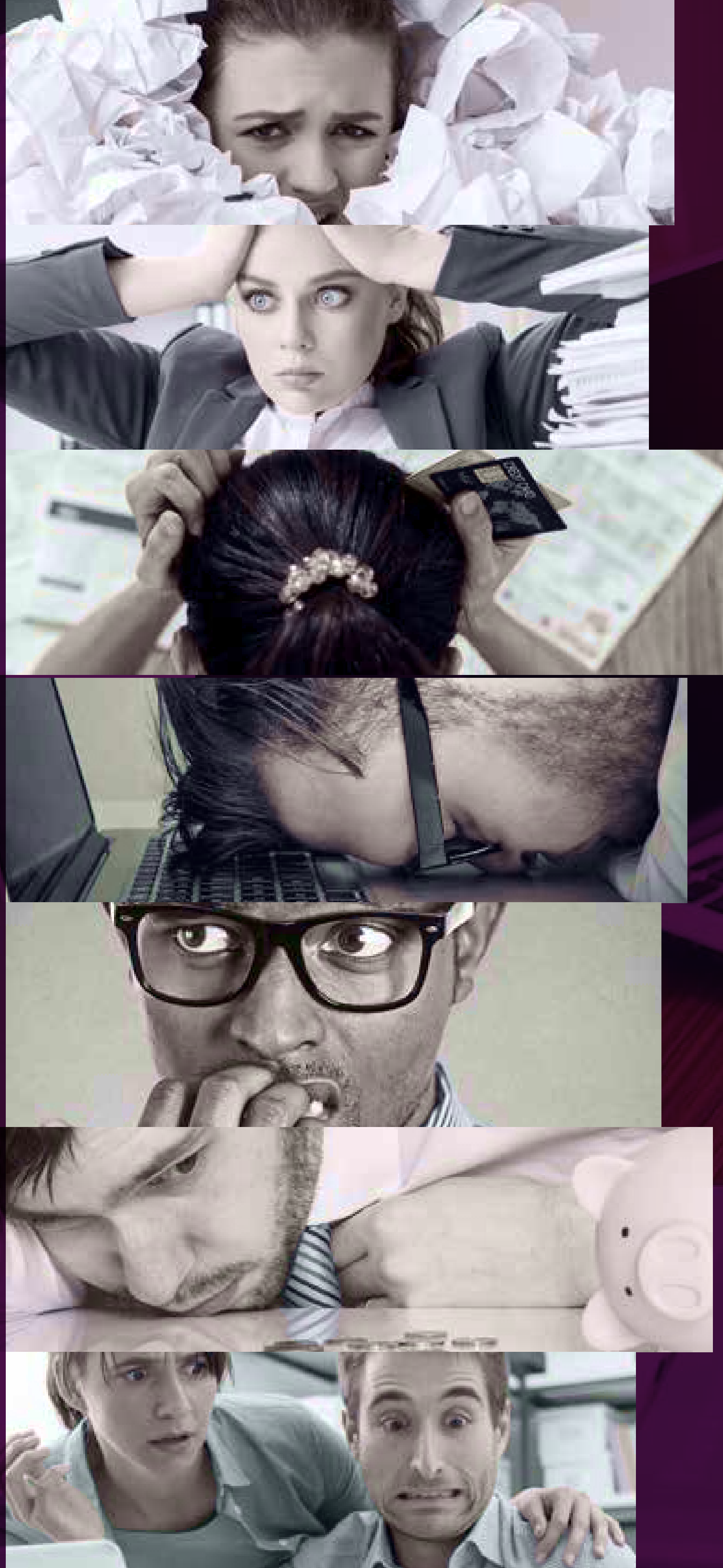

7 ACCOUNTING MISTAKES Small Business Owners Make

and Quick Fixes to Stay Out of Trouble!

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Helping You Work Less and Get Paid More

1

Keeping Receipts in a Shoebox and Only Dealing with Them Once A Year

Why It Happens: We hear horror-stories of audits gone bad where tax collectors bust through the door yelling "show me your receipts!" It could happen to you tomorrow, right? So, the receipts get collected, piled up, tucked away to be dealt with another day.

The Problem

Crumpled receipts get lost and thermal-printed receipts will fade over time, especially if they're exposed to the sun (i.e. kept in the car or near a window). As the year goes on, the pile gets bigger. The mountain of receipts feels more and more overwhelming as it grows. The longer we avoid something the more we build it up in our minds as being terribly painful, which makes it easier to procrastinate, and the pile grows larger still. It's the circle of life.

At the end of the year we're forced to deal with the paperwork monster. This means we either need to set aside the hours required and categorize our own receipts or pay someone else to do it. Neither one is appealing.

The Quick Fix

There is no reason to keep paper receipts. The CRA will accept digital copies. It's easy to snap a photo with your phone every time you get a receipt. Save your photos and name the files so you can search for them later. Once it's digitized you get to experience the pure joy of crumpling up that paper receipt and gleefully tossing it into the recycling bin, never to clutter your desk again.

You can drop all the files in a "to be sorted" folder, then go through once a week, or month, entering the expenses into your bookkeeping system. Now the task only takes an occasional 15 to 30 minutes instead of piling up to painful hours or days.

Incorporating Too Soon

Why It Happens: Starting a business is a grand adventure, and a personal leap of faith. Incorporating makes it feel "real" and seems to lend credibility to your dream. You may have heard that all businesses need to be incorporated, or were advised to do so. Maybe you heard, as a corporation, you would have to pay significantly less in taxes.

It's easy to misunderstand corporations – their structure, their purpose, their costs, etc. The bits of information we have, and hear from others, are sometimes misinformed or out of date.

The Problem

Incorporation makes your business much more complicated plus it comes with extra costs and obligations. A corporate tax filing will often cost ten times more than a personal tax service, and depending on your business, or the government policies of the day, you may not find a significant savings in your effective tax rate.

In other words, it can be a big pain in the neck with no benefits.

The Quick Fix

Don't incorporate until you absolutely must do so, with professional guidance from your accountant and lawyer. Begin growing your business as a sole-proprietor, or a simple partnership if you're working with others. It may be years before you need to consider incorporation. It may be never!

If you've already filed your incorporation papers and are feeling some regrets, there is always the option to dissolve the corporation. It's another expense (legal consult and final tax return) but in the long run life as a sole-proprietor may be simpler and more cost-effective.

Mixing Personal and Business Bank Accounts

Why It Happens: As a small business owner, it's sometimes hard to draw the line between personal and business. Our top priority is to pay our bills (rent, grocery, etc.) and whatever's left over (if there is any) will go towards the business. The business income pays for our personal expenses so why wouldn't it just go into one account?

The Problem

When everything is in one account it becomes very difficult to draw a line between business and personal spending. When you are trying to understand how your business is going, and growing, the extra stuff mixed into your statements and reports makes them confusing.

The other problem is taxes. The CRA wants to see a clean distinction between personal and business. If you put everything into one account, it's far more difficult to prove a restaurant meal was truly a business expense.

It also means you're doing twice as much bookkeeping work as you go through business and personal receipts to figure out which is which.

The Quick Fix

Get a designated business chequing account. It will have its own debit card and cheques. You'll receive a statement that will be 100% business transactions. No more wasted time trying to do forensic bookkeeping.

I would also encourage you to get a second credit card just for business use. It can still be a personal card, with your name on it, but you only pull it out of your wallet for business related purchases.

Tip: If you end up with business debit or credit cards that look the same as your personal cards attach a sticker to clearly identify which is which. Card mix-ups cause a real pain in the bookkeeper's neck!

Using the Wrong Accounting Software

Why It Happens: When we're dreaming up our new business, bookkeeping is usually not part of the picture. It's not fun, and most people try to avoid it as long possible. When it becomes painful enough, we look for the cheapest possible solution. Sometimes this means an Excel spreadsheet, sometimes it means signing up for free accounting software. We think it's fine for now and it's free, so we're saving lots of money, right?

The Problem

These free solutions have hidden costs. They may be difficult to use because they are poorly designed. Or they may be too simple, and limited in what they can do, so you will hit a wall as your business grows.

If you eventually work with a professional bookkeeper or accountant, your "cheap" system may slow them down and cost you more in hourly fees.

If your business is booming, you may find you out-grow this free system and suddenly must switch to a paid system. The switch will be time consuming (you have to re-learn everything), costly, and not all your data will transfer over.

The Quick Fix

Get started right now with a bookkeeping system that will support your business in the long term.

I personally use and recommend Quickbooks Online. It can keep up with your business no matter what happens, and you can get started for less than $10 per month.

As your business booms, you'll be ready to grow into all the advanced features of Quickbooks.

Like all pro software tools, it can be a steep learning curve at the beginning, but the time spent learning the ropes is an investment in your future. (oh, yes, and it will help shave more time off your repetitive bookkeeping tasks!)

Setting Prices Too Low

Why It Happens: Pricing is one of the hardest things to do as a small business owner, especially if you're a service-based company. We tend to set our prices too low due to fear, or insecurity. We feel if we're too expensive no one will buy our services. Better to be on the low side and make sales than to be on the high side and make nothing, right?

The Problem

When prices are too low you end up working long hours for not enough pay, which will cause a domino effect in your life. If you can't pay your bills you tend to put in more hours. If you're working too many hours keeping up with the work, you aren't spending enough time acquiring new clients. You're going to be stressed-out, and eventually you'll burnout.

You start out trying to provide a bargain, and you end up in debt, shutting down your business. Woof!

The Quick Fix

There's no need to feel guilty about asking to be paid. Believe in the value you provide. Your business helps people! When you charge a good price it enables you to grow and in turn help more people.

Stand your ground and don't offer discounts "to be nice." The nice thing to do is to charge what you're worth and feel good about delivering your best service.

From an accounting point of view, it's important to understand the true cost of overhead, materials, labour, and taxes which all must be included as part of your price. Make sure you are rewarded for your time and expertise, plus give your business enough profit to invest in its own growth.

Receiving a Payment and Not Saving for Taxes

Why It Happens: When we send out an invoice and receive a payment it feels like the entire amount is our money earned. We worked, we invoiced, we got paid, yay! It all goes into our bank account and we spend it on our bills or re-invest it into the company.

The Problem

The problem is when it gets to tax time, and we don't have the money to pay the amount we owe. We forget that part of our payment, the sales tax, already belongs to the CRA and we're merely collecting it on their behalf. Then, another chunk of that revenue will be owed for income taxes.

Over the course of an entire year it can add up to a heart-fluttering amount, and we get crushed by a "surprise" bill.

The Quick Fix

If you are doing your bookkeeping regularly your system should be able to give a running total of taxes owed. On a regular basis you can be depositing money into a "piggy bank" to pay this bill at the end of the year.

Many banks allow you to have a sub-account, or savings account, to keep this separate from your daily chequing account. It's harder to spend that money when it's not showing in your available balance.

Misunderstanding The Ins and Outs of Sales Tax

Why it Happens: Between GST, HST, PST, and QST sales tax in Canada can be a confusing alphabet soup. It can be tricky to decipher the official write-ups on when and if you need to be collecting tax on your business invoices.

The Problem

Not having a solid understanding of sales tax can create a real big mess for you.

Common problems are charging tax when you shouldn't (not being registered for a sales tax ID number) or not charging tax when you should (when you reach the $30k income threshold). You also need to be keeping close track of sales tax going in and out so you aren't over-paying.

It gets more tangled when you do business across provincial borders. You may need to register for PST, or QST, and file separate tax returns with the provincial offices.

The Quick Fix

If your world-wide income reaches $30k in four consecutive quarters, and your industry is not exempt, you must register for sales tax with the CRA. You will be assigned a sales tax number. Include your number on every invoice, and clearly state how much tax is being charged. Even if you say tax is "included in the price" it needs to be clearly documented on the invoice.

In addition to your income tax filing, you'll need to submit a sales tax return. Report your total sales, total sales tax collected, and total sales tax paid out on expenses. Then, unfortunately, you have to hand over any surplus tax dollars collected.

You Can't Rely On Quick Fixes Forever

I've suggested quick fixes for these common mistakes to help business owners to get back on track. They are a great starting point, but they are by no means the complete solution. I'm offering them as general suggestions and they are not intended as professional advice to address your specific situation.

I believe small business owners can really benefit from a foundational understanding of accounting and bookkeeping. In the early years of your business you can save a lot of cash by doing your own bookkeeping if you've learned the basics. (If you haven't learned the basics, you can lose a lot of cash paying somebody to clean up mistakes!) Then, as you grow, being able to read and understand financial reports will provide great insight into how your business is operating under the hood.

If you've made it this far, and you're looking for the next step to learning about small business accounting, you can find it at AccountingAnswers.ca

Thanks for reading,

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