across cited sources.
7. <5% of disposable income is saved by the average American (Goal = 20-25%). This is <1/2 the average during the period between 1950 and 2000.
8. 44% of Americans cite money matters as their #1 source of stress, ahead of personal relationships or work.
9. Money issues are the #1 reason for marital arguments and the #2 cause of divorce, behind infidelity.
10. Less than 25% of millennials have a basic understanding of finances and the need to save and budget.

Balance Sheet Example

Resources to leverage:

Bank statements
 Investment account statements
 Retirement plan statements
 Loan summaries
 Credit Card statements
 Mortgage statements
 Zillow (real estate value)
 Kelley Blue Book (auto value)
 Life Insurance Statements

Statement of Financial Position - <Client Name>			
Date Completed			
Assets		Liabilities	
Cash / Cash Equivalents		Mortgage Balance	
Savings Accounts		Home Equity Loan Balance	
Checking Accounts		Auto / RV / Boat Loan Balances	
CDs		Tax Liability	
Money Market Accounts		Alimony / Child Support	
Life Insurance Cash Value		Student Loan Balance	
Total Cash / Cash Equivalents	\$0.00	Credit Card Balance	
		Other	
		Total Liabilities	\$0.00
Invested Assets			
Mutual Funds			
IRAs			
401Ks / Pensions			
Stocks/Bonds			
Investment Real Estate			
Total Invested Assets	\$0.00		
Personal Use Assets			
Primary Home		Net Worth	\$0.00
Second Home			
Autos			
Boat/RV			
Jewelry /Collectibles			
Other			
Total Personal Use Assets	\$0.00		
Total Assets	\$0.00		
<u>Notes</u>			

Income Statement Example

Statement of Income - <Client Name>				
Date Completed				
	Monthly Amount	Start Date	End Date	Description
GROSS INCOME				
Salary, Bonuses and Commissions				Pre-tax amounts
Investment income (interest, dividends, capital gain distributions)				Only include if NOT re-invested.
Social Security				
Retirement Plan Distributions				
Pension				
Annuity				
Alimony / Child Support				
Business and Rental income				
Other (tips, royalties, etc.)				
Total Gross Income	\$0			
	Monthly Amount	Start Date	End Date	Description
WITHHOLDING				
Withholding - Retirement Plan				
Withholding - Health, Dental, Vision Insurance				
Withholding - Life/Disability Insurance				
Withholding - FSA/HSA				
Withholding - Income Taxes				
Withholding - Other				
Total Withholding	\$0			
Net Take Home Pay	\$0			

Resources to leverage: Pay stubs, Pension/Annuity Statements, SocSec statements, Credit Card statements, Checking Account statement/register.

	Monthly Amount	Start Date	End Date	Description
EXPENSES				
Alimony / Child Support				
Charitable contributions / Gifts				
Clothing				
Entertainment				
Food (groceries and dining out)				
Gifts				
Gym and other memberships (streaming services, etc)				
Household supplies and maintenance				
Insurance - Auto				
Insurance - Health and LTC				
Insurance - Homeowner's / Renter's				
Insurance - Life / Disability				
Insurance - other				
Loan - Auto				
Loan - Other				
Loan - Student				
Medical / Dental / Vision out-of-pocket				
Mortgage				
Rent				
Taxes (property)				
Transportation (fuel, parking, maintenance, etc.)				
Travel				
Utilities (electric, water, cable, internet)				
Other				
Total Expenses	\$0			
Monthly Cash Flow - SURPLUS / (DEFICIT)	\$0			
Notes				
1) All values are MONTHLY, unless otherwise noted.				
2) All income is PRE-TAX.				

Monitoring and Maintenance

1. Once a Balance Sheet and Income Statement are established, they need to be monitored and updated on a regular basis and when personal situations change.
2. The frequency of monitoring and updates varies by financial situation:
 - When first establishing a Balance Sheet and Income Statement, I suggest quarterly reviews/updates.
 - Once your financial statements are in place and proven to be accurate, 1-2x per year is sufficient.
 - Both financial statements should be updated upon any significant life change, such as marriage, new job, new child, inheritance, divorce or death of a spouse, significant purchase, etc.
3. Always save the current version of the financial statements, then create updated versions.
4. Balance Sheet monitoring should focus on net worth growth over time, asset allocation (diversity), tax status and debt management.
5. Income Statement monitoring helps validate the accuracy of your budget, defines how much surplus income is available for investment or debt reduction, and confirms expense levels and categories (i.e., areas in which expense reduction may be possible to improve cash flow).
 - Portfolio and Passive income should be monitored closely, as this income rarely has taxes withheld and may lead to significant income tax obligations.

Resources

1. Eustace Advisors has Balance Sheet, Income Statement and Budget templates available for client use.
2. www.investopedia.com – this is a great resource for financial, tax and estate related topics.
3. www.nerdwallet.com - this resource is very helpful for assessing “best of” subjects such as credit cards, insurance, loans, banks.
4. www.thebalancemoney.com – similar to Nerdwallet, this resource has a wide range of calculators, “best of” articles and useful posts on a range of personal finance topics.
5. <https://tickertape.tdameritrade.com/personal-finance/types-of-debt-good-debt-bad-debt-15813>.

Questions?