Article

Accounting Terminology

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1. **Accounting Period**

Any period of time utilised to measure accounting performance e.g. 1 year, 1 month, 3 months.

2. **Accounts Payable (Sundry Creditors)**

Short term or current financial obligations that are created through the purchase of merchandise, or obtaining of service.

3. **Accounts Receivable (Sundry Debtors)**

Amounts owed to the firm by customers in the form of regular accounts for services rendered or goods supplied.

4. **Assets**

Those items acquired by the firm to aid it in accomplishing its business objectives.

5. **Benchmarks**

The comparison of operating figures from one business with another in that same industry, to assist in achieving Best Management Practice.

6. **B.O.S. (Before Owners' Salary)**

Before Owners' Salary - this is a term used to indicate what the financial result is prior to including Owners/Management Salaries.

7. **Break Even Sales**

The level of sales necessary to cover all variable and fixed expenses, i.e. the point of no profit or loss.

8. **Capitalisation Rate**

In valuing businesses the future maintainable profit is expressed at a Capitalisation Rate.

The Capitalisation Rate is the rate of return that a prudent 'arms-length' investor would require from an investment in this type of business after the allowance of reasonable management salaries.

The Capitalisation Rate normally reflects a mark up on prevailing interest rates to reflect the risk of the business, lack of negotiability of shares, economic conditions, restrictions on entry into the business, size of the share parcel (if a company) and general business risks.

9. **Cost Of Goods Sold**

The figure calculated in a Trading Account to represent the cost of goods sold in that accounting period.

The figure is the result of the calculation:-

Opening Stock	$
Plus Purchases	
Plus Freight Inwards	$____________
Less Closing Stock	
Equals Cost of Goods Sold	$____________

10. Current Assets

Those items owned by the firm which are usually turned into cash within the normal operating cycle of the business (usually twelve months). Examples of current assets are Cash, Sundry Debtors, Stock, Deposits, Cash Floats.

11. Current Liabilities

Those amounts owed by the business, which will normally be repaid within the operating cycle of the business. (Usually twelve months). Examples of Current Liabilities are Bank Overdraft, Sundry Creditors, Accruals, Provision for Employee Benefits now due or due within 12 months.

12. Current Ratio

The relationship between current assets and current liabilities. This ratio is an indication of the business's ability to meet ongoing liabilities. To calculate, Current Assets are divided by Current Liabilities.

13. Current Market Value

Is the business' valuation of assets, particularly fixed assets which would probably have been reflected in the Statement of Financial Position at their original cost? (historical cost).

14. Days Creditors Outstanding

This is a means of checking how a business is paying its creditors as compared to negotiated payment terms.

Calculated:

- Purchases from creditors on credit terms (not cash) divided by 365 equals average daily credit purchases
- Creditors balance divided by average daily credit purchases equals days creditors are outstanding

15. Days Debtors Outstanding

This is a means of checking customers' payments as against the business's credit terms.

Calculated:

- Credit sales divided by 365 equals average daily sale

- Debtors balance divided by average daily sales equals days debtors are outstanding

16. Debtors Ratio

Indicates the percentage of Debtors outstanding as compared to credit sales.

Calculated:

$$\frac{\text{Debtors}}{\text{Credit Sales}} \times \frac{100}{1}$$

17. Debtors

Amounts owed to the firm by customers in the form of regular accounts for services rendered or goods supplied.

18. Debt To Equity Percentage

This is a means of establishing the percentage of external debt to equity owned by the owners of a business.

Calculated:

$$\frac{\text{Total Debt}}{\text{Equity}} \times \frac{100}{1}$$

19. Expenses

These are the costs incurred in producing net profit.

20. Fixed Assets

Those items owned by the business which are not expected to be converted into cash but are used to generate business revenue.

21. Fixed Assets As A Percentage Of Total Assets

Calculated:

$$\frac{\text{Fixed Assets}}{\text{Total Assets}} \times \frac{100}{1}$$

22. Future Maintainable Profits

When a business is valued it is normal to calculate its Future Maintainable Profit.

The Future Maintainable Profit is the expected profitability of the business after having regard to previous years trading and after adjustment has been made for unusual or non-recurring items. Reasonable management salaries are also included in the calculations as is 'notional rent' if the business is operating from premises that are owned by the business.

23. Gross Profit

The difference between sales and cost of goods sold.

24. Gearing

Represents the level of borrowings expressed as a percentage on the value of assets.
eg:

Assets Worth	$100,000
Borrowings	$ 62,000
Gearing is	62%

25. Historical Cost

Is the original cost for which the assets are acquired?

In a Statement of Financial Position many assets are normally reflected at their cost price thus being expressed at historical cost.

26. **Inventory (Stock On Hand)**

Goods which the firm has purchased or manufactured and expects to sell to customers during the next year.

27. **Inter Business Comparisons**

Detailed reports on specific types of businesses prepared by the Waikato Management Research Centre to enable detailed review and comparison of a business against a 'pool of similar businesses'.

The data is made available on a confidential coded basis by Accountancy Practices throughout New Zealand so as to enable these very important financial reports to be prepared.

28. **Liabilities**

Amounts owing by the firm to external organisations.

29. **Liquidity**

Refers to the firm's short term cash position and its ability to pay financial obligations as they fall due.

30. **Long Term Liabilities**

Amounts owed by the business which in the normal course of events are not due for repayment within the next twelve months.

31. **Mark - Up**

The amount added to invoice cost to arrive at the selling price.

32. **Net Profit**

The amount remaining after cost of goods sold and operating expenses have been deducted from sales.

33. **Owners' Funds As A Percentage Of Total Assets**

Calculated:

$$\frac{\text{Total of Owners, Shareholders, Partnership or Beneficiaries' Funds}}{\text{Total Assets}} \quad \times \quad \frac{100}{1}$$

34. **Productivity**

A measure of the firm's output generated from resources (people, wages and premises).

35. **Quick Ratio**

The ratio between current assets minus stock, and current liabilities minus bank overdraft. This ratio is another measure of a firm's liquidity. Calculated Current Assets less Stock divided by Current Liabilities less Bank Overdraft.

36. **Stock On Hand**

Goods which the firm has purchased or manufactured and expects to sell to customers during the next year.

37. Stock Turnover.

The number of times on average during the year that the entire inventory of stock on hand is sold and replaced.

38. Reasonable Management Salaries

Are the salaries that management believes are reasonable to be paid if external persons were to be appointed to management positions in the organisation.

39. Return On Assets

The relationship between net profit and total assets. This ratio is used in evaluation of a firm's profitability and efficiency in its use of assets.

Calculated:

$$\frac{\text{Net Trading Profit}}{\text{Assets}} \quad x \quad \frac{100}{1}$$

40. Return On Equity (Investment)

The relationship between net profit (after owner's salary) and owner's equity. It is an indicator of efficiency in the use of owner's capital.

Calculated:

$$\frac{\text{Net Trading Profit}}{\text{Equity}} \quad x \quad \frac{100}{1}$$

41. Times Interest Covered By Profit

Is a test carried out by financiers to ascertain the ability of a borrower to service the interest cost of a Loan out of the business profits.

Calculated:

$$\frac{\text{Profit Before Tax and Interest}}{\text{Interest}} \quad x \quad \frac{100}{1}$$

42. Working Capital

The excess of current assets over current liabilities.

Calculated:

Current Assets less Current Liabilities.

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