

The Language of Business – In-Class Exercise (KEY)

Classify each of the following items associated with Tim’s lawn-mowing business under the appropriate term(s).

- | | |
|---|--------------------------|
| A. Revenue | F. Asset |
| B. Operating Expense (Variable Expense) | G. Account Receivable |
| C. Overhead Expense (Fixed Expense) | H. Account Payable |
| D. Gross Margin | I. Liability |
| E. Profit | J. Equity (or Net Worth) |

- F Tim’s 2 riding mowers, valued at \$4,250 each.
- A \$2,000 paid to Tim for his mowing services this week.
- I \$3,000 remaining on the loan used to purchase one of the riding mowers.
- G \$1,500 that Tim’s customers owe him for mowing their lawns “on account”. They will pay him within the next month or so.
- H \$500 that Tim owes the supply store for parts to repair his mowers.
- B \$750 that Tim paid to his hired worker for this week’s wages.
- C \$2,000 insurance premium payment for auto insurance coverage for the year.
- I Tim wants to borrow \$2,500 to buy attachments for his mowers. He doesn’t have the cash on hand, so he will try to borrow this money from a lender.
- D For the month Tim received revenues of \$5,000. He had variable expenses of \$2,800 for fuel, parts, and hired labor. He says, “I made \$2,200 this month.” What is the term for that \$2,200?
- J Tim’s truck has a market value of \$18,000. He still owes \$4,000 on the loan he used to purchase the truck. What is the term for the \$14,000 difference between the market value of the truck and the remaining loan balance?
- B Tim bought \$1,400 of fuel and parts for 2 weeks of mowing.

Use the following information to help Tim understand the financial side of his business:

For the entire year of 2016:

Tim mowed 800 lawns at an average price of \$50/lawn

He paid for the following items:

Fuel - \$6,000

Advertising - \$1,000

Office Rent - \$12,000

Parts & repair costs - \$2,000

Property taxes - \$2,000

Hired Labor for mowing - \$8,000

Interest on mower loans - \$500

Calculate the Total Revenues for Tim's business = **800 lawns x \$50/lawn = \$40,000 revenues**

Calculate the Total Operating Expenses for the year = **\$6,000 fuel + \$2,000 parts + \$8,000 labor = \$16,000**

(Only include the costs that change as the number of lawns mowed change)

Calculate the Total Overhead Expenses for the year =

= \$12,000 rent + \$1,000 advertising + \$2,000 taxes + \$500 interest = \$15,500

Calculate the Gross Margin for Tim's business for the year

Gross Margin = Revenues – Variable Expenses = \$40,000 - \$16,000 = \$24,000

Calculate the Gross Margin per Lawn for Tim's business.

= \$24,000 / 800 lawns = \$30/lawn

This indicates that Tim is earning \$30/lawn above his variable costs – this margin can be used to pay for the overhead expenses of the business.

Calculate the Profit (or Net Income) for Tim's business for the year

Because Tim did not include a salary for himself, the profit for the year is what he can pay himself.

Profit = Revenues – Variable Expenses – Overhead = \$40,000 - \$16,000 - \$15,500 = \$8,500

Tim thinks the market value of his business assets is \$30,000. He owes a total of \$12,000 in loans and accounts payable at the moment. Calculate the total equity of Tim's business.

Equity = Market Value of Assets – Liabilities = \$30,000 - \$12,000 = \$18,000 of equity