Finance for the Life of Your Language Services Business

By Memuna Williams

This article is not intended to constitute legal, financial, or other business advice. Each individual or company should make its own independent business decisions and consult its own legal, financial, or other advisors as appropriate.

The professor of my first finance course in business school told the class that finance was the subject that would help us, as future managers, add the most value to our companies. I greeted his assertion with skepticism, since I wondered whether intangibles such as the quality of a company's offerings, company culture, or how a company treats its people were not better measures of value creation.

I have since learned that finance is needed at start-up, during the life of the business, and even at exit. Language services companies are no different from other businesses in this respect. Viewing our businesses through the prism of finance will help us start, manage, grow, and exit better businesses over the long run. I have also learned that in order to achieve our goals, we need a plan for growth and a consistent and reliable system for recording and analyzing our companies' financial information.

Finance at Start-Up: The Business Plan

The foundation for most companies is a business plan. Business schools teach students how to create them, business literature is replete with references to them, and bankers, financiers, and business counselors often want to see them. There is no single formula for a successful business plan, but it should contain sections describing the business, its marketing strategy, potential competition, operating procedures, an executive summary (statement of the business's purpose), and financial data (including projections and budget and cash flow analysis). An excellent place to get started is the website of the Small Business Administration, which contains sample templates for writing a thorough plan.[1]

Ultimately, a business plan should answer such questions as:

- What do you want to do?
- How realistic is the plan given the competitive environment and the size of your market?
- What employees will you need to hire for the business?
- What training will you need to provide employees?
- How much money can you contribute to start the business?
- How much money will you need to borrow?
- In what form do you need the funds?
- When will you be able to repay the money borrowed?
- What documents will you need to

provide to your lender?
- How much will each of these strategic operating decisions cost?

As a language services professional, it is important for you to have a plan. Why? Because at some point during the life of your business you will likely be asked by outside stakeholders to provide at least some of the information outlined in the questions above, and you need a way to present it in a succinct manner. More importantly, a business plan is critical because it helps you analyze and organize decisions to see how they relate to the goals you are trying to achieve. A business plan will also help you understand the financial implications for each decision, including what type of business structure you choose to adopt (e.g., sole proprietorship or S corporation), where you want to locate the business, and what products and services you wish to provide. For example, accountants might tell you that choosing to be a sole proprietor exposes you to a higher tax rate and makes you personally liable for business debts. They might also point out that an S corporation can be more expensive than other types of businesses to set up. However, as the owner of an S corporation, you will be taxed only once on your personal returns (at a lower rate than the sole proprietor) and will not be personally liable for debts incurred by the business. (More information on the two types of corporations can be found on the website of the Internal Revenue Service.[2])

A business needs to be viewed like any other investment from which a return should be expected for the risk being taken. As such, planning the business with a critical eye on finances will help determine whether it meets this test. In addition, the perennial and vexatious question of how much to charge for language services can be addressed through the business planning process by looking at actual costs and such factors as the target market and the business's corresponding position in the marketplace. As the details for the business plan are completed, the financial implications for each of its components are summarized. These summaries will then be used to compile the financial sections of the plan outlining projections and budget information. Business planning assistance and resources are available through the Service Corps of Retired Executives (SCORE) and the Small Business Administration.[3]

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Finance at Start-Up: Projections

Once the initial sections describing the business are complete, it is time to develop the financial sections of the business plan. Compiling financial data for your company is as much an art as a science. The art is in deciding what you want the financials to reflect. The science is in ensuring that the information is as realistic as possible by researching what items cost or finding industry comparables.

Developing the financials starts with the assembly of a cash flow statement. As stated in *Small Business Management: A Framework for Success,* by Charles Bamford and Garry Bruton, the cash flow statement, or cash budget, is the most vital document for establishing proper financial health for a small business.[4] This statement helps anticipate cash shortages so something can be done about them before they occur. Let's use a sample freelance translation business to demonstrate how to set up a proper cash flow statement. (Please note that the numbers provided in the sample forms in this article are not meant to be exact. They serve merely as examples to show you a possible way of organizing and tracking information.)

Sales Forecast

The cash flow projection starts with the sales forecast. Everything else flows from there.

Figure 1 on page 26 shows that the owner of this freelance business is planning to have four income streams (translation, revision, interpreting, and project management), and expects variability in the amount of words translated and the number of hours spent on hourly functions. For each income stream, the number of units sold, the unit price, and total sales are estimated. (A sales forecast for an agency will likely show additional income streams and very different numbers.)

The assumptions underlying these estimates should be stated clearly in the business plan. For example, the assumptions for this business include the number of business days in particular months, the number of actual working hours in a business day, and the percentage of time spent on each activity. Initially, you might find such projections difficult to make because you might not know from which areas of the business to draw the information. However, the marketing research, analysis, and summary sections you compiled earlier in the business plan should make coming up with realistic estimates easier.

Start-Up and Operating Costs

After sales are forecast, the start-up and operating costs can be estimated. Start-up costs are one-time expenditures the business will incur to get off the ground. Operating costs are the expenditures the business owner will incur to run the business month to month. (See Figures 2a and 2b.)

Cash Flow Statement

The next step is to consolidate the sales, start-up costs, and total expenses into two cash flow statements. The first statement will show the income and expenses over a certain period, without equity or debt investment information. (See Figure 3 on page 27.) This first statement is critical because it will enable you to see anticipated low cash points, which in turn will help determine how much of an initial investment will be needed for the business. The second cash flow statement presented in Figure 4 on page 27 shows the same scenario, only this time the equity and/or debt investment is included. (Equity and debt will be addressed in the next section.)

The cash flow statement is a great way to start a language services business on healthy financial footing. The cash flow statement analysis can be complemented with break-even analysis to give you an idea of the level of sales or length of time needed to cover all costs and make a profit. The analysis can be extended further by including such factors as harvesting cash and exiting the business.[5] This level of analysis helps provide a long-term view of the business, allows the business to be contemplated as a risk-

Figure 1: Sales Forecast

Months	Jan	Feb	Mar	Total
Translation				
Units Sold: Words	7,800	9,880	14,300	
Unit Price: Cents/Word	$0.15	$0.15	$0.15	
Total Sales	**$1,170**	**$1,482**	**$2,145**	**$4,797**
Revision				
Units Sold: Hours	16	20	29	
Unit Price: Hourly Fee	$40	$40	$40	
Total Sales	**$640**	**$800**	**$1,160**	**$2,600**
Interpreting				
Units Sold: Hours	16	20	29	
Unit Price: Hourly Fee	$40	$40	$40	
Total Sales	**$640**	**$800**	**$1,160**	**$2,600**
Project Management				
Units Sold: Hours	16	20	29	
Unit Price: Hourly Fee	$40	$40	$40	
Total Sales	**$640**	**$800**	**$1,160**	**$2,600**
Total-All Service Sales	**$3,090**	**$3,882**	**$5,625**	**$12,597**

Figure 2a: Start-Up Costs

Months	Jan	Feb	March	Total
Computer	$1,200	0	0	$1,200
Laptop	$1,500	0	0	$1,500
All-in-one Printer	$ 800	0	0	$ 800
Cell Phone	$ 300	0	0	$ 300
Air Card	$ 300	0	0	$ 300
CAT Tool	$1,000	0	0	$1,000
Quickbooks	$ 900	0	0	$ 900
Adobe Professional	$ 900	0	0	$ 900
Total	**$6,900**	**0**	**0**	**$6,900**

Figure 2b: Operating Costs

Months	Jan	Feb	Mar	Total
Labor				
Salaries and Wages	$1,386	$1,386	$1,386	$4,158
Payroll Taxes	$ 396	$ 396	$ 396	$1,188
Total Labor Expenses	$1,782	$1,782	$1,782	$5,346
Non-Labor				
Telephone	$210	$210	$210	$630
Internet	$105	$105	$105	$315
Advertising	$168	$168	$168	$504
Insurance	0	0	$252	$252
Legal	0	$378	0	$378
Gas	$ 25	$ 25	$ 25	$ 75
Supplies	$ 19	$ 19	$ 19	$ 57
Loan	$126	$126	$126	$378
Total Non-Labor	**$653**	**$1,031**	**$905**	**$2,589**

Figure 3: Cash Flow Statement (Without Equity or Debt Investment)

Months	Jan	Feb	Mar	Total
Total-All Service Sales	**$3,090**	**$3,882**	**$5,625**	**$12,597**
Total Start-Up Costs	$6,900			$6,900
Total Labor Expenses	$1,782	$1,782	$1,782	$5,346
Total Non-Labor Expenses	$ 653	$1,031	$ 905	$2,589
Total Disbursements	**$9,335**	**$2,813**	**$2,687**	**$14,835**
Beginning Balance	**$ –**	**($6,245)**	**($5,176)**	
Equity Investment				
Loans				
Net Cash Flow	($6,245)	$1,069	$2,938	($2,238)
Ending Balance	**($6,245)**	**($5,176)**	**($2,238)**	**($2,238)**

Figure 4: Cash Flow Statement (With Equity or Debt Investment)

Months	Jan	Feb	Mar	Total
Total-All Service Sales	**$3,090**	**$3,882**	**$5,625**	**$12,597**
Total Start-Up Costs	$6,900			$ 6,900
Total Labor Expenses	$1,782	$1,782	$1,782	$ 5,346
Total Non-Labor Expenses	$ 653	$1,031	$ 905	$ 2,589
Total Disbursements	**$9,335**	**$2,813**	**$2,687**	**$14,835**
Beginning Balance	**$ –**	**$3,755**	**$4,824**	
Equity Investment	$3,300			$3,300
Loans	$6,700			$6,700
Net Cash Flow	($6,245)	$1,069	$2,938	($2,238)
Ending Balance	**$3,755**	**$4,824**	**$7,762**	**$7,762**

return investment, and forces consideration of valuation of the business. Exit and harvest data can be analyzed through such methods as discounted cash flow and asset-based valuation. The final step, a sensitivity analysis, added to the initial assumptions and forecast made earlier in the plan, will help ensure that the projections are as accurate as possible. For instance, what if sales are lower than expected? What if they are higher? These are very important questions, but even more important is the question of how to reach the desired level of sales. (Successful sales can be the most difficult task for a new business.) Extensive analysis of the cash flow statement will help business owners work through these types of issues.

Equity or Debt?

All the information compiled up to this point can now be used to determine how much of an investment is needed for the new business. It is recommended that at least one and a half times the amount estimated to start the business be requested. This is because costs are almost always greater than expected, even with careful analysis.

The next question facing you as a business owner is whether to obtain the investment in the form of equity or debt. Equity is funding that does not need to be repaid, but gives contributors a stake in the business. Equity can be provided by the founders, other companies, venture capitalists, and angel investors.[6] Debt is funding that results in an obligation to repay or return an asset (usually money). Sources of debt include loans from banks, finance companies, individuals and founders, credit cards, and supplier credit. Sources of funding include leasing and factoring.[7] When deciding which form of financing to choose, you should consider how much control you want others to have in the business, how much interest you are willing to pay, and how you will maintain a healthy cash flow.

Pro-Forma Financial Statements

After a decision has been made about where to obtain the money for the business, all the information to prepare pro-forma (forecast) financial statements is ready. A balance sheet showing what the company owns and who owns it and an income statement showing anticipated income expenses and profit are the two key financial statements to be prepared. (See Figures 5 and 6.) These statements can be used to measure the company's anticipated liquidity, activity, leverage, and profitability. You should use the information contained in these statements to assess your business's performance periodically.

Running the Business Through Finance: Management and Growth

With the business up and running according to plan, it is vital that you implement and maintain a thorough system to keep your financial records in order. Maintaining good records includes designing the accounting system and systematically recording regular transactions such as invoices, checks, receipts, and bank reconciliations. Additional steps include planning and preparing income tax returns and maintaining a budgeting system to monitor performance. Regardless of whether you do all of this yourself by using accounting software or hire an accountant, you will still need some basic accounting knowledge.

Cash flow management starts with managing projects as efficiently as possible. The faster a project is completed, the faster the company can bill for it. Speed *must* be balanced with quality to ensure that clients return with more business. One method of creating an incentive for customers to pay sooner is to consider giving an early payment discount. Faster billing and receipts means cash in hand to pay bills on time. This in turn helps ensure that the business does not run out of cash and can continue as a going concern. It also helps the business to maintain a good credit rating and remain in good standing with creditors.

As a business owner, you need to stay informed to prevent bad actors from harming the business. You must also stay up to date with legal and financial requirements to ensure that you have the information needed to run the business and keep track of collections. Maintaining excellent financial records will put the business in a good position for future growth or exit.

Figure 5: Income Statement

Sample Translation Business for the period ended March 31, 2009				
Months	**Jan**	**Feb**	**Mar**	**Total**
Sales	**$3,090**	**$3,882**	**$5,625**	**$12,597**
Gross Profit	**$3,090**	**$3,882**	**$5,625**	**$12,597**
Expenses				
Computer	$1,200			$1,200
Laptop	$1,500			$1,500
All-in-one Printer	$ 800			$ 800
Cell Phone	$ 300			$ 300
Air Card	$ 300			$ 300
CAT Tool	$1,000			$1,000
Quickbooks	$ 900			$ 900
Adobe Professional	$ 900			$ 900
Salaries and Wages	$1,386	$1,386	$1,386	$4,158
Payroll Taxes	$ 396	$ 396	$ 396	$1,188
Telephone	$ 210	$ 210	$ 210	$ 630
Internet	$ 105	$ 105	$ 105	$ 315
Advertising	$ 168	$ 168	$ 168	$ 504
Insurance			$ 252	$ 252
Legal		$ 378		$ 378
Gas	$ 25	$ 25	$ 25	$ 75
Supplies	$ 19	$ 19	$ 19	$ 57
Loan Repayment	$ 126	$ 126	$ 126	$ 378
Total Expenses	**$9,335**	**$2,813**	**$2,687**	**$14,835**
Income Before Taxes	**($6,245)**	**$1,069**	**$2,938**	**($2,238)**
Taxes				
Net Income	**($6,245)**	**$1,069**	**$2,938**	**($2,238)**

Finance at Start-Up…and Beyond

By the end of business school, I had come around to my finance professor's way of thinking. Finance truly is indispensible to the life of a business. The experiences I am gaining in my business every day convince me of that point of view. With access to reputable online resources such as the IRS and SCORE, it is now much easier to learn how to use finance to build valuable companies.

Notes

1. Small Business Administration Business Plan Template, www.sba.gov/content/templates-writing-business-plan.

2. S corporations are corporations that

Figure 6: Balance Sheet

BALANCE SHEET				
March 31, 2009				
ASSETS			**LIABILITIES**	
Current Assets			**Current Liabilities**	
Cash	$7,762		Accounts Payable	
Accounts Receivable			Short-Term Notes	
(Less Doubtful Accounts)			Current Portion of Long-Term Notes	$1,517
Inventory			Interest Payable	
Temporary Investment			Taxes Payable	$396
Prepaid Expenses	$252		Accrued Payroll	$1,386
Total Current Assets	$8,014		**Total Current Liabilities**	$3,299
Fixed Assets			**Long-Term Liabilities**	
Long-Term Investments			Mortgage	
Land			Other Long-Term Liabilities	$6,700
Buildings			**Total Long-Term Liabilities**	$6,700
(Less Accumulated Depreciation)				
Plant and Equipment	$6,900			
(Less Accumulated Depreciation)			**Shareholders' Equity**	
Furniture and Fixtures			Capital Stock	$3,300
(Less Accumulated Depreciation)			Retained Earnings	$1,615
Total Net Fixed Assets	$6,900		**Total Shareholders' Equity**	$4,915
TOTAL ASSETS	$14,914		**TOTAL LIABILITIES & EQUITY**	$14,914

Related Links

Small Business Administration Business Plan Template
www.sba.gov/content/templates-writing-business-plan

Internal Revenue Service
www.irs.gov/businesses/small/article/0,,id=98263,00.html

Score
www.score.org/index.html

Tax Information
www.sba.gov/content/getting-your-small-business-ready-tax-season

elect to pass corporate income, losses, deductions, and credit through to their shareholders for federal tax purposes. Shareholders of S corporations report the flow-through of income and losses on their personal tax returns and are assessed tax at their individual income tax rates. This allows S corporations to avoid double taxation on corporate income. S corporations are responsible for tax on certain built-in gains and passive income (www.irs.gov/businesses/small/article/0,,id=98263,00.html).

3. The SCORE website can be found at www.score.org/index.html.

4. Bamford, Charles E., and Garry D. Bruton. *Small Business Management: A Framework for Success* (Mason, Ohio: Thomson/South-Western, 2006).

5. Extracting, or harvesting, cash from a business involves limiting the amount of new money that is committed. For example, a cereal manufacturer may limit advertising for a particular brand that appears to offer little opportunity for sales growth. Rather, the firm harvests cash from the brand (referred to as a "cash cow") in order to have funds available for more promising brands.

6. An angel investor (also known as a business angel or informal investor) is an individual who provides capital for a business start-up, usually in exchange for convertible debt or ownership equity.

7. Factoring is the practice of purchasing and collecting accounts receivable or advancing cash on the basis of accounts receivable.

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