



Multiple Bank Accounts

1	<p><i>Which Profit First accounts should be access accounts and which ones should be savings accounts?</i></p> <p>It is important to understand the difference between an access account and a savings account. As a general rule, savings accounts yield interest, but are limited in the number of withdrawals allowed during the statement period. An access account typically offers an unlimited number of withdrawals and cheques, but does not yield interest.</p> <p>Income, Profit, Owner's Comp, Tax, and OpEx should all be set up as access accounts. The flexibility offered by checking accounts far outweighs any miniscule interest you get by using savings accounts.</p> <p>The two "no-temptation" accounts set up at your secondary bank - Profit Hold and Tax Hold - should be set up as savings accounts. This is where you will collect interest because your money will pool for a while.</p>
2	<p><i>More bank accounts will result in a lot more bookkeeping work. Is Profit First really worth the effort?</i></p> <p>Profit First is absolutely worth the effort! The additional bookkeeping time required to manage and reconcile multiple accounts for Profit First is negligible, and possibly even more efficient than using just one account. With Profit First, you simply need to reconcile the deposits and periodic transfers from the Income account. All expenses and payments come from the OpEx account. All the other accounts are typically a single transfer in on the 10th and another on the 25th, and a single transfer out at those times.</p> <p>The additional accounts are easy to manage and reconcile. More importantly, the Profit First benefits of instantly knowing what money is allocated to what purpose will have profound effects on the financial health of your business. Xero soon learns where the transfers have gone and suggests the bank transfer. Too easy.</p>
3	<p><i>Which banks are the best and most flexible in terms of creating multiple accounts (e.g. Income, Profit, Tax, etc.) without charging fees?</i></p>

Profit First readers have had great success with credit unions, community banks, and some regional banks. Often, there are no fees and no minimum balance requirements at these smaller institutions.

As you open multiple access or savings accounts, some bankers may look at you cross-eyed (because most businesses don't do Profit First...yet.) Don't let that phase you; the banker simply doesn't understand the process. Just open the multiple accounts and make sure you won't incur fees as a result, even when the balance in certain accounts approaches or goes to zero at times. If the bank insists on charging fees and requiring minimum balances, consider a different bank.

The 10/25 Rule

4 *Why should I allocate money from the Income account to the Profit, Tax, Owner's Comp, and OpEx accounts on the 10th and 25th instead of daily or as needed?*

By doing the allocation process and paying bills according to an established rhythm (i.e., on the 10th and 25th) you benefit in two ways. First, a rhythmic allocation process means you are batching your work, which in turn means you are more efficient. Second, sticking to an established rhythm gives clarity on cash flow trends. You will see the cash flow in and out of your business, like waves in the ocean. When you see trend changes it may indicate an overall change in the business (either problem or opportunity.)

5 *Can I make allocations more frequently or on different days than the 10th and 25th?*

Yes. Profit First was designed to be flexible; however, the 10/25 rule is a best practice. The 10th and the 25th are good dates because it achieves a semi-monthly rhythm of accumulating money and then allocating it (the cash flow wave.) Additionally, when bills are paid on the 10th and 25th they arrive at vendors by the 15th and end of month, respectively. This is when bills are typically due.

For some businesses a weekly rhythm is better, especially during the implementation period. In that case, select a specific day of the week to be the business' "money day." Allocate funds from the Income account to the allocation accounts on this specified day each week.

Avoid doing the allocation process "ad hoc" or more frequently than once a week. A highly frequent rhythm or sporadic rhythm makes it difficult to observe the cash flow waves in the business.

Real Revenue

6 *What is the difference between Total Income and Real Revenue?*

Total Income is a business' top line revenue. Real Revenue is Total Income minus the cost of materials and subcontractors (Mats & Subs).

A business should only adjust for Mats & Subs for Profit First purposes if Mats & Subs costs amount to 25% or more of the business' Total Income. Service based businesses without

	<p>significant subcontractor costs make their Profit First allocations based on Total Income, which will be the same as Real Revenue (because Mats & Subs costs will be set to \$0.)</p> <p>Manufacturers, retailers, restaurateurs, and service providers who rely heavily on subcontractors need to base Profit First allocations on Real Revenue after subtracting Mats & Subs costs.</p> <p>One final, but very important, note: Real Revenue is similar to Gross Profit, but is not the same.</p>
7	<p><i>What does Real Revenue mean?</i></p> <p>Real Revenue is a term we use in Profit First to show a business owner the "real" money their business makes. The top line revenue is not truly representative of the revenue size of your business. Your business may make a margin on materials and subcontractor costs, but that margin is not the core driver of profitability in your business.</p> <p>This can be a real wake-up moment. For example, a home builder may have \$10M in annual revenue and Mats & Subs costs of \$7M per year. This means the company has \$3M in Real Revenue and manages another \$7M in materials and subcontractors' costs. This business needs to operate like a \$3M company, not a \$10M company.</p> <p>Real Revenue is NOT the same as gross profit. Real Revenue is total revenue minus the cost of materials and subcontractors utilized to create and deliver the service or product. Gross profit can take into account burdened labor, building costs, and other "cost of sales" expenses.</p>
8	<p><i>Is Real Revenue the same as Gross Profit?</i></p> <p>No. Gross Profit is the total revenue minus Cost of Goods Sold (COGS). COGS can include materials, subcontractors, employee labor, project costs, ancillary costs, and a host of other expenses depending on your business' accounting structure.</p> <p>Real Revenue is a simpler calculation and less subjective. It is total revenue minus materials and subcontractors.</p>
9	<p><i>My business requires that I run Profit First based on my Real Revenue. How do I manage the deposits from Total Income?</i></p> <p>If you are making a Real Revenue calculation, that means you have material costs and/or subcontractors. In this case you need to open an additional bank account.</p> <p>All your deposits from sales go into the Income account. Next, you take out the normal percentage of your Mats & Subs and move the money to the new Materials & Subcontractors account. Then, the remaining money in the Income account is allocated according to your Current Allocation Percentages.</p>
10	<p><i>Please give me an example of a business that needs to determine Real Revenue.</i></p> <p>Let's look at an electrical contractor.</p> <p>For this example, let's use simple round numbers and say the contractor has \$100,000 in Total Income. He spends \$30,000 in materials (cables, outlets, etc.) and \$25,000 on subcontractors (other electricians he hires for certain projects.) He also spends \$11,000 on an internal</p>

administrator, \$9,000 on vehicle costs, \$8,000 on rent, and has take home pay of \$15,000. Finally, our electrical contractor has taxes of \$2,000, and he has never had a profit.

55% of the Total Income (\$100,000) is being used for Materials & Subcontractors (\$30,000 + \$25,000.)

When deposits come in, they would go into the Income account. On the 10th and 25th, 55% of the Income account total would be allocated to a Mats & Subs account. The money in the Mats & Subs account would be used to purchase more materials and to pay subcontractors. (Side note: The "best practice" is to transfer the funds from the Mats & Subs account into the OpEx account and make purchases and pay subcontractors from there. Remember, we want to limit the transactions in all but the OpEx account to transfers in and out. To avoid temptation, only transfer the amount needed for materials purchases and subcontractor payments and make those payments immediately.)

The remaining 45% in the Income account would be allocated to the Profit, Owner's Comp, Tax, and Operating Expenses accounts. For this example, let's say that the allocation percentages match the Target Allocation Percentages (TAPs) specified in Profit First for a business under \$250,000 in Real Revenue. That means 5% goes to Profit, 50% to Owner's Comp, 15% to Tax, and 30% to Operating Expenses.

Based on \$45,000 in annual Real Revenue, the Profit allocation would be \$2,250, Owner's Comp would be \$22,500, \$6,750 would be reserved in the Tax account, and \$13,500 would be moved to the OpEx account.

With \$11,000 going to an admin, \$9,000 to vehicle costs, and \$8,000 to rent (a total of \$28,000,) this business needs to clearly cut costs and run leaner. Costs need to be no greater than \$13,500 annually.

The other opportunity to increase Real Revenue in this scenario is to reduce the Mats & Subs costs. Reducing these costs will automatically make more money available for Profit, Owner's Comp, Tax, and Operating Expenses.

11

I have 15 part-time employees who do pet sitting for me and are paid on a per-job basis. For the purpose of Profit First, are they considered subcontractors?

Yes. Employees or contractors who are compensated per project and only for income-generating activities are considered subcontractors for the purposes of Profit First. You would subtract the costs of those individuals from your Total Income to find your Real Revenue.

Profit, Owner's Comp, & Tax Allocations

12

Since the Profit, Owner's Comp, and Tax accounts are all for the benefit of me, the owner of the business, can't they just be one account instead of three?

No. While the money allocated to these accounts does benefit the owner(s), the use of the money in each account is distinct. Owner's Comp is for the owner's salary or regular recurring

	<p>distribution. The Profit account is used as a quarterly bonus (and can also function as a rainy day fund, or be used for a "Death to Debt" quarterly distribution.) The Tax account is used to pay the owner's taxes and any corporate taxes on profits. So while the money does all benefit the owner, the accounts need to be kept separate so you can instantly tell just by looking at your bank balance what money is allocated for which purpose.</p>
13	<p><i>I take a salary from payroll, do I still need an Owner's Comp account?</i></p> <p>Yes. You will transfer the money from Owner's Comp to the Payroll or OpEx account each pay day. The purpose is to always be able to instantly see what money the company is allocating to Owner's Comp (and the other accounts) when you look at your bank balances.</p>
14	<p><i>I take my compensation in distributions. Do I still need separate Profit and Owner's Comp accounts, since all the money flows to me?</i></p> <p>Yes, you still need both an Owner's Comp and a Profit account. Owner's Comp will be distributed to you on the 10th and 25th and should be a consistent amount (acting like a payroll.) On a quarterly basis, 50% of the balance in the Profit account will be distributed, acting like a bonus (which it is.)</p>
15	<p><i>Why is the Tax allocation 15%? It seems very high.</i></p> <p>The Tax account is intended to pay corporate taxes due on the business' profits AND the personal taxes of the business owner(s), even if the business owner has taxes withheld from their payroll. 15% of Real Revenue is typically enough to cover these taxes, but some businesses with low operating expenses and high profits may have to allocate more than 15%.</p>
16	<p><i>I am an owner in the business, and our payroll is such that my taxes are already deducted from pay. Do I still need to reserve such a high percentage in the Tax account?</i></p> <p>Yes. The Tax account will "reimburse" you for the taxes withheld from your salary. While logically you could just increase the Owner's Comp allocation and reduce the Tax allocation with the same result, reimbursing yourself for taxes withheld from your salary makes a big difference behaviorally.</p> <p>When taxes are deducted from your pay, it can feel like a loss. This triggers the behavioral pain response of "loss aversion." But if the business pays your taxes directly or reimburses you for the taxes that were "taken" from your pay, the negative association you feel with paying taxes is reduced. If you have taxes deducted from your pay, use the money allocated to the Tax account to reimburse yourself for those taxes on a regular basis.</p> <p>Another benefit of allocating 15% to the Tax account is your tax liabilities can't be "hidden" from you as part of your salary. This will give you a much better understanding of your real compensation and total tax liabilities.</p>
17	<p><i>I want to pay as few taxes as possible. Shouldn't I run up expenses to cut taxes?</i></p> <p>That is the most damaging myth of money management. Running up expenses to reduce taxes is the same as spending \$10 to save \$3. It is very damaging to the business.</p> <p>The goal is to run the business as profitably as possible (that is the only way to achieve financial freedom.) You should work closely with a Profit First Professional to additionally reduce your tax liabilities as much as you can.</p>

18	<i>My business is a company, and as an owner/shareholder I am on payroll. My taxes are deducted from my salary. Do I still need a Tax account?</i>
	Yes. The purpose of the Tax account is to pay taxes due on your business' profits AND to reimburse you for the taxes withheld from your paycheck. Allocate to your Tax account on your regular allocation schedule, and then do a distribution to reimburse yourself quarterly for the taxes withheld from your paycheck.
19	<i>I am a retailer and have to pay GST. Which account does that come from?</i>
	You would open a separate checking account and name it GST. Every penny of the GST you collect is allocated to this account. For example, if you sell something for \$100 and the GST is 10%, you will deposit \$110 into your Income account. Transfer that \$10 in GST into your GST account, then do your Profit First allocations with the remaining \$100. Remember, GST collected isn't legally your money. You are acting as a collection agent for the government, so never treat that money as income in your Profit First allocations.

Operating Expense Allocations

20	<i>I pay all my vendors on the same day on the month. If I do allocations to Operating Expenses (OpEx) on the 10th and 25th will it be problematic for paying vendors on time?</i>
	No, this will not pose a problem. Let's say you pay vendors on the 10th of each month. When you make your allocation to the OpEx account on the 25th, that money will just sit in the OpEx account. When you make your allocations on the 10th, you will add to what is in the OpEx account from the previous allocation. After making your allocation for the 10th of the month, you will pay your vendors from the balance in the OpEx account just as you did prior to implementing Profit First.
21	<i>Where do I pull the money from if I don't have enough money to pay expenses from my Operating Expense account?</i>
	This is the "moment of reckoning" when you follow Profit First. The moment will come for every business when there is not enough money in the Operating Expense account to cover all the expenses. You may NOT use other money. Your business is yelling at you and shaking you saying you CAN'T afford to continue to carry all these expenses and you need to find a better way. Reduce your expenses, and find a way to pay what you owe when the next allocation to OpEx comes in. But no matter what, <i>you must cut your expenses.</i>
22	<i>Why do I need Profit and Tax accounts at my primary bank if I'm just going to move that money to my Profit Hold and Tax Hold accounts at my secondary bank?</i>
	The transfer of money to the Profit Hold and Tax Hold accounts at the second bank can take a day or two, and sometimes longer. Without Profit and Tax accounts at the primary bank, the money allocated for Profit and Tax would sit in the Income account at the primary bank for a few days. This can become confusing...or tempting.
23	<i>Should Profit First be implemented retroactively?</i>

No. The allocations start the day you implement Profit First, with your very next deposit. You don't make retroactive allocations apart from the transfers you have to make from your existing bank account to open your Profit First accounts.

Debt

24 *My business has debt. I can't be profitable until I pay off all my debt.*

Wrong. In fact, the only way to pay off debt (which is simply past expenses that you haven't paid for yet) is to be profitable. You must make more money than you are currently spending in order to have current profits. You then use those profits to pay off your debt (past expenses).

25 *I have multiple loans and forms of debt. How do I pay it all off?*

Pay the minimum balances due out of your Operating Expenses account. These should be considered "regular" bill payments. Then, use any money you have left in Operating Expenses after paying your other "regular" bills to make an additional payment to your smallest debt.

No matter what, keep allocating to your Profit account on the 10th and 25th. This may sound crazy since you have debt to pay, but you MUST build up that habit of always taking your Profit first.

When you do your quarterly profit distribution, take 95% to 99% of that distribution money and use it to make an additional payment to your smallest debt. The goal is to pay off your smallest debt as quickly as possible.

The remainder of your quarterly profit distribution (5% to 1%) is used for you to celebrate. This process has you constantly chipping away at debt (from Operating Expenses) and then quarterly hitting that debt really hard. It is kind of like boxing... jab, jab, jab, then a massive right hook.

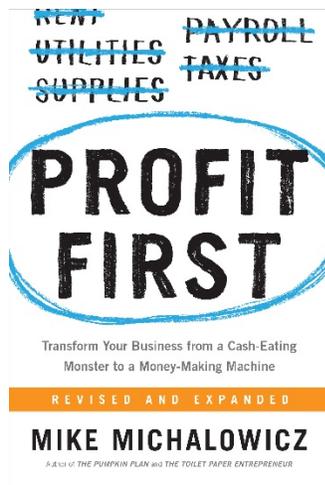
26 *I have lots of debt, including credit cards, personal loans, and banks loans. Some of this debt has very high interest rates. Shouldn't I pay off the high interest debt first?*

While logic dictates you should pay off your highest interest rate debt first, Profit First is all about leveraging human behavior. One of these behaviors is celebrating "early successes." When we see early progress in our management of money, we become more committed to the process, even if the progress is very small. In regard to debt, Dave Ramsey, author of *The Total Money Makeover*, suggests a technique that is in perfect alignment with Profit First.

The process is simple. First, sort all your debts from smallest amount due to largest. Then, put all your financial effort into eradicating the smallest debt first, while continuing to pay the minimum balance due on all other debts. Once the smallest debt is paid off, target the next smallest debt on your list, adding the amount you were paying to the first debt to the payment you make on the next debt. Wipe that out, and then hit the next. This will build a series of "early successes" and create a "snowball effect" as more and more money is freed up to target the remaining debts.

Other Applications Of Profit First

27	<i>Can I use Profit First to identify a good business to buy?</i>
	Yes! An Instant Assessment will show what needs to be "corrected" in the business. Less correction = a better buy.
28	<i>Can I implement the Profit First system <u>before</u> my business is profitable?</i>
	If your business is not profitable, you need to implement Profit First right away! Implementing Profit First forces profitability rather than waiting for it. Start with low allocation percentages - like 1% to Profit and Tax - but get started NOW!
29	<i>How do you adjust the Profit First allocation percentages for other currencies (outside the US)?</i>
	<p>Profit First is a percentage-based system, so it works regardless of the currency used. You can convert your currency to US dollars to find your Real Revenue range and the corresponding Target Allocation Percentages. Then follow the implementation process as you would for a business using US dollars.</p> <p>Since the TAPs are just targets, every quarter you will need to adjust your Current Allocation Percentages and analyze what is working for your business. You may discover your Tax allocation needs to be higher, or other adjustments might be necessary.</p> <p>Perfecting the allocation percentages is secondary to getting started. Over time you will find the perfect percentages for your business.</p>
30	<i>My business is a brand new startup. When should I implement Profit First?</i>
	Immediately. The sooner you start with Profit First, the sooner you will master financial discipline and force your business to run efficiently. No matter how new or established your business is, you should not wait to implement Profit First.
31	<i>Does Profit First translate into personal finances?</i>
	Yes. This is explained in more detail in "The Profit First Lifestyle" section of <i>Profit First</i> , but the premise is the same. Set up multiple bank accounts: Income (for deposits only,) Vault (savings account to cover the unexpected,) Recurring Payments (for recurring fixed, varying, and short-term bills,) Day to Day (for groceries, school supplies, etc..) and Debt Destroyer (all money remaining after allocation to the previous four accounts goes into this account.) Then, determine your allocation percentages and your allocation schedule. Most importantly, STICK WITH IT , even when it gets hard.



Want to dive deeper into Profit First? Read the book!

PROFIT FIRST

A Simple System to Transform Any Business from a Cash-Eating Monster to a Money-Making Machine.

The success formula for business has always been: Sales - Expenses = Profit. The problem is, it's wrong. You are about to discover the profoundly simple, Profit First Formula that ensures your business will be profitable from your very next deposit forward.

[LINK HERE](#)



Ready for your business's profit to skyrocket?

Work with a Profit First Professional!

Profit First Professionals is an international network of extraordinary accountants, bookkeepers, and financial coaches who are not only masters of their trade, but have a vast amount of skills and experience in helping companies grow their bottom line using the Profit First method.

[LINK HERE](#)