Andrew: This session is about how to transform any business from a cash- eating monster to a money-making machine. It's led by Mike Michalowicz, a founder of two multi-million dollar companies which he built and sold, and he transitioned to writing books and teaching.

His latest book is called "Profit First," and that's where I got the title for the session. The subtitle from the book is "A simple system to transform any business from a cash-eating monster to a money-making machine."

My team and I . . . by the way, I should say my name is Andrew Warner. I'm the founder of Mixergy, where proven founders teach. And the team here at Mixergy pulled out of the book a collection of tactics that we think you'll be able to apply quickly and get results from. And hopefully if you like those and you find them helpful, you can go and get the book "Profit First."

Mike, welcome back.

Mike: Andrew, it's just great to be here again. I love that you do this with me. So thanks for inviting me back.

Andrew: Me, too. Thanks for being here even though apparently the word "transform" still is too tough for me.

Mike: [??]

Andrew: But I'm working on becoming more pro.

Hey, you did something really cool. You sold your company, and then you brought . . . you bring this up, not this specific one. But this is the car you got. What car is that?

Mike: It's on my screen, yeah. I presume it's a Viper.

Andrew: A Viper.

Mike: Oh my God, and that's hauntingly similar. Mine was a darker blue. It's a GTS. That's a 2001. Like, actually, I'm sorry, that's not 2001. That's '97.

So I . . . after I sold my second company, I was like, "Oh, okay. Now it's time to play out all my little college fantasies."

Andrew: Mm-hmm.

Mike: And one of them was to get that car. So I got that exact car you're looking at, with a darker blue and a more current year. And thought that it was important for me to show off my wealth and my success through trophies.

That was just one. I got an LR3 Land Rover. I got the 7-series BMW. I moved into an

expensive town. I joined the club, all these things to show my success to the world.

Andrew: Yeah.

Mike: And I have to summarize by saying I became a dick, a big, big dick.

Andrew: You mean, you were a jerk to people.

Mike: A jerk, yeah, to people.

Andrew: Okay. What kind of things did you say to them? "Here's $5. Wipe my butt"?

Mike: Yeah, right, well, that was one of them. No, I didn't say things. I felt things.

Andrew: Oh, okay.

Mike: So if you and I ran into each other in the street, Andrew, and you were telling me about your business, in my head I'd be like, "Ugh, here we go, another pathetic soul."

Andrew: Ah.

Mike: "They don't know how to be successful. I'm the genius in the room. Just listen to me. And if you don't believe it, look at all the crap I'm accumulating."

Andrew: Oh, I see. I get it. Yeah, and you feel like you've earned it, because, you know, you really put in the hard work. You want to treat yourself.

What does a Viper cost?

Mike: New, at the time, I think $85 or 90,000. The LR3 was $100,000. BMW, $100,000.

Yeah, it was . . . you know what it was? It was just . . . I thought that wealth was the stuff we showed, and not something inside. And when I finally sold a company to have it, I felt like it was time to show off my trophies.

I've subsequently come to realize that well-dressed poverty is still poverty. Like, when we still have an impoverished mind, it doesn't matter what we look like. I still didn't have the right mentality. I thought I did. I didn't.

Andrew: So what happened to your bank account as a result of all these cars and spending?

Mike: Yeah, so that's not the only way I spent. After selling my second company, I was like, "Oh my God, I know the formula to grow companies. I'm going to become an angel investor. I'm going to invest in all these companies."

Quite frankly, I became the angel of death. Every time I put money into a company, I

was destroying it, it seems. And I started or participated in the launch of about 10 companies over about 10 months, and every single one . . . except for one. But every single one except for this one was done, was a failed venture, within six months to a year.

And I remember I was spending money so quickly, these businesses were out of business and I just kept on throwing money at it. And it took me a mere two years to lose everything. I mean, literally every penny I had made.

Andrew: Wow.

Mike: So people go, "Oh, Mike, you know how to grow businesses." I'm like, "Yeah, well, that took me 15 years. I know how to lose money even better than that. It only took me two."

Andrew: You know what? And I think a lot of people in the audience might say, "You know what? I'm not going to spend money on a Dodge Viper. I'm not going to buy myself a BMW and all these other cars."

Mike: Right.

Andrew: But where we do often run into trouble is where we make seemingly good business decisions, like investing in other companies for you. Or for others, it's buying an office, or investing in certain kinds of ads, et cetera. Seemingly reasonable decisions that end up causing trouble because we don't judge them properly.

And we're going to talk about, in this session, how to judge them properly.

Mike: Yeah.

Andrew: After you did all this, after you did so much of what you're going to talk to us, did you end up okay, or are you still now with no money in the bank and just a memory of the car?

Mike: Yeah, well, memory of the car, but money in the bank, right? So I am in a much better position than I've been in my entire life. I have built a profit habit.

So I used to believe profit was an event. I called it, you know, pump and dump. That's the popular term. I'd build a company fast, sell it. That's how you make your money.

And that's what's kind of perpetuated in the media. You build a company. It doesn't matter if it makes money. You build Twitter. It can fail. Until you sell it, and that's where you make your money.

Andrew: Right.

Mike: So that's what I was doing.

Today, I have a whole different vantage point, I believe. A much healthier understanding of what profit is. And it's not these events. It's a habit. It's a daily habit.

Andrew: Okay. And we're going to talk about how you did that. And here are some of the ideas from the book.

The first is "get your credit cards reissued." What do you mean reissued, and why is that such an important thing to do?

Mike: Oh my God. So . . . well, as I was running out of money in my life, but also in my business, I believed in the old adage "it takes money to make money." So I just took other people's money. Credit cards. And was spending that, and hoping I could turn.

And we've got to realize that borrowing money from a credit card company is no different than borrowing from a friend. It's other people's money. It's very easy to spend.

One habit I think every business needs to have, everyone needs to have, is get rid of the credit cards and go to debit cards. Because when you use a debit card, every time there's a transaction, it immediately comes out of your business bank account, or your personal bank account. You feel the pain immediately. And now it's no longer other people's money. It's your money.

And just that little, subtle change is a huge behavioral change. Now my spending . . . I'm a lot more cautious. "Whoa, whoa, wait, wait. I'm not buying that software. I don't want to spend my money." But when it was credit card? "Ring, ring!" So changed . . .

Andrew: You know, one of the cool parts about having it reissued is . . .

Mike: Yeah.

Andrew: So we found this photo of you . . . this is really your chest here, right?

Mike: So . . .

Andrew: Right?

Mike: Yeah, that really is my chest hair.

Andrew: Not your chest hair. This is your chest here, is what I meant to say.

Mike: Oh, chest here. And my chest hair.

Andrew: And your chest hair. And you're a fit guy. And one of the reasons you're a fit guy is you go to the gym.

And of course when we go to the gym, we have to give them a credit card -- or we can

do a debit card -- and they charge that card month after month after month.

Mike: Right.

Andrew: By having that card reissued, you stop that ongoing monthly expense. When you got the new card, you had to decide, "Do I want to give this to the gym or not?" And what did you decide?

Mike: Yeah. So that was my exact experience. I joined the gym. I had a gym membership.

Andrew: Mm-hmm.

Mike: And what happens is these recurring charges, I lost sense of this. I stopped going to the gym, because I just stopped going, but I forgot that there's ongoing costs were going on.

When I changed cards, when I canceled my credit card and put on my debit card, all of a sudden my phone starts ringing from all these vendors I haven't heard from in years. "Hey, we can't process your payment. Are you still going to be part of the gym?"

I'm like, "I am part of the gym? I totally forgot."

Andrew: Yeah.

Mike: But this is true for . . . a CRM I forgot I was using, and all this other stuff.

So what happens . . . there's these recurring we invoke in our business that at the time made sense, but sometimes we forget we even have them. By ditching the credit cards, it's a full reset, and a lot of these things you aren't aware you're doing all of a sudden comes right in front of your face, and you are presented with a decision. Is this something that's still appropriate for my business, or is this a gym membership that I'm not using, and I'm working out in my house now? I should cancel it.

Andrew: I see. Yeah. And there's a drastic decision. You make that one decision one time, you get a new card, and suddenly all those recurring payments stop, and you get to reanalyze whether you want them or not.

Mike: Exactly.

Andrew: Fair enough. All right. Onto the big board. And the next big idea we want to talk about is to perform an instant assessment so you can figure out the numbers that will make your business profitable.

And sometimes this is where I think we sometimes delude ourselves. You were at a period in your life where you were near bankruptcy, and you said, "You know what? I'm going to look at all my expenses." And one of the expenses was office expense.

What happened . . . do you remember what your office expense was, and what you did to it?

Mike: Yeah. So I ran through this instant assessment. I have it in "Profit First." I think we were talking about showing that a little later on.

Andrew: Yeah.

Mike: And, all right, so basically, what this instant assessment does is I analyzed all these companies, from small start-ups -- a couple, you know, thousand dollars, brand-new start-ups -- to $50 million companies, and everyone in between, and discovered what healthy companies, the healthiest of companies, run at, and what kind of profits they make, what the owners get paid, what the tax liabilities are, blah, blah, blah.

And what I learned about was there expenses. And some of the healthiest companies, of their gross revenue . . . say a company makes -- round numbers -- a million dollars a year. They have about a 30% operating cost. So that means they get a million dollars in sales, but only $300,000 is sent to pay rent, pay employees, etc. Thirty percent.

Well, I ran this number against my business, and found that I had 80% cost. And that was not even considering my pay. So a million dollar business, I had $800,000 going out to rent and employees and so forth. And then with the remainder, I was trying to pay my taxes, and then pay myself, and I had no profit.

Well, what I discovered was when I ran this, that a lot of my expenses which I thought were pretty reasonable -- I only had $1000 a month in rent -- that really, my business now is shaking and screaming at me, saying, "You can't afford that stuff. Mike, your business isn't at the size to afford this."

So what I did specifically with my office, when I thought $1000 was fair, but ran this assessment and said, "No, I can't afford the costs I'm incurring." I cut my cost down to zero for office space.

Actually, the story I have in the book. I moved into a factory that was owned by a friend. He manufactures cookies. Gave me free office space. Just as good as any other office space. Plus free cookies. So that picture you have is kind of like mid-cookie. It gets worse after.

Andrew: You mean the one where we saw your chest hair and chest hair.

Mike: Yeah. My chest hair and the beginning gut there. You see the gut rolling down the sides there.

Andrew: Looks good.

Mike: Yeah.

Andrew: So here's what I'm thinking.

Mike: Yeah.

Andrew: You used to have $14,000 a month in office expense. You said, "Great. I'm going to cut that down to $1000."

Mike: Right.

Andrew: That seemed reasonable. And only after you did this in-depth analysis did you realize -- tell me if I'm wrong -- only after then did you realize, "That is not enough. I have to take it down to zero. I might be feeling proud of myself for going from 14 to 1000 a month, but that's not enough." Right?

Mike: Exactly it. And the key word you say, Andrew, is reasonable. You know, reasonable isn't good enough. If you want to grow a healthy business, you have to be unreasonable. You have to find ways to get the same things done with way less cost instead of . . .

Andrew: So the part that I didn't understand in the conversation right now . . . and I do have the instant assessment, I thought we could go over in a moment. But can you just help me understand what you were saying earlier about gross profits versus net profits, and what . . . how . . . why wasn't the $1000 a month enough? How did you figure that out, that cutting to $1000 wasn't enough?

Mike: Yeah. So the assessment of a business that wants to be healthy is real simple. You take your revenue -- what your total revenue is -- and you can run it . . . there's a free download that you're offering with this chart. You run your revenue number against these percentages.

And the chart will tell you very quickly, if you have a million dollar business, for example, that you can run an operating expense upwards of 30, maybe 40%. I can't remember the exact number off the top of my head.

But because the other dollars have to be allocated towards stuff. Towards tax responsibility, pay, perhaps buying capital equipment, and so forth.

So the problem that most businesses have is that we have a million dollar business, we think that we have a million dollars for expenses. We can just run our business off a million dollars. And that's not true. Because if you run your business to cover expenses, there'll never be profit left over.

So this instant assessment tells you what you really have available for expenses. It's kind of like a bucket of cold water in your face. It's a wake-up call saying, "You can't afford what you're doing right now. You have to find a better, more innovative way."

Andrew: So this was the PDF you were talking about earlier.

Mike: Yeah.

Andrew: With the Profit First Instant Assessment. We can give this out to the audience. Which, this is the step-by-step instructions. Here is I think what you were talking about, Figure 1 and Figure 2. Right?

Mike: Yup. That's the charts. Yeah.

Andrew: Okay. So if we're looking at here at a million dollar business, that's Column C, maybe.

Mike: Exactly.

Andrew: Right. So Column C tells me real revenue, 100%. Profit is 15%. Owners' pay, 20. Tax 15, et cetera.

Mike: Yeah.

Andrew: What does all that mean?

Mike: Yeah. So if you're running a business . . . and those are the exact numbers. This is what I studied with healthy businesses. A healthy $1 million business . . . and I know this is a generalization, and most people say, "My business is unique." But you know what? It really isn't that unique.

Of all these businesses in all different fields, I discovered that a million dollar business will be taking a profit of about 15%. So at the end of the year, that company's taking $150,000 in profit distribution. Now, that's above and beyond the owners being paid $200,000.

And then taxes. You know, we shouldn't be paying taxes ourselves. The business was designed to serve us. So $150,000 is reserved for corporate tax responsibilities and personal tax responsibilities of the owner. What that leaves, at the end of the day, is 50%. And that 50% is used to run the rest of your operations. It's payroll, everything.

What this forces you to do as a business is you have to be efficient. And if you don't pre-allocate your money toward profit and paying yourself first, what the default nature of all entrepreneurs is that 100% of top line goes to 100% of expenses. And these companies now survive check by check, barely getting by, because the money that comes in instantly flows out.

This instant assessment tells you where to stop it, where to allocate your money, before you pay a single bill.

Andrew: All right. So let me do it again with a different set of numbers. I'm just going to

wipe that out. Here's what . . . let's suppose someone is in this column right here. Column 1. They're making roughly a quarter million a year.

For them, you're saying all of their expenses should amount to 30% of revenue. All of those expenses.

Mike: Exactly.

Andrew: And anticipate taxes of roughly 15%.

Mike: Right.

Andrew: Anticipate taking home . . .

Mike: 50%.

Andrew: . . . half the revenue as profits.

Mike: Exactly. For your own pay. Yeah. And the reason . . .

Andrew: Uh-huh . . .

Mike: The reason . . . and, yeah, 5% profit.

Andrew: Five percent profit. That's what your business should be doing, but it's not that 100% of your expenses can towards running the business. You just have to think in your mind 30% of the money coming in is going to expenses. If I get to 50% I've gone too far.

Mike: Exactly. The reason this happens is that's a smaller company. You're basically a free lancer at this mode. If you have 250,000 or less, chances are you are the only employee or maybe a part-timer. As the business grows, you have to put the infrastructure in and the people. So the things start shifting. So that's the ideal numbers.

The other tip I have for people is this is ideal numbers, but if your business right now is running check by check, if you implement those numbers immediately it's like taking a frozen mug and putting it into a hot oven. It's going to burst. So what you need to do is slowly move towards those numbers. I suggest starting out at a lower percentage point knowing that's what you're targeting. But every quarter, every ninety days, move it up, move it up, get closer to those targeted perfect percentages.

Andrew: All right. So on to the big board again. We're going to the next idea here which is to determine your profit allocation percentage and tell your accountant so you can get on a path to profit immediately. And you talk about the founders and owners of this company [??] and they did that, right?

Mike: Yeah, these guys are amazing. They found out about me from my first book, "Toilet Paper Entrepreneur" and I've got a good relationship. The guy in the center and

to the far right that's George and Jose. They built this company, and they started doing Profit-First. There's target allocation percentages with just that chart which we went over just now, but I have an alternative life. You don't want to go with my chart because it's, you know, "too generic."

You can also go on to Yahoo Finance or Google Finance and look at public companies that are playing in your sector. So if you provide coaching services, look at training companies that are public. If you're a law firm, look at a public law service firm. And you'll find out the healthiest of companies, what their numbers are and you can target those. Not surprisingly those target allocation percentages for profit, pay, and so forth, you'll find to be very similar to the chart that we just showed you.

That's an alternative way of finding the specific target allocation percentages for your market.

Andrew: Got it. And when they did it, they went to 2%.

Mike: Right. So when Jose and George started, they realized in their market they could run a 15% bottom line and a 25% owners pay margin, but they said, you know what? We're first going to start with a 2% pay because the first step of this Profit-First mentality is to get into the habit of taking a profit first. What you're learning here is basically the pay yourself first process, something that we're supposed to be doing in our personal lives. But you need to apply it to the entrepreneurial side, to your business life.

And if you go full bore, you may not be prepared for it. You may have too many expenses going on. You may not be able to cut back fast enough, and now you're going to start borrowing. That's stealing from yourself. It's there for profit. You're going to take it back, and that defeats the system. The key is start small, build the profit habit, and slowly build it over time to bigger and bigger margin.

Andrew: So it was take 2% of the business out at first as profit.

Mike: Yeah, that's what I started. The last time I spoke to them a few months ago they're about 12%. But those two guys went on some wild vacations and had some amazing dreams come true for themselves in their personal lives because they built this profit habit.

Andrew: But it's 2% profit for the business, or 2% owners pay?

Mike: Those are different, profit for the business. You didn't realize as owner of a business you actually serve two functions. You're an equity owner. You're a stockholder, just like you'd own stocks in a public company, and you get dividends. That's your profit.

The second thing is you're also an employee as an owner. That's owners pay. You're paid to work inside the business.

Andrew: Okay. So for them it was profit for the business 2%. They still took money off

themselves.

Mike: Oh yeah.

Andrew: The business kept that profit and allowed it to grow in the future, and then they kept upping and upping that percentage.

Mike: Exactly. So they gave themselves healthily a 2% profit. They did quarterly distributions, again, just like a public company. When Bloomberg is announcing a 15 cents per share distribution, George and Jose were taking about $2,000 a share distribution for themselves and celebrate with it. We all should be doing that.

Andrew: All right. On to the next idea here from the book, and that is, to brainstorm ways to become more efficient. And you talk about UPS. I found this article about them. This is from their website. Let me zoom in. It says, "When in doubt, UPS avoids left turns," and they explain how and why they want to do that. This is from an internal document, I think.

Mike: Yeah, yeah, I include that in the book, and this is an amazing story of the power of a public company doing this, but any company can do this. UPS, just like any other business, is trying to maximize profitability. The wins for profitability happen in the minutia, the small elements. And what they realize is they just started measuring things that were going on and that their drivers a lot of time were idle. They drive up to a traffic light and sit there. They're trying to cross an intersection, they're sitting there. They realize that left turns can take up to ten times more time than taking right turns. You can turn right on red, you don't have to cross traffic when you take a right.

Andrew: Mm-hmm.

Mike: So once they realize this they say, 'What if we set up the navigation for each driver for each day so that their route is mostly or almost exclusively right turns?' And sure enough, they were able to make a big efficiency gain. Now the same driver can do five or six more stops. They can increase their productivity by 10 or 15%, by not taking left turns. Now they do all these efficiency, little steps forward in different areas, and by doing a lot of small improvements in efficiency they get one major efficiency improvement overall in profit increases.

Andrew: Do you have an example of how brainstorming like this helped a smaller company, a smaller entrepreneur come up with an idea that they wouldn't have discovered otherwise but saved then money on an on-going basis?

Mike: Oh, yeah, yeah. I'll talk about one company that I'm an investor in. It's a manufacturer of outdoor products. I own 25% of the company. I'm just going to reserve saying their name. What they do is, we make some certain products. And what we realize is that making a certain product requires rivets. That there's ten different rivets required. And what we did is we sat down with the entire team and this is critical. You as an owner may not know it, so we sat down with our entire team and we're a small shop.

Our entire team literally is five people. The guy on the floor to the owner, and everyone in between, we got together and said, "To make this product as well as we can takes ten rivets. But we also realize is we can do it with two rivets less, we're going to save serious money for each unit, about 50 cents a unit. But we make thousands and thousands of units, becomes real money. How do we cut this thing down by at least two rivets?" The team brainstormed, came up with a new way to fold in the material and it didn't require two less rivets, it required four less rivets now and was sturdier.

Andrew: Wow.

Mike: So what you have to do is just put out the questions of how do you get the same or better results with less material. My favorite question to ask is this: Whatever you do today in your business no matter what it is, how do you do double the productivity, double the results with half the cost? I know it sounds like an absurd question, but if you ask it, you may nail it, or you may find somewhere in between, but it will move you forward.

Andrew: That makes sense. And we're so resistant to doing that because it feels, if I were in the business that you just described, I would say, "Of course we have to have rivets. We want as many as possible so that we could have a really quality product." But as you say, sometimes folding it a different way requires fewer rivets, less time and just as good if not a better product.

Mike: Less time. Yeah, it was a snowball effect too. It wasn't just less material, right. It was less time too.

Andrew: All right. Onto the big board. Next big idea is create a stocking account so big purchases don't crush your business. You talk about JB in your book.

Mike: Oh yeah.

Andrew: JB who has a roof deck company. What's the name of the roof deck company?

Mike: it's called Roof Deck Solutions.

Andrew: Roof Deck Solutions. I think this is them, isn't it? What did he do? Is this them?

Mike: That's them. Yep, that's them, that's them. They make cool roof decks in Manhattan and different metropolitan areas. What they do is they go to those abandoned roofs on top of a building and they renovate it over. JB, his business is a multi-million dollar business, but one of the challenges going on is he has to buy a lot of materials.

So here's what you need to do. If you have a business that's material intensive, as revenue comes in, before you allocate to a profit and other stuff, the direct material costs you must reserve and put into a stocking account. Because ultimately you're going

to have to replenish those goods. He has to get the woods, the materials and so forth. So instead of just having one account, you have to have multiple accounts for different purposes with your bank. So I would set up a profit account, a owners pay account, and his case, I would set up a stocking account because he has to get more materials.

Andrew: You mean, literally a different bank account where we wire the money in on a regular basis. In his case, I think it was $250 that he kept doing every month.

Mike: Yup.

Andrew: And then when a big purchase comes in, you have that separate account ready to go.

Mike: That's exactly what this is. This is Grandma's old envelope method.

Andrew: Yeah.

Mike: What my grandmother did is get $100 of pay in a week, and she would put $5 for groceries, $10 for rent, $5 to give back to the community, blah, blah, blah and so forth. She always had enough money. If she needed groceries, she'd go to the grocery envelope and have enough money to buy groceries. It wasn't always the same amount of money. If it was little, she realized we're doing peanut butter and jelly this week. If it was a little more, we might get a roast chicken. But she would use the money that was available, and we all need to do this. Set up envelopes for different purposes.

Yes, we can use G/L accounts and accounting but the thing is, that's what logical people do. We have to realize that we as humans, entrepreneurs, we're not necessarily logical as much as we are emotional or behavioral. So by setting up all these different physical accounts that will give us the clarity of understanding what our money truly is available for.

Andrew: By the way, his work is stunning. I don't know if I can show enough of it here up on the screen here. Let me see if I can do it. Where is it?

Mike: His work is amazing.

Andrew: It's amazing. He's turning outdoors areas, you said, in Manhattan?

Mike: In Manhattan and Boston.

Andrew: I love this one. Let's see if we can show it. I'll zoom. This is like an outdoor shower out on a roof in Manhattan.

Mike: Yeah, and you know whose place that maybe? That maybe Jon Stewart from the Daily Show.

Andrew: Oh, okay.

Mike: That maybe his place. So a lot of celebrities do this for their custom space. So there are open public spaces that do this, but J.B. also does it. That's definitely Jon Stewart's place.

Andrew: This is Jon Stewart's place?

Mike: Yeah, you're looking at Jon Stewart from the Daily Show. That's his house you're looking at.

Andrew: Really.

Mike: His apartment in the city, yeah.

Andrew: Phenomenal setup, wow.

Mike: A lot of celebrities like this stuff too. And yes, really phenomenal cool stuff.

Andrew: I see.

Mike: If you have the means.

Andrew: Sorry? If you have means.

Mike: I said, if you have the means, it may be fun. [??]

Andrew: All right, so it makes sense the way that he was able to build his business and keep those big expenses from crushing him is by setting money aside every month in a separate bank account, not a separate entry in his QuickBooks, separate bank account.

Mike: Separate physical bank account. That's the mandatory step. Before this he was doing the old bank account method saying, "Oh, I have money reserved." But the natural tendency of most entrepreneurs is you look at your one checking account and you believe that money's available for whatever your next need is. So, J.B. was catching himself without enough money to buy materials and he was getting in real trouble. Simply by setting up a separate account and reserving the money there first, he doesn't get caught with his pants down.

Andrew: All right. Onto the next big idea and this one was a surprise, what happened to someone that you know, Ernie. The tactic is, you want to value profit over selling more so you can break out of the survival trap and you had someone who came in and did some lawn work for you. A guy who you're calling Ernie in the book to protect his identity.

Mike: Yeah, and I protect his name because I question if the business formationed [SP] properly. But I wanted to include his story because it represents what a lot of entrepreneurs do. It's called the up-sell and we've been told to do this. Ernie's my lawn

guy. He comes in and I'm in New Jersey. Fall is a big time for cleaning up leaves. He does it. He comes to my door and says, "Hey, Mike, there are leaves in your gutters. I'll gladly go on the roof and clean it out. Its only another 200 bucks." "Sure, do it." He goes up there.

He's up there. He comes back down, knocks on my door, says, "You know some of your shingles are coming off. I can replace those and I noticed your chimney's falling apart. I can fix that." "Sure." Another 500 bucks or whatever. He did it.

The thing was it wasn't his skill set. He didn't have the tools. He didn't have the labor. So he had to run out and get the resources to do it. At the end of the day he made some good money for sure on the top line, but he didn't make a profit. And his big bet was, "Well, I had to buy this different equipment and ladders and stuff to take care of Mike, but I'll make it up going forward."

Well, the problem was while he's up on the roof and trying to make the money on other things going forward, his blowers and rakes, and all that stuff is sitting idle on his truck. As we up-sell into more and more diversity we become more and more inefficient. So, the story I shared in the book is at the end of the day, yeah, maybe he took home 1500 bucks or 2,000 bucks that day, but when he's at the bar talking to the other lawn guys and saying how much money he made, and he made twice as much as they did, he's the guy who can't afford to buy the beer. Someone else is buying the round because they're doing one thing super efficiently.

Andrew: Yeah.

Mike: And that's the key to profitability. Be the master of one thing replicated over and over, be able to do it faster and faster, better and better, and you'll make margin profit, and you'll be successful.

Andrew: You know what? I see that in text so much. Consultants specifically, they'll come to me and they say, "I'm really good at installing WordPress. Do you want me to install WordPress for you?" "Yeah, absolutely. I don't want the headache of doing it. It's not that tough, but you do it."

Mike: Yeah.

Andrew: And they come back and say, "Well, I can also install all these plugins, do you want me to do that?" "Well, yeah, go ahead." And now they give me a price, they go do it, and they realize there's some conflicts in the plugins, so they have to go and figure that out. But before they finish figuring that out they say, "I can also get you a new design for the site." They're thinking, "I'll just go to WooThemes. I'll buy the design then I'll hire someone to edit it and make it look really nice." Again, more and more things and they end up doing nothing right. I pay them more and I hate them more.

Mike: Yeah, you're disappointed as a customer.

Andrew: Yeah.

Mike: It's ultra-inefficient. The first time you run into the problem you had to solve it. The second time you run into a problem you got to find the commonalities of that problem and it still takes time. It's by the hundredth time that you run into the same problem that then you get into the routine you can [??] with.

Andrew: Yeah.

Mike: But if you keep on diversifying what you do, every time you face a problem it's your first or second time, pure inefficiency. It's a loser. You make money after you hit the same problem 100 times over and know how to fix it every time perfectly.

Andrew: I don't want to be your guinea pig if I pay for that and don't tell me, I don't need the excuses that it's taking so long. That's one of my big frustrations with consultant companies. And I get why they do it. They have a customer, now they're told "grow that business." But you know, there's a limit to what you can do. Before you know it you're like Ernie.

Mike: It's a dangerous job. And by the way the shingles are coming off the roof. He hasn't done it before, it was inefficient. So I call him and say "Hey Ernie, it's not working can you come fix it?" He's like "Aw, God" he's like "I'm trying to go out and do leaves, uh, yeah I'll come there."

Andrew: And now you're the difficult customer.

Mike: Yeah. He's upset with me, he did a poor job up there, he's not servicing his other customers, he's losing other business to cater to something that he should have never done in the first place.

Andrew: Yeah and like you said he that things are going well because he's more money but he's the guy that ends up not being able to somehow not being able to afford to buy drinks. Alright, onto the final point that we pulled out here and that is to get an accountability partner who will help keep you profitable. You talked about this woman who did that. I've never seen this woman before. I know the company that she's a part of.

Mike: Oh, Jean Nidetch. Yeah she's the founder of Weight Watchers.

Andrew: Yeah.

Mike: That's the founder of Weight Watchers and that's her before and after. That's her before on the left; that's her after on the right. She's still alive today, still thin today! So you can see in that left picture that she had a weight issue into her 30s early 40s and the awakening moment for her was she was at the food store and someone came up and "Congratulations, I didn't know you were having a child!" And she wasn't, and she said "That's enough." Up to this point she had tried diet plans and sure enough diet

plans worked but then she went back into her habit and put weight back on. It never stuck.

What she found was she needed a support group so she founded Weight Watchers in her living room with other women that were struggling with their weight, and they stuck together. And as a team they were able to support each other through the process, and they were able to lose weight permanently.

Andrew: Yeah.

Mike: Same is true for our profit. You just learn the "Profit First" system in our video here together, and you'll be able to do it. You can, and you should. The problem is there's going to be a dark day where you need money because you have a new bill. It came in unexpectedly, and you're going to steal from yourself by taking money away from your profit account, not paying yourself as much, and that's when the system falls apart. You need an accountability partner or an accountability group.

I'll tell you the one thing you've got to do is your accountant . . . This is a person that's a trained professional. Like a trainer in a gym they know the numbers. They should be supporting you in driving profit in your business. And if your accountant doesn't do that, shake them and wake them up to this process to make sure they do start doing it or find an accountant that does.

Secondly, you should surround yourself with other entrepreneurs that are also driving profit first in their business because now you need a support group for each other. You need accountability.

Andrew: So if you want to start out small, first of all, read the book. And second, get an accountability partner, one person who holds you accountable. How often should they meet?

Mike: Yeah, I suggest meeting twice a month. I believe in getting into what's called a rhythm. I think we should pay our bills twice a month, do distributions twice a month. Every single day, not freak out in the moment. Get into a rhythm of doing this.

Andrew: And what happens in these meetings when they do it twice a month?

Mike: Well, what you do is you talk. You print out your bank statements. There's no BS'ing. At Weight Watchers, when you show up, you don't say, "Yeah, I lost weight." You get on the scale, and the guy looks at it and says, "Yes, you did lose weight." With your accountability partner you print out your bank statement for your profit account and say, "Here's what I'm doing." And so there's no BS'ing around about it, and then you talk about strategies to improve profit and drive it forward for each other.

Andrew: Got it. Great. So, again, the book is called . . . I'll bring it up on the screen . . . "Profit First." The website you guys are looking at right now for the book is ProfitFirstBook.com. Mike, I obviously didn't cover everything from the book. We

covered some of the big ideas from it. If there's one thing that people, when they get the book should jump into that I didn't cover here today, what would you recommend? What's one of the things that they should look at?

Mike: Just one thing is to realize that there's a flawed formula. It's called the Gap Formula. It's generally accepted in accounting principles. It says that sales minus expenses equals profit. It's been the foundational profit formula since the beginning of business, and I'm here to tell you it's total bull shit. It's the worst formula in the world because it says sales comes first, expenses come second, and profit is the remainder. It's a leftover. It's an after-thought which is absurd.

The core principle that I want you to walk away with is this. Sales minus profit equals expenses. Sell as much as you can. Take your profit first, and run your business off the remainder. The expenses is the remainder, and you'll become more efficient and more innovative when you have less money available for your expenses.

Andrew: Oh that is a mindset shift. I paid so much money to go to college so I learned the opposite side of it. It is a mindset shift, and it does make so much more sense for younger businesses. Thank you so much for coming on here and talking about this. Again, the website is ProfitFirstBook.com, and if you can spell his name, MikeMichalowicz.com. And, of course, we'll link over to it. I love this where you describe where you hired a professional voiceover artist to talk about . . . to say your name.

Mike: Oh yeah, yeah, yeah. He makes fun of my name. Well, no one can get it right, so make your weakness your strength. So if no one can say my name, might as well make fun of it.

Andrew: I love how you have fun with it. Thank you again for coming back here. Thank you all for being a part of it. If you've got anything of value, come back and let me know, let Mike know. And let us know what you ended up doing with it.

Congratulations, guys, for being a part of it. Bye.