# FINANCIAL MANAGEMENT I

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## INSTRUCTOR

Stacey Church, CVE
Chief Operating Officer
Georgia World Congress Center Authority
Atlanta, GA

Author's Credit
This monograph was written and edited by Chris Whitney, CPA

## COURSE OUTCOMES

At the conclusion of this session, participants will be able to:

1. Understand what accounting is and why it's important to a venue.
2. Review the payables process and how it impacts all departments within the venue.
3. Review the receivables process and how it relates to the overall success of the venue.
4. Understand the event settlement process.
5. Have access to a glossary of commonly used accounting terms.

## Introduction

Regardless of your current position within your venue, understanding the fundamentals of accounting is critical to the success of your venue and to you professionally. This class is designed to cover the basics of accounting at a high-level with an emphasis on how it applies to you even if you are not working in the accounting/finance department.

Additionally, event settlements are somewhat unique to the venue management industry. We will cover this process in greater detail to prepare you as a venue manager, to understand what goes on an event settlement, how to obtain the information, and what to expect during the actual event settlement with the promoter and/or licensee.

## What is Accounting?

Accounting can be described as a way to communicate the financial health of a business or an organization to any and all interested parties. It is a way of assessing the assets, liabilities and cash flow, or the future of an entity for all current and future investors. It is the lifeblood of a business, and all types of businesses have basic information that is recorded to get that job done. All accounting or bookkeeping has a standard set of accounting principles. It stands for every type of business. In this way there is unity in all business accounting procedures to ensure that there is a clear understanding no matter what business is being monitored. This system is called GAAP or Generally Accepted Accounting Principles which are general rules that all businesses follow when recording their financial information.[1]

## Does Accounting Matter?

Why is accounting so important? Well, for starters, it's all about the "money". An important part of any business or organization is, arguably, the money that comes in and the money that goes out. The accounting department typically monitors this closely by recording transactions, analyzing transaction patterns, and dealing with things like payroll and taxes. Overall, the accounting department can determine the health and efficiency of a business, and increase profitability just by

**1** Barizo, Dee. "The Accounting Degree Review." *The Accounting Degree Review 1/27/15* studying this information.[2]

## *Types of Accounting*

In businesses there are typically two methods of accounting, cash basis and accrual. For smaller businesses, cash basis accounting is usually what is used. It acknowledges and records financial transactions when cash physically moves between involved parties. So, if Santa Claus purchases inventory on a credit card from the North Pole in September but doesn't pay on the credit card until December, using the cash basis method, Santa would record the transaction in December. The transaction would be recorded in December because that's when the money actually left the business and is considered a payment.

For accrual based accounting, using the same example of Santa Claus, the business would record the transaction in September even though no money was actually paid until December. The transaction or intent to pay still exists. The accrual method tracks all commitments to pay or to be paid when the commitment is made, regardless of if actual funds were transferred. This method is typically used for larger businesses and most prevalent in the venue management business.[3]

## *Why does accounting matter?*

Try and imagine your local grocery store decides they don't need an accounting department. At first glance, you may be thinking that they could get by because all the transactions are recorded in the registers and through other electronic means. However, what about inventory? What about the employees' paychecks? What about federal, state and city taxes? What about cash flow patterns? The accounting department exists to ensure that a business isn't losing unnecessary money, employees are being paid, obligations like taxes are correctly fulfilled, trends and patterns that affect the businesses profits and losses are being analyzed and inventory is being paid for.[4]

**2** Sponaugle, Brittani. "Importance of Accounting: Basic Financial Concepts To Know." *The Accounting Degree Review 1/27/15*

**3** Id.

**4** Id.

## *Accounts Payable*

Account payable is defined in Webster's New Universal Unabridged Dictionary as: account payable, pl. accounts payable. a liability to a creditor, carried on open account, usually for purchases of goods and services. [1935-40]

When a company orders and receives goods (or services) in advance of paying for them, we say that the company is purchasing the goods on account or on credit. The supplier (or vendor) of the goods on credit is also referred to as a creditor. If the company receiving the goods does not sign a promissory note, the vendor's bill or invoice will be recorded by the company in its liability account Accounts Payable (or Trade Payables).

As is expected for a liability account, Accounts Payable will normally have a credit balance. Hence, when a vendor invoice is recorded, Accounts Payable will be credited and another account must be debited (as required by double-entry accounting). When an account payable is paid, Accounts Payable will be debited and Cash will be credited. Therefore, the credit balance in Accounts Payable should be equal to the amount of vendor invoices that have been recorded but have not yet been paid.

Under the accrual method of accounting, the company receiving goods or services on credit must report the liability no later than the date they were received. The same date is used to record the debit entry to an expense or asset account as appropriate. Hence, accountants say that under the accrual method of accounting expenses are reported when they are incurred (not when they are paid).

The term accounts payable can also refer to the person or staff that processes vendor invoices and pays the company's bills. That's why a supplier who hasn't received payment from a customer will phone and ask to speak with "accounts payable."

The accounts payable process involves reviewing an enormous amount of detail to ensure that only legitimate and accurate amounts are entered in the accounting system. Much of the information that needs to be reviewed will be found in the following documents:

1. **Purchase orders issued by the company**
2. **Receiving reports issued by the company**
3. **Invoices from the company's vendors**
4. **Contracts and other agreements**

The accuracy and completeness of a company's financial statements are dependent, in part, on the accounts payable process. A well-run accounts payable process will include:

1. **The timely processing of accurate and legitimate vendor invoices,**
2. **Accurate recording in the appropriate general ledger accounts, and**
3. **The accrual of obligations and expenses that have not yet been completely processed.**

The efficiency and effectiveness of the accounts payable process will also affect the company's cash position, credit rating, and relationships with its suppliers.[5]

## *Accounts Receivable*

Accounts receivable is the money that a company has a right to receive because it has provided customers with goods and/or services. For example, a manufacturer will have an account receivable when it delivers a truckload of goods to a customer on June 1 and the customer is allowed to pay in 30 days. From June 1 until the company receives the money, the company will have an account receivable (and the customer will have an account payable).

Companies who sell on credit are unlikely to have liens on their customers' property. Hence, there is a risk that the full amount of their accounts receivable might not be collected. This means that companies need to be cautious when granting credit and establishing an account receivable. If there is uncertainty of a potential (or existing) customer's credit worthiness, it is wise for the company to require the customer to pay with a credit card or certified funds before delivering goods or services.

**5** Averkamp, Harold. "Accounts Payable | Explanation | AccountingCoach." *AccountingCoach.com 1/27/15*

It is also important for a company to monitor its accounts receivable and to immediately follow up with any customer who has not paid as agreed. An aging of accounts receivable is a tool that will help, and it is readily available with most accounting software. A general rule is that the older a receivable gets, the less likely it will be collected in full.

Accounts receivables are reported as a current asset on a company's balance sheet. Good accounting requires that an estimate be made for the amount that is unlikely to be collected. That estimate is reported as a credit balance in a related receivable account such as Allowance for Doubtful Accounts. Any adjustments to the Allowance balance will also be recorded in the income statement account Uncollectible Accounts Expense.[6]

## *Event Settlements*

Event Settlement is the process of settling the financial terms of an event contract by calculating what each party is due. This is typically performed towards the end of the event to ensure the contracted event actually took place. The event settlement process can vary greatly depending on the type of show. For example, an event settlement for an arena event with a promoter will look vastly different than a convention center trade show which will look different than a settlement where the venue has bought the act directly without the use of a promoter. The key to remember is at the conclusion of every event that comes through the venue, there should be a settlement prepared where all involved parties agree of the money owed.

In order to perform a settlement of a ticketed event with a promoter, a significant amount of information must be assembled and processed. The settlement statement should include information on ticket sales, charges to the promoter for rent and other services as specified in the event contract. Additionally, any additional requests the show has made outside what is covered by the rental fee, advances previously paid to the promoter, deposits paid in advance by the promoter, and any money retained by the facility to cover damages should also be included on the settlement statement.

**6** Id.

A settlement statement looks much different when purchasing an act directly without the use of a promoter. In this situation, there most likely have been artist deposits paid in advance of the show with a final payment due night of show (typically to be paid before they take the stage). The sum of these payments is called the artist guarantee. In addition to the artist guarantee, the contract may call for a split of the net proceeds after expenses with a certain percentage to the artist and the remaining to the venue. Typically, artist contracts call for a guaranteed amount vs. 85% of net adjusted gross box office receipts after fees, taxes, and approved expenses, whichever is greater. In the case where the contract calls for a flat artist guarantee, no settlement statement is required other than a document the artist signs indicating they have received the full guarantee. In the event there is a split point, the settlement statement is prepared and reviewed with the artist representative once the artist has taken the stage to review ticket sales, expenses, and the final calculation to agree whether the split point has been achieved.

Non-ticketed event settlements are very common within the convention center niche. These settlements should again include all expenses due to the venue including rent (aka license fee), labor, equipment rentals, catering, set-up/clean-up fees, etc. Additionally, any deposits paid to the venue should be included on this settlement. Payment terms should be established in the contract and should be followed when settling the event with the licensee. Due to the large number of events that occur within a convention center, it is possible the finance team is not as intimately involved with the event settlements. If this should occur, a facility settlement checklist is a good best practice to implement. A facility settlement checklist defines the essential steps that must be completed during or immediately after an event in order to have a complete and accurate settlement. It typically lists the steps the Event Services Department is to perform in order to coordinate effectively with the Finance Department in preparation for settlement.

## *Glossary of Key Accounting Terms*

**Accrual** – Accrual accounting is the method that records revenue and expenses when they are incurred, regardless of when cash is exchanged. The term “accrual” refers to any individual entry recording revenue or expense in the absence of a cash transaction.

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**Assets** - Things that are resources owned by a company and which have future economic value that can be measured and can be expressed in dollars. Examples include cash, investments, accounts receivable, inventory, supplies, land, buildings, equipment, and vehicles.

**Amortization -** the systematic allocation of a balance sheet item to expense (or revenue) on the income statement.

**Balance Sheet** - One of the main financial statements. The balance sheet reports the assets, liabilities, and owner's (stockholders') equity at a specific point in time, such as December 31. The balance sheet is also referred to as the Statement of Financial Position.

**Cash Flow -** Actual changes in cash as opposed to accounting revenues and expenses.

**Cash Flow Statement -** One of the main financial statements (along with the income statement and balance sheet). The cash flow statement reports the sources and uses of cash by operating activities, investing activities, financing activities, and certain supplemental information for the period specified in the heading of the statement. The cash flow statement is also known as the statement of cash flows.

**Deferred Revenue (Liability) -** A balance sheet liability account that reports amounts received in advance of being earned. For example, if a venue receives $10,000 today as a rent deposit for an event in the next accounting period, the $10,000 is unearned in this accounting period. It is deferred to the next accounting period by crediting a liability account such as Deferred (Advanced) Deposit. During the next period, when it is earned, a journal entry will be made to debit the liability account and to credit a revenue account.

**Direct Expense** – A cost that can be traced to a specific event. Examples of this include guest services labor, cleaning, security, box office fees, credit card fees, and runners.

**Expenses** - Costs that are matched with revenues on the income statement. For example, Cost of Goods Sold is an expense caused by Sales. Insurance Expense, Wages Expense, Advertising Expense, Interest Expense are expenses matched with the period of time in the heading of the income statement. Under the accrual basis of accounting, the matching is NOT based on the date that the expenses are paid. Generally, expenses are debited to a specific expense account and the normal balance of an expense account is a debit balance. When an expense account is debited, the account credited might be Cash (if cash was paid at the time of the expense), Accounts Payable (if cash will be paid after the expense is recorded), or Prepaid Expense (if cash was paid before the expense was recorded.) [7]

**In the Black** – Makes reference to a profit on the books; opposite of "in the red." Black Friday sales are known for the profit retailers are adding to their books.

**In the Red** - Makes reference to a loss on the books; opposite of "in the black". In the days of handwritten accounting, ledger entries written in black meant there was a profit, but those in red meant there was a loss.[8]

**Income** - This term is used in several ways. Some use the word interchangeably with revenues. Others use the word to signify a net amount, such as income from operations (revenues minus expenses in the company's main operating activities).

**Income Statement** - One of the main financial statements (along with the balance sheet and the statement of cash flows). The income statement is also referred to as the profit and loss statement, P&L, statement of income, and the statement of operations. The income statement reports the revenues, gains, expenses, losses, net income and other totals for the period of time shown in the heading of the statement.

**Indirect Expense** - A cost or expense that is not directly traceable to an event or perhaps even a department. As a result, indirect costs and expenses are sometimes allocated to the event, department, etc. For example, a concert has some costs that are directly traceable to it, such as the guest services and security wages, cleaning, and equipment rentals. However, the heat for the entire building appears only on one utility bill. Therefore, a portion of the heating bill is an indirect cost to the concert.

**7** Averkamp, Harold. "Dictionary of 1,000+ Accounting Terms | AccountingCoach." *AccountingCoach.com 1/27/15*

***8** "Accounting Terms" http://allaccountingcareers.com/about-us*

Generally it will be assigned as an indirect expense on the income statement and not allocated directly to the event.

**Liability** - Obligations of a company or organization. Amounts owed to lenders and suppliers. Liabilities often have the word "payable" in the account title. Liabilities also include amounts received in advance for a future service to be performed such as deposits and advance ticket sales.

**Prepaid Expense** - A current asset representing amounts paid in advance for future expenses. As the expenses are used or expire, expense is increased and prepaid expense is decreased. An example of this would be the tuition fee paid by your venue for you to attend Venue Management School. This fee would have been paid prior to you attending the school, yet the school didn't occur until June; thus, it would have been accounted for as a prepaid expense. In June, then a journal entry would be made to move it from "prepaid expense" on the balance sheet to an actual expense account on the income statement.

**Revenue** - Fees earned from providing services and the amounts of merchandise sold. Under the accrual basis of accounting, revenues are recorded at the time of delivering the service or the merchandise, even if cash is not received at the time of delivery. Often the term income is used instead of revenues.[9]

## *Summary*

During this class, we have discussed the basic fundamentals of accounting, the event settlement process, and provided a quick reference of commonly used accounting terms. While you may not be an expert and ready to join the accounting/finance team, becoming familiar with the process and how your position directly impacts the net income of the venue is very important. Whether you are an Event Coordinator in charge of preparing the billables to go on an event settlement, an Operations Manager in charge of ensuring there are supplies in the closet for the janitorial staff, or a Marketing Manager placing advertising for an upcoming show, every dollar spent and every dollar earned passes through the accounting/finance department to be accounted for appropriately. The more familiar you are with the accounting process established in your venue, the easier the communication flows between the two departments.

**9** Averkamp, Harold. "Dictionary of 1,000+ Accounting Terms | AccountingCoach." *AccountingCoach.com 1/27/15*