loss. You can then take steps to correct the problems before your net losses run you out of business.

Preparing monthly income statements will encourage you to keep your ledger up-to-date and accurate. You will use the information in your ledger to prepare your income statement at the end of each month.

Income statements are made up of the following parts (we'll be using their call letters, A through G, when we place these parts in equations):

A. Sales: How much money the company will be receiving for selling a product.

B. Total Cost of Goods Sold: The cost of making one unit times the number of units sold. *Never disclose your Cost of Goods Sold.* Keep secret how much you are paying to make your product so you can sell it for a profit.

C. Gross Profit: Sales minus Cost of Goods Sold.

D. Operating Costs: Items that must be paid to operate a business, including:

D1. Fixed Costs.

D2. Variable Costs.

These items include Utilities, Salaries, Advertising, Insurance, Interest, and Rent (referred to as USAIIR).

E. Profit Before Taxes: A business's profit before paying taxes but after all other costs have been paid.

F. Taxes: Payments required by federal, state, and local governments, based on a business's profit. A business must pay sales, income, and other business taxes.

G. Net Profit or Loss: A business's profit or loss after taxes have been paid.

Remember Hector's small business, described in Chapter 1? Let's say Hector finds a wholesaler looking to unload some ties. Hector buys twenty-five ties at $2.00 each and sells them all at $4.00 each. His revenue is $100.00. He spent $24.00 on flyers to advertise his ties. The income statement quickly shows whether Hector is making a profit.