profitfocuspartners
BUSINESS AND TAXATION CONSULTANTS
Your Business Partner

THE LANGUAGE OF BUSINESS RECORD KEEPING

Accounts Payable
Money owed to creditors (suppliers of goods and services on credit) and due for payment.

Accounts Receivable
Money owed to a business by its customers (i.e. debtors) for goods and services sold or supplied on credit.

Accrual (method of record keeping)
A record-keeping method in which profit or loss is measured by comparing income and expenses. In effect, the accrual method is not based solely on the movement of cash.

Accumulated Depreciation
The total of depreciation written off an asset since its purchase, i.e. during its life in the business thus far.

Aged Debtors Schedule
A list of debtors shown in groups according to the length of time the debts have been owed.

Assets
Items of property owned by a business, and what is owed to it by customers (e.g. cash balances, buildings, machinery and equipment, accounts receivable, inventories and goodwill). Assets are the resources to be used by a business.

Australian Business number (ABN)
A unique identification number required for certain types of business to help in their dealings with government departments and agencies.

Bad Debt
Money owed to a business (that is, accounts receivable) which cannot be collected and is written off as an expense.

Balance Sheet
A financial statement which shows the assets in which a business has invested, and the sources of those invested funds. It, therefore, indicates the net worth of the business to its owner(s).

Bank Overdraft
An arrangement with a bank by which a business is allowed to overdraw its cheque account to an agreed limit. It is a form of loan to a business and is, therefore, a debt or liability, since it must be repaid.

Bank Reconciliation
A procedure whereby the final balances shown on a bank statement and the firm’s cash book (or summary) are adjusted to show the true current cash position, by making adjustments for transactions recorded in only one of the two sets of records (e.g. cheques not presented for payment at the bank).

Book (or written down) Value
The ‘value’ of a fixed asset in the books of a business, expressed as cost less all accumulated depreciation written off.

Break-even Point
The level of sales or output at which income and total expenses are equal and there is neither profit nor loss.

Budget(ing)
Business plans in financial terms; a statement of likely future income and expenditure (or of cash receipts and payments) indicating a forecast profit or loss (or cash surplus or deficit) for a future period of time.

Capital
The funds invested in a business by its owner(s), also known as equity capital. The term is also used to refer to all funds available to a business to invest in assets and, therefore, includes both equity capital and debt capital (i.e. borrowed funds).

Capital Expenditure
Money spent on buying fixed assets.

Cash Budget
A forecast of the amount and timing of the firm's cash receipts and cash payments for a future period of time, adjusted for any unusual items.

Cash Discount
A discount allowed to customers for early payment of their debts.

Cash Flow (Liquidity)
The flow of cash into or out of a business. Liquidity is a measure of how well a business can pay its debts from its cash flow (which can include borrowed funds I needed). Negative cash flow occurs when cash payments exceed cash receipts.

Cash Flow Statements
A statement summarizing a firm's cash flows, showing the cash balances at the start and end of the period.

Contribution Margin
The difference, shown either in dollars or as a percentage, between a firm's sales income and its variable costs. The contribution margin must be large enough to cover all fixed costs and provide a profit.

Cost Of Goods Sold (COGS)
The cost of goods actually sold during any trading period, calculated as follows Cost of goods in stock at start of the period, plus the cost of goods purchased or manufactured (including freight, insurance and similar costs), less the end-of-period stock (at cost price).

Cost Price
The total cost of buying an item of merchandise or raw materials, which includes the invoice cost and any freight, insurance, import duty and other costs associated with the purchase.

Cost-Volume-Profit Analysis
Analysis of the relationship between a firm's costs, its sales or production volume and its profit. This is also widely known as break-even analysis.

Credit Note
A source document used when the account of a charge customer (i.e. debtor) is to be credited because goods were returned or an allowance is made for some other reason.

Creditors
Those to whom money owes.

Current Assets
Cash and other assets that can be changed into cash fairly quickly if needed, such as accounts receivable and inventories. Current assets are part of a firm’s working capital.

Current Liabilities
Debts that need to be paid within a month or two, such as trade creditors (accounts payable).

Debt
An amount of money owed by a debtor to a creditor.

Debtor
One who owes money (to a creditor).

Depreciation
The loss over time of the value of fixed assets due to aging, wear and tear and general obsolescence. Depreciation is a tax-deductible business expense.

Direct Labor Costs
The cost of labour (i.e. wages) involved directly in the manufacture of goods in a factory or workshop. Direct labour costs can be directly identified with making a particular product or with a particular production run.

Direct Materials Costs
The cost of materials and components used in manufacturing of product. Direct materials can be identified with a particular product or production run.

Dividends
A payment to company shareholders of their personal share of the company’s profit which it has been decided to distribute.

Drawings
Cash or goods taken out of a business by its owner(s) in the case of a sole proprietor or partnership. Drawings represent a distribution or withdrawal of part of the profit by the firm’s owner(s).

Equity / Owner’s Equity
An owner’s financial interest in a business or property. It is also known as the net worth. If a business has total assets worth $100,000, and owes $30,000 in debts and liabilities, the net worth to the owner(s) is $70,000.

Expenses
The cost of buying, renting, leasing and using resources needed to operate a business and earn income – wages, interest, insurance, etc.

Factoring
A means of collecting accounts receivable promptly. A finance or factoring company buys the book debts of a business for a price less than their book value, and then collects the full value.

Financial Ratios
Calculations used to assess the firm’s financial health.

Financial Statements
Financial reports and summaries outlining the firm’s financial situation and performance. Key financial statements are the Profit and Loss Statement, Balance Sheet and Cash Flow Statement.

Financial Structure
The mix or proportions of each source of business funding used. The two sources are equity funds (from owners) and borrowed funds (from lenders). The proportion of borrowed funds used to invest in assets is the gearing ratio.

Fixed Assets
Assets of a ‘permanent’ nature, such as business premises, equipment, machinery, furniture and fittings, and motor vehicles owned by the business and not intended for resale as part of normal trading activities.

Fixed Costs
Costs which remain constant over the normal range of activities (i.e. sales and output). Examples are rent, depreciation, rates, insurance premiums, office costs and stationary.

Forecast
A prediction of future events or outcomes, such as cash flow, sales or profits. Most forecasts are made by extrapolation (i.e. extending) from past trends over past financial periods, and then making adjustments for known and likely present and future variations.

Funds (Borrowed)
Any money borrowed by a business is a debt to be repaid with interest. All money contributed into a business, whether borrowed or invested by owners (i.e. equity) is often referred to as funds.

Funds Statement
A summary of the sources and uses of the funds in a business.

Gearing Ratio
The proportion of a firm’s assets funded with borrowed money. If a firm’s assets are worth $100,000 and borrowed funds total $60,000, the gearing ration is 60%.

Goods & Services Tax (GST)
road-based tax on the purchase of most goods and services. Liability for GST flows along the supply chain from manufacturer to the end buyer, so that it is the end customer who pays it. The GST is collected by each business in the supply chain on behalf of the government.

Goodwill
The monetary value of the favourable attitudes of customers about a business. Goodwill is recorded as an asset only when the business is bought as a going concern and goodwill is paid for by the buyer over and above the cost of the tangible assets. Its value is based on estimated or forecast future profits above what might be regarded as ‘normal’ earnings for that type of business.

Gross Margin / Gross Profit
The difference between a firm’s sales income and its cost of goods sold. Also known as ‘gross profit’. Gross margin must be sufficient to cover all other costs and provide a profit.

Incremental Costs
Any cost which increases on small increments as the level of activity increases. This mainly applies to variable costs.

Information System
The system of documents, books, summaries, statements and reports installed in a business to generate up-to-date and accurate information about the health and performance of a business.

Input Tax Credit
A rebate of the GST included in the price of allowable acquisitions bought for the use in a business.

Insolvency
A situation in which a person or business is unable to pay debts as they fall due. This is not the same as being bankrupt, but insolvency may lead to a refusal or inability to pay debt, which, in turn, may lead to bankruptcy. Poor cash management can lead to insolvency, as can poor marketing.

Installment Income
Business income for a trading period for which a PAYG installment is being paid.

Installment Rate
The rate of tax payable in installments to the Australian Taxation Office. The rate is determined by the ATO.

Intangible Assets
Assets which exist only on paper, unlike such tangible assets as machinery and motor vehicles. Examples are goodwill and patent rights.

Interest
The cost of borrowing money.

Inventories
Stock of goods (merchandise or raw materials) bought either for resale (by retailers and wholesalers) or for use in manufacturing or providing services.

Inventory Control
Control over the ordering, purchasing, receipt, storage and issue of all inventories, whether merchandise, raw materials or partly finished goods.

Journals
Books of account used for recording details of various types of transactions on a daily basis, for example cash receipts and payments, credit sales and credit purchases.

Ledgers
Books of account in which summaries are kept of entries first recorded in the journals. In a double entry record system, a General Ledger is kept. Every business should also have a Debtors' Ledger and a Creditors' Ledger.

Leverage
The use of borrowed money to finance a business.

Liabilities
Debts; money owed by a debtor to a creditor.

Liquid Assets
Assets which can be converted into cash quickly and easily.

Liquidity
The ability of a business to pay its debts as they fall due. The opposite of liquidity is insolvency.

Loan Principle
The amount actually borrowed and which must be repaid.

Long-Term / Non-Current Liabilities
Debts not requiring payment in the near future.

Margin
The difference between cost price and selling price, expressed in dollars or as a percentage of selling price. Margin is an abbreviation for 'margin on gross profit' or 'gross profit margin'.

Mark-Up
The amount added to the cost price of goods and services to arrive at the selling price. Mark-up can be expressed either in dollars or as a percentage of the cost price.

Merchandise
Goods bought for resale (by retailers and wholesalers) or finished goods manufactured and ready for resale. Unsold merchandise at the end of any trading period is known as 'stock on hand'.

Mortgage Loan
A loan to buy real estate by using the premises (i.e. building) as security for the loan.

Net Present Value
The difference between the initial cost of a fixed asset and the total of the present values (i.e. in present dollar values) of the future net cash flows produced by that asset.

Net Profit
The earnings of a business from sales or any other type of income (such as fees, commissions and rents) less all expenses incurred in earning that income. Net profit is the owner's financial return on the equity, for risking the financial investment in the business and for the necessary contributions of work, time, experience, expertise, qualifications and overall responsibility. A net profit increases the owner's equity in the business; a net loss will decrease it.

Operating Profit
The profit form a firm's normal trading activities.

Overdraft
Borrowed funds provided by banks, in the form of approval for a customer to overdraw their cheque account.

Overhead Costs
All operating costs except cost of goods sold and direct labor costs (i.e. employee wages)

Partnership
A business owned and operated by more than one person, but not a company. By law a partnership is not a separate legal entity and, if necessary, all partners are personally liable to help pay the partnership's debts.

Pay As You Go (PAYG)
A system of paying taxation (replacing PAYE, PPS, company tax installments and provisional tax) as from 1 July 2000, which requires some tax payers to pay income tax installments on income earned.

Payback Period
The time (usually in years) it is forecast it will take to recover the investment in a fixed asset from the net cash inflows it produces.

PAYG Installments
The amounts to pay (usually quarterly) to the ATO as tax on business income. This is calculated by multiplying instalment income by the prescribed instalment rate.

PAYG Withholding
Periodic payments to the ATO of all amounts deducted from payments to others. These will usually be deductions from employee wages and salaries (the old PAYE) and from subcontractors (the old PPS).

Petty Cash
A sum of cash set aside for buying small (i.e. petty) items such as postage stamps, small stationary needs and other small office requirements. The petty cash supply is topped up at regular intervals by drawing a cheque and cashing it.

Prepaid Expenses
Payments made in advance for future services. An example is paying an annual premium for insurance which provides cover for the year ahead. A prepaid expense is an asset.

Profit
A financial gain calculated by subtracting all expenses from income earned.

Profit & Loss Statement
The financial statement which summaries all of a firm's operating expenses and all of its income, the difference being the net profit or net loss for the trading period.

Private / Proprietary (Limited) Company
An association of people who have invested share capital to form an incorporated business which the law recognises as having an existence separate from its shareholders. There is a limit of 50 shareholders and restrictions on selling shares. Each shareholder's liability for the company's debts is limited to the cost of the shares they hold. For example a shareholder with 1000 shares of $10 each has a total liability of $10,000. The continuation of a company is not affected by the death or retirement of any shareholder.

Ratio
A figure which expresses the relationship between two things, for example if a sales person visits 40 potential customers and this generates eight sales, the ratio of sales to calls is 8:40, 1:5 or 20%.

Raw Materials
Materials to be used in a firm's production manufacturing work.

Retained Profits
That proportion of net profit that is kept (i.e. invested) in the business rather than being withdrawn by owners as drawings or paid to shareholder as dividends.

Revenue
Income earned by a business from sales, fees, commissions and other sources.

Sale
A business transaction in which goods and / or services are exchanged for money. A cash sale involves the immediate transfer of money from purchaser to seller, whereas a credit sale creates a debt owed by the purchaser to the seller. In the seller's records, this debt is called either a 'debtor' or 'account receivable', which is converted to cash when paid.

Shareholders' Funds
The capital subscribed by shareholders to form a company.

Small Business
A business which (1) is managed by its owner(s) in a personalised way; (2) is independent of external control; and (3) is relatively small in its industry. No common agreement exists about the numerical size (number of employees) of a small business, although for 'official' government purposes in Australia it is one hundred for manufacturers and twenty for all others.

Sole Proprietorship
A business owned and operated by one person.
Solvency Being able to pay one's debts as they become due.

Source Documents
All documents which originally record the details of all business transactions – receipts, cheque butts, invoices and credit notes.

Stock
The value of all merchandise, raw materials and partly finished goods at a specified date, being held for resale, production or further conversion.

Supplies
For GST purposes, the goods and services sold by a business to its customers. Some supplies are taxable and others are GST-free.

Tax File Number
The number required for every tax payer, as a unique identifier for all dealings with the ATO concerning taxation matters.

Tax Invoice
An invoice issued in relation to a supply where the content of the invoice may be subject to GST credits. All tax invoices must have the firm's ABN clearly shown.

Term Loans
Loans made for a specified and fixed period of time.

Trade Credit
Short term credit, usually one month, given by a supplier to a buyer when goods or services are bought. The creditor (account payable) is often known as a 'trade-creditor'.

Trading Stock
Stocks of merchandise for sale or raw materials for production.

Transaction
A commercial activity involving the exchange of money and / or goods and services between two parties. Examples include sale, leasing property, hiring employees and paying the phone account.

Turnover
For a business, total sales for a specific trading period.

Under Capitalization
A condition in which a firm has a shortage of working capital. This is a condition faced by many new firms at and following start up. It can also occur when a business expands its operations too rapidly.

Variable Costs
Business costs which vary in direct proportion to changes in the level of business activity – that is, sales or production. Examples are factory wages, purchases of raw materials and merchandise, freight and sales commissions.

Variance
The difference between budgeted of forecast sales (or some other activity, such as cash flow) and actual results. If budgeted annual sales were $500,000 and actual sales were $450,000, there would be a 10% negative variance.

Withholding
Amounts deducted from payments to others (such as employees and sub-contractors) which are to be sent to the ATO.

Working Capital
The funds needed to run a business on a daily basis. Working capital is expressed as a ration of current assets to current liabilities.

Liability limited by a scheme approved under Professional Standards Legislation

736 Waverley Road, East Malvern Victoria 3145
PO Box 167, Chadstone Centres Vic 3148
T 03 9530 4722 F 03 9563 3018
E enquiries@profitfocus.com.au
W www.profitfocus.com.au
ABN 40 359 253 386

Profit Focus Partners Pty Ltd is a CPA Practice