Harlands Accountants

Accountants – Jargon Buster

Accountants love long words, words that make no sense to anyone else and most of all abbreviations.

We've created our A-Z of the most common accounting terms used to help you to understand what these type of people are saying.

Balance Sheet Terms

The Balance Sheet is one of the two most common financial statements produced by accountants. This section pertains to potentially confusing terms that relate to the balance sheet.

Income Statement Terms

The Income Statement AKA Profit and Loss Statement is the second of the two common financial statements. These are the terms that are most commonly used in reference with this reporting tool.

Accounts Payable (AP)

Accounts Payable include all of the expenses that a business has incurred but has not yet paid. This account is recorded as a liability on the Balance Sheet as it is a debt owed by the company.

Accounts Receivable (AR)

Accounts Receivable include all of the revenue (sales) that a company has provided but has not yet collected payment on. This account is on the Balance Sheet, recorded as an asset that will likely convert to cash in the short-term.

Accrued Expense

An expense that been incurred but hasn't been paid is described by the term Accrued Expense.

Asset (A)

Anything the company owns that has monetary value. These are listed in order of liquidity, from cash (the most liquid) to land (least liquid).

Balance Sheet (BS)

A financial statement that reports on all of a company's assets, liabilities, and equity. As suggested by its name, a balance sheet abides by the equation <Assets = Liabilities + Equity>.

Book Value (BV)

As an asset is depreciated, it loses value. The Book Value shows the original value of an Asset, less any accumulated Depreciation.

Equity (E)

Equity denotes the value left over after liabilities have been removed. Recall the equation Assets = Liabilities + Equity. If you take your Assets and subtract your Liabilities, you are left with Equity, which is the portion of the company that is owned by the investors and owners.

Inventory

Inventory is the term used to classify the assets that a company has purchased to sell to its customers that remain unsold. As these items are sold to customers, the inventory account will lower.

Liability (L)

All debts that a company has yet to pay are referred to as Liabilities. Common liabilities include Accounts Payable, Payroll, and Loans.

Cost of Goods Sold (COGS)

Cost of Goods Sold are the expenses that directly relate to the creation of a product or service. Not included in this category are those costs that are needed to run the business. An example of COGS would be the cost of Materials, or the Direct Labour to provide a service.

Depreciation (Dep)

Depreciation is the term that accounts for the loss of value in an asset over time. Generally, an asset has to have substantial value in order to warrant depreciating it. Common assets to be depreciated are automobiles and equipment. Depreciation appears on the Income Statement as an expense and is often categorized as a "Non-Cash Expense" since it doesn't have a direct impact on a company's cash position.

Expense (Cost)

An Expense is any cost incurred by the business.

Gross Margin (GM)

Gross Margin is a percentage calculated by taking Gross Profit and dividing by Revenue for the same period. It represents the profitability of a company after deducting the Cost of Goods Sold.

Gross Profit (GP)

Gross Profit indicates the profitability of a company in dollars, without taking overhead expenses into account. It is calculated by subtracting the Cost of Goods Sold from Revenue for the same period.

Income Statement (Profit and Loss)

The Income Statement (often referred to as a Profit and Loss, or P&L) is the financial statement that shows the revenues, expenses, and profits over a given time period. Revenue earned is shown at the top of the report and various costs (expenses) are subtracted from it until all costs are accounted for; the result being Net Income.

Net Income (NI)

Net Income is the amount that is earned in profits. It is calculated by taking Revenue and subtracting all of the Expenses in a given period, including COGS, Overhead, Depreciation, and Taxes.

Net Margin

Net Margin is the percent amount that illustrates the profit of a company in relation to its Revenue. It is calculated by taking Net Income and dividing it by Revenue for a given period.

Revenue (Sales)

Revenue is any money earned by the business.

Accounting Period

An Accounting Period is designated in all Financial Statements (Income Statement, Balance Sheet, and Statement of Cash Flows). The period communicates the span of time that is reported in the statements.

Allocation

The term Allocation describes the procedure of assigning funds to various accounts or periods. For example, a cost can be Allocated over multiple months (like in the case of insurance) or Allocated over multiple departments (as is often done with administrative costs for companies with multiple divisions).

Business (or Legal) Entity

This is the legal structure, or type, of a business. Common company formations include Limited Company, Sole Trader, Partnership, Limited Liability Partnership (LLP), S-Corp and CIC. Each entity has a unique set of requirements, laws, and tax implications.

Cash Flow

Cash Flow is the term that describes the inflow and outflow of cash in a business. The Net Cash Flow for a period of time is found by taking the Beginning Cash Balance and subtracting the Ending Cash Balance. A positive number indicates that more cash flowed into the business than out, where a negative number indicates the opposite.

Credit

A credit is an increase in a liability or equity account, or a decrease in an asset or expense account.

Debit

A debit is an increase in an asset or expense account, or a decrease in a liability or equity account.

Diversification

Diversification is a method of reducing risk. The goal is to allocate capital across a multitude of assets so that the performance of any one asset doesn't dictate the performance of the total.

Fixed Cost (FC)

A Fixed Cost is one that does not change with the volume of sales. For example, rent and salaries won't change if a company sells more. The opposite of a Fixed Cost is a Variable Cost.

General Ledger (GL)

A General Ledger is the complete record of a company's financial transactions. The GL is used in order to prepare all of the Financial Statements.

Generally Accepted Accounting Principles (GAAP)

These are the rules that all accountants abide by when performing the act of accounting. These general rules were established so that it is easier to compare 'apples to apples' when looking at a business's financial reports.

Interest

Interest is the amount paid on a loan or line of credit that exceeds the repayment of the principal balance.

Journal Entry (JE)

Journal Entries are how updates and changes are made to a company's books. Every Journal Entry must consist of a unique identifier (to record the entry), a date, a debit/credit, an amount, and an account code (that determines which account is altered).

Liquidity

A term referencing how quickly something can be converted into cash. For example, stocks are more liquid than a house since you can sell stocks (turning it into cash) more quickly than real estate.

Material

Material is the term that refers whether information influences decisions. For example, if a company has revenue in the millions of dollars, an amount of £0.50 is hardly material. GAAP requires that all Material considerations must be disclosed.

On Credit/On Account

A purchase that happens On Credit or On Account is a purchase that will be paid at a future time, but the buyer gets to enjoy the benefit of that purchase immediately. “Bartender, put it on my tab...”

Overhead

Overhead are those Expenses that relate to running the business. They do not include Expenses that make the product or deliver the service. For example, Overhead often includes Rent, and Executive Salaries.

Payroll

Payroll is the account that shows payments to employee salaries, wages, bonuses, and deductions. Often this will appear on the Balance Sheet as a Liability that the company owes if there is accrued vacation pay or any unpaid wages.

Present Value (PV)

Present Value is a term that refers to the value of an Asset today, as opposed to a different point in time. It is based on the theory that cash today is more valuable than cash tomorrow, due to the concept of inflation.

Receipts

A Receipt is a document that proves payment was made. A business produces receipts when it provides its product or service and it receives receipts when it pays for goods and services from other businesses. Received Receipts should be saved and catalogued so that a company can prove that its incurred expenses are accurate.

Return on Investment (ROI)

Originally, this term referred to the profit that a company was making (Return), divided by the Investment required. Today, the term is used more loosely to include returns on various projects and objectives. For example, if a company spent £1,000 on marketing, which produced £2,000 in profit, the company could state that it's ROI on marketing spend is 50%

Trial Balance (TB)

Trial Balance is a listing of all accounts in the General Ledger with their balance amount (either debit or credit). The total debits must equal the total credits, hence the balance.

Variable Cost (VC)

These are costs that change with the volume of sales and are the opposite of Fixed Costs. Variable costs increase with more sales because they are an expense that is incurred in order to deliver the sale. For example, if a company produces a product and sells more of that product, they will require more raw materials in order to meet the increase in demand.

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