



# Budgeting & Pricing Terms & Tips

## Accounting Terminology Every Business Owner Should Know

**Direct Costs** - Expenses incurred to produce a product or provide a service. These not only include the obvious raw materials or inventory that goes into a product. The cost of any employees, contractors, shipping, sales taxes or other expenses that are only incurred in producing & delivering a specific product or service, are considered a direct cost.

**Indirect Costs** - Commonly called overhead expenses, these are general expenses to run your company. You will have to pay these bills even when you're not making any sales.

**Cash Flow** - The availability of cash on hand to cover ongoing expenses. Cash flow acts as a buffer to cover both planned and unplanned expenses when your sales cycle is at its lowest ebb.

**Cost of Goods Sold (COGS)** - The total sum of direct costs incurred to manufacture goods or purchase inventory in order to sell your *product*.

**Cost of Sales** - The total sum of direct costs incurred to provide a *service*.

**Gross Revenue** – This is a time-based view of the sales income earned during a specified period such as a month or a quarter. Watch this to keep track of sales trends.

**Net Revenue/ Net Income.** This is a time-based view the sales income that remains after subtracting all the expenses incurred during a specified period. Watch this to ensure solid cash flow.

## Costs to Consider When Establishing Your Business Budget

**Marketing:** Costs to run ads, host your website, rent an exhibit booth, and build your brand, such as blogs, social posts, and other marketing efforts.

**Office supplies and equipment:** Everything you use in the office, from paper clips to toilet paper. If you have a home office, it's the printer, and other dedicated technology hardware.

**Technology:** Software and other subscriptions or licenses, such as your email provider, scheduling calendar and internet phone app.

**Rent and utilities:** If you have a home office, this can include the portion of your rent or mortgage for that space, it also includes a portion of electricity, water, home cleaning, etc.



**Legal and administrative:** Any fees paid to attorneys, accountants and other consultants.

**Employee compensation:** Expenses such as salaries, wages, commissions and employee retirement benefits paid to people you've hired as company employees.

- When employees are paid to produce your product or service, much of their compensation may be considered a direct expense.
- When employees are paid to help operate the business, their compensation may be considered an indirect overhead expense.

**Contractor expense:** The hourly, daily, or contracted rate to outsource tasks to an independent contractor.

- If they are hired to help produce a product, it's part of the Cost of Goods Sold.
- If the task helps run your business, such as hiring a social media manager on a platform such as Upwork, that could be considered an indirect cost.

**Taxes:** Federal, State and local taxes you pay for running your business, such as payroll, sales, and income taxes.

## Formula to Price Your Product or Service

Cost of Sales/Goods Sold	(Direct costs to provide 1 unit of your product /service)
+ % of Overhead Expenses	(The portion of each sale that helps keep the lights on)
+ <u>% Profit Margin</u>	(Per-unit mark-up)
= Selling Price	(Is this in line with the market?)

Is the price you came up with in line with what people are willing to pay for similar items?

If it's far out the ballpark, you may need to:

- 1) Prove its premium value. Show why it's far more desirable than alternatives.
- 2) Reduce the COGS. Are there any direct costs that can be reduced?
- 3) Reduce the percentage contributed toward overhead. This may require a higher sales volume to pay the bills, so be sure to include any extra marketing costs in your budget.
- 4) Lower your profit margin. But make sure there at least IS a profit margin.