Dictionary of Accounting Terms

Harold Averkamp
CPA, MBA

AccountingCoach®

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Accounting Terms (A)

a

A symbol that indicates the total amount of fixed costs during a specified period of time. In the equation of the straight line, $y = a + bx$, the total amount of fixed costs during the period is represented by "a".

ABC

See activity-based costing.

ABC inventory system

The ABC inventory system is different from activity-based costing. The ABC inventory system is used in order to focus on the most important items in inventory. Usually a relatively few items will account for a very significant value. These relatively few items with great importance are categorized as the "A" items. It is also common for many of the items in inventory to have a relatively small aggregate value. These items are categorized as "C" items. The remaining items are categorized as the "B" items. By closely monitoring the "A" items, a company is able to manage the most important items with a relatively small effort.

a/c

An abbreviation for the word *account*.

abnormal spoilage

Scrap or waste that should have been avoided. In other words, abnormal spoilage is the amount that is over and above the normal amount that is expected in a production process.

absorption costing

Costing system wherein fixed manufacturing overhead is allocated to (or absorbed by) products being manufactured. This system, which treats fixed manufacturing costs as a product cost, is required for external financial statements.

accelerated depreciation

The allocation of the cost of a plant asset to expense in an accelerated manner. This means that the amount of depreciation in the earlier years of an asset's life is greater than the straight-line amount, but will be less in the later years. In total the amount of depreciation over the life of the asset will be the same as straight-line depreciation. The difference between accelerated and straight-line is the timing of the depreciation. For profitable companies, the use of accelerated depreciation on the income tax return will mean smaller cash payments for income taxes in the earlier years and higher cash payments for income taxes in later years. To learn more, see Explanation of Depreciation.

account

A record in the general ledger that is used to collect and store similar information. For example, a company will have a Cash account in which every transaction involving cash is recorded. A company selling merchandise on credit will record these sales in a Sales account and in an Accounts Receivable account.

accounting cycle

A term that describes the steps when processing transactions (analyzing, journalizing, posting, preparing trial balances, adjusting, preparing financial statements) in a manual accounting system. Today many of the steps occur simultaneously when using accounting software.

accounting department

Part of a company's administration that is responsible for preparing the financial statements, maintaining the general ledger, paying bills, billing customers, payroll, cost accounting, financial analysis, and more. The head of the accounting department often has the title of controller.

accounting equation

Assets = Liabilities + Owner's Equity. For a corporation the equation is Assets = Liabilities + Stockholders' Equity. For a nonprofit organization the accounting equation is Assets = Liabilities + Net Assets. Because of double-entry accounting this equation should be in balance at all times. The accounting equation is expressed in the financial statement known as the balance sheet. To learn more, see Explanation of Accounting Equation.

accounting net income flows

The amounts reported on the income statement. Because of accrual accounting the net income flows will be different from the cash flow.

accounting principles

The standards, rules, guidelines, and industry-specific requirements for financial reporting. To learn more, see Explanation of Accounting Principles.

Accounting Principles Board (APB)

This group preceded the current Financial Accounting Standards Board (FASB). The APB members served in a part-time capacity to determine the accounting standards from 1962 to 1973. The accounting rules established by the APB were titled Opinions and remain as part of the generally accepted accounting principles (unless superseded by standards issued by the FASB).

accounting rate of return

An indicator of profitability that is measured by dividing the accounting net income by the amount invested.

Accounting Research Bulletin (ARB)

These pronouncements were issued by the Committee on Accounting Procedures of the American Institute of Certified Public Accountants during the years 1953 to 1959. They were and are part of the generally accepted accounting principles unless superseded by pronouncements of the APB or FASB.

accounts payable

This current liability account will show the amount a company owes for items or services purchased on credit and for which there was not a promissory note. This account is often referred to as trade payables (as opposed to notes payable, interest payable, etc.)

accounts receivable

A current asset resulting from selling goods or services on credit (on account). Invoice terms such as (a) *net 30 days* or (b) *2/10, n/30* signify that a sale was made on account and was not a cash sale.

accounts receivable - net

The combined amount of the debit balance in the current asset account Accounts Receivable and the credit balance in the contra asset account Allowance for Doubtful Accounts. The difference between the balances in these two accounts is an approximation of the amount of the accounts receivable that is likely to turn to cash (be collected).

accounts receivable turnover ratio

The financial ratio which indicates the speed at which a company collects its accounts receivable. If a company's turnover is 10, this means the company's accounts receivable are turning over 10 times per year. It indicates that the company, on average, is collecting its receivables in 36.5 days (365 days per year divided by 10). To learn more, see Explanation of Financial Ratios.

accounts written off

Usually refers to one of the accounts receivable that was deemed to be uncollectible or worthless and was removed from the general ledger account Accounts Receivable.

accrual basis of accounting

The accounting method under which revenues are recognized on the income statement when they are earned (rather than when the cash is received). The balance sheet is also affected at the time of the revenues by either an increase in Cash (if the service or sale was for cash), an increase in Accounts Receivable (if the service was performed on credit), or a decrease in Unearned Revenues (if the service was performed after the customer had paid in advance for the service).

Under the accrual basis of accounting, expenses are matched with revenues on the income statement when the expenses expire or title has transferred to the buyer, rather than at the time when expenses are paid. The balance sheet is also affected at the time of the expense by a decrease in Cash (if the expense was paid at the time the expense was incurred), an increase in Accounts Payable (if the expense will be paid in the future), or a decrease in Prepaid Expenses (if the expense was paid in advance).

accrual method of accounting
See accrual basis of accounting.

accrual-type adjusting entry
An adjusting entry made at the end of the accounting period in order to report (1) revenues that have been earned but have not yet been entered into the accounting records, (2) expenses that have been incurred but have not yet been entered into the accounting records, (3) revenues already recorded that involve more than the current accounting period, or (4) expenses already recorded that involve more than the current accounting period. To learn more, see Explanation of Adjusting Entries.

accruals
See accrual-type adjusting entry.

accrue
To report a revenue or expense that has occurred, but has not yet been entered in the accounting records as of the end of the accounting period. To learn more, see Explanation of Adjusting Entries.

accrued expense
An expense that has occurred but the transaction has not been entered in the accounting records. Accordingly an adjusting entry is made to debit the appropriate expense account and to credit a liability account such as Accrued Expenses Payable or Accounts Payable. To learn more, see Explanation of Adjusting Entries.

accrued expenses payable
A liability account that reflects the estimated amount a company owes for expenses that occurred, but have not yet been paid nor recorded through a routine transaction. To learn more, see Explanation of Adjusting Entries.

accrued liability
The amount a company owes for expenses or losses incurred that have not yet been paid nor recorded through a routine transaction. To learn more, see Explanation of Adjusting Entries.

accrued payroll
The amount of wages and related expenses that have been incurred by the employer (and earned by the employees) but have not yet been paid.

accrued rent
See accrued rent expense. Also see accrued rent income.

accrued rent expense
The amount of rent that has been incurred by a tenant during an accounting period shown in the heading of the income statement, but it has not been paid as of the last day of the accounting period.

accrued rent income
The amount of rent that has been earned by the landlord or owner during the accounting period shown in the heading of the income statement, but it has not been received as of the last day of the accounting period.

accrued rent liability
Usually a current liability that reports the amount of rent that the tenant has incurred but has not paid as of the date of the balance sheet.

accrued rent receivable
Usually a current asset that reports the amount of rent that the landlord/owner has earned, but has not been received as of the date of the balance sheet.

accrued revenue
Revenue that has been earned but not yet invoiced to the customer.

accrued vacation
The amount of vacation that an employee has earned but has not yet taken.

accrued vacation liability
See vacation pay payable.

accrued vacation pay
The amount owed to employees as of a specified date for the amount of vacation pay that has been earned but has not been taken. For example, the accrued vacation pay as of December 31, 2023 is the amount the employees have earned as of December 31, 2023 but have not taken as of that date. The employees might take the vacation time during 2024 or they might be paid the amount in 2024.

accumulated deficit
The term used in place of retained earnings when a corporation has a negative (debit) balance in its account Retained Earnings.

accumulated depletion
The cumulative amount of depletion expense pertaining to the natural resources shown on the balance sheet. The account has a credit balance and will be reported on the balance sheet as a contra asset.

accumulated depreciation
The amount of a long-term asset's cost that has been allocated to Depreciation Expense since the time that the asset was acquired. Accumulated Depreciation is a long-term contra asset account (an asset account with a credit balance) that is reported on the balance sheet under the heading Property, Plant, and Equipment.

accumulated depreciation - buildings

This is a contra long-term asset account which is credited for the depreciation associated with Buildings. Since it is a balance sheet account, the accumulated depreciation account balance does not close at the end of each year; therefore, its credit balance will increase each year. However, its balance cannot become greater than the cost of the buildings.

When the credit balance in Accumulated Depreciation - Buildings is netted with the cost in the Buildings account, the result is the book value or carrying value of the buildings.

Depreciation Expense - Buildings is the income statement account that is debited when Accumulated Depreciation - Buildings is credited.

accumulated depreciation - equipment

The contra asset account which accumulates the amount of Depreciation Expense taken on Equipment since the equipment was acquired. As a contra asset account it will have a credit balance.

accumulated depreciation - land improvements

This account is a contra long-term asset account which is credited for the depreciation associated with land improvements. As an asset account, the accumulated depreciation account balance does not close at the end of each year; therefore, its credit balance will increase each year. However, its balance cannot become greater than the cost shown in the Land Improvements account.

When the credit balance in Accumulated Depreciation - Land Improvements is netted with the cost of land improvements, the result is the book value or carrying value of the land improvements.

Depreciation Expense - Land Improvements is the income statement account that is debited when Accumulated Depreciation - Land Improvements is credited.

accumulated other comprehensive income

A separate line within stockholders' equity that reports the corporation's cumulative income that has not been reported as part of net income on the corporation's income statement. The items that would be included in this line involve the income or loss involving foreign currency transactions, hedges, pension liabilities, and the unrealized gains and losses on certain investments. To learn more about this go to www.FASB.org, select Accounting Pronouncements from the left panel, and then select Statement of Financial Accounting Standards No. 130, *Reporting Comprehensive Income*.

acid test ratio

See quick ratio.

activity-based costing (ABC)

A technique for allocating costs to a product, service, customer, etc. The premise is that activities cause an organization to incur costs. Once the costs of the activities have been identified and each activity's cost has been determined, the cost of the activities is then allocated to the product, service, customer, etc. that required the activity. This technique is more logical for allocating overhead than simply allocating costs based on machine hours or direct labor hours. To learn more, see Explanation of Activity Based Costing.

activity-based management

Using the information generated in activity-based costing to plan and control activities and processes.

actual costing

A method of costing manufactured items that differs from normal costing and standard costing. Under actual costing each accounting period's actual manufacturing overhead costs and each accounting period's production volume are used to assign manufacturing overhead to the output.

actual overhead

The indirect manufacturing costs actually incurred during an accounting period.

adjunct account

An adjunct account is a valuation account that increases the book value or carrying value of a liability account. For example, the account Unamortized Premium on Bonds Payable (or simply Bond Premium) is an adjunct account since its credit balance is *added* to the amount in Bonds Payable in determining the book value of the bonds.

adjusted trial balance

A listing of the general ledger accounts and their account balances at a point in time after the adjusting entries have been posted. The grand total of the accounts with debit balances should equal the grand total of the accounts with credit balances.

adjusting entries

Journal entries usually dated the last day of the accounting period to bring the balance sheet and income statement up to date on the accrual basis of accounting.

Adjusting entries are made to report (1) revenues that have been earned but not yet entered into the accounting records, (2) expenses that have been incurred but have not yet been entered into the accounting records, (3) revenues already recorded that pertain to a future accounting period, or (4) expenses already recorded that pertain to a future accounting period. To learn more, see Explanation of Adjusting Entries.

administrative expenses

Administrative expenses are part of the operating expenses (along with selling expenses). Administrative expenses include expenses associated with the general administration of the business. Examples include the salaries and fringe benefits of the company president, human resource personnel, accounting, information technology, the depreciation expense for equipment and space used in administration, as well as supplies, utilities, etc.

Under the accrual basis of accounting, administrative expenses appear on the income statement for the period in which they occurred (not the period in which they were paid).

advance from customer

A liability account used to record an amount received from a customer before a service has been provided or before goods have been shipped. This account is referred to as a deferred revenue account and could be entitled Customer Deposits or Unearned Revenues.

advance to employee

An asset account used to record amounts given to an employee with the expectation of repayment. For example, if an employee is given money by a company and the money is expected to be repaid or spent for company purposes, the amount will be recorded in this current asset account until it is repaid or until the expense documentation is provided.

advertising expense

Advertising Expense is the income statement account which reports the dollar amount of ads run during the period shown in the income statement. Advertising Expense will be reported under selling expenses on the income statement.

after-tax

The result after subtracting the income tax associated with a given amount. For example, if a corporation has a gain of $100,000 before tax, and its income tax rate is 30%, its after-tax gain is $70,000. If a corporation has a loss of $30,000 before tax, and its income tax rate is 30%, its after-tax loss is $21,000.

after-tax cost of debt

The interest rate of debt (bonds, loans) after deducting the income tax savings. For example, if a corporation has issued bonds with an interest rate of 8% and the corporation's income tax rate is 25%, the after-tax cost of the bonds' interest is 6% (8% minus the tax savings equal to 25% of 8%).

aging of accounts payable

A sorting of a company's accounts payable by due date.

aging of accounts receivable

A sorting of a company's accounts receivables by the age of the receivables.

AICPA

See American Institute of Certified Public Accountants.

allocate

To assign costs to a product, department, customer, etc. on an arbitrary basis. For example, the heating cost might be allocated to the five departments located in the area that is heated. The allocation is often based on each department's square footage.

allocated

Costs that have been divided up and assigned to periods, departments, products, etc. In depreciation it is the asset's cost that is assigned to each of the years that the asset is in use. In cost accounting it is the assigning of common production costs to various production departments, product lines, individual products, activities.

allocation

The assigning or dividing up of amounts. For example, depreciation is an allocation process because it assigns an asset's cost to expense in each of the years the asset is expected to be used. There is also an allocation process when the cost of goods available for sale is divided up between ending inventory and cost of goods sold. Manufacturers allocate (or assign) fixed overhead such as factory rent to the units of products produced in the factory.

allowance for doubtful accounts

Allowance for Doubtful Accounts is a contra current asset account associated with Accounts Receivable. When the credit balance of the Allowance for Doubtful Accounts is subtracted from the debit balance in Accounts Receivable the result is known as the net realizable value of the Accounts Receivable.

The credit balance in this account comes from the entry wherein Bad Debts Expense is debited. The amount in this entry may be a percentage of sales or it might be based on an aging analysis of the accounts receivables (also referred to as a percentage of receivables).

When the allowance account is used, the company is anticipating that some accounts will be uncollectible in advance of knowing the specific account. As a result the bad debts expense is more closely matched to the sale. When a specific account is identified as uncollectible, the Allowance for Doubtful Accounts should be debited and Accounts Receivable should be credited.

allowance for uncollectible accounts

See Allowance for Doubtful Accounts.

allowance method for bad debts expense

Under this method of recognizing losses on credit sales, a contra asset account Allowance for Doubtful Accounts is reported on the balance sheet. Prior to specifically identifying an account receivable as uncollectible, a company debits Bad Debts Expense and credits Allowance for Doubtful Accounts for an estimated amount. The estimate could be based on a percentage of sales or it could be based on the age of its accounts receivables.

allowance to reduce inventory to net realizable value (NRV)

This is a valuation account for the asset Inventory. A credit balance should be reported in this account for the amount that the net realizable value of inventory is less than the cost reported in the Inventory account. The credit entered into the Allowance for Reduction of Cost to Net Realizable Value will mean a debit is entered into the income statement account Loss From Reducing Inventory to Net Realizable Value.

American Institute of Certified Public Accountants (AICPA)

This is a national organization of certified public accountants. For more information go to www.aicpa.org.

amortization

The systematic allocation of the discount, premium, or issue costs of a bond to expense over the life of the bond.

The systematic allocation of an intangible asset to expense over a certain period of time.

The systematic reduction of a loan's principal balance through equal payment amounts which cover interest and principal repayment.

amortization expense

The allocation to expense of the cost of an intangible asset such as a patent or goodwill.

amortization of bond discount

The systematic allocation of the discount on bonds payable (reported as a debit in a contra-liability account) to Bond Interest Expense over the life of the bonds. The journal entry to amortize contains a debit to the income statement account Bond Interest Expense and a credit to the balance sheet account Discount on Bonds Payable. To learn more see Explanation of Bonds Payable.

amortization of bond issue costs

The systematic allocation of the costs incurred to issue bonds (reported in a contra liability account) to Interest Expense over the life of the bonds.

amortization of bond premium

The systematic allocation of the premium on bonds payable (reported as a credit in a liability account) to Bond Interest Expense over the life of the bonds. The journal entry to amortize the premium contains a debit to the balance sheet account Premium on Bonds Payable and a credit to the income statement account Bond Interest Expense. To learn more see Explanation of Bonds Payable.

amortization of intangible assets

The expensing of an intangible asset from the balance sheet to the income statement.

amortization schedule

A multi-column listing of the amounts needed to eliminate a balance in a systematic manner over the life of the item. For example, an amortization schedule for a 15-year mortgage loan would show the 180 payments. The first column might be the payment number. The second column would show the amount of the payment. Column 3 would show the amount of interest being paid. Column 4 would show the principal amount being paid (total payment minus the interest payment). Column 5 would show the principal balance remaining after the payment (previous principal balance minus the current principal payment).

An amortization schedule for bond discount would show the amounts needed to be journalized over the life of the bonds in order to systematically move the amount from the balance sheet to interest expense on the income statement.

annuity

A series of equal amounts at equal time intervals. Also see annuity due, annuity in advance, annuity in arrears, and ordinary annuity.

annuity due

A series of equal amounts occurring at the beginning of each equal time interval. Also known as an annuity in advance. An example would be the monthly rent on an apartment.

annuity in advance

A series of equal amounts occurring at the beginning of each equal time interval. Also known as an annuity due. An example would be the monthly rent on an apartment.

annuity in arrears

A series of equal amounts occurring at the end of each equal time interval. Also known as an ordinary annuity. An example would be the monthly payments on a loan. Another example is the semiannual interest on a bond.

APB

See Accounting Principles Board.

applied overhead

Manufacturing overhead assigned to units of output. Often this is applied via a standard overhead rate. To learn more, see Explanation of Standard Costing.

apportionment

An allocation based on some proportions. For example, a corporation's taxable income that was earned in many of the U.S. states might be allocated or apportioned to the states in which the corporation has conducted business.

appraisal

An estimate of an asset's market value.

appraisal report

A report prepared by a professional appraiser with detailed information on the calculation of an asset's current market value.

appropriated retained earnings

A second retained earnings account that reports the amount that a company has transferred from the unappropriated or regular retained earnings account.

ARB

See Accounting Research Bulletin.

arm's length transaction

A phrase that indicates a transaction was between two independent parties and that the resulting amount is a fair representation of the value.

arrears

A term meaning behind, such as dividends in arrears, or something occurring at the end of a period, such as the recurring payment in an annuity in arrears.

articles of incorporation

A document filed when a corporation is formed. Among other things, it lists the number of shares of stock that the corporation is authorized to issue.

asset turnover ratio

The mathematical result of sales revenues divided by average total assets during the period of the sales.

assets

Things that are resources owned by a company and which have future economic value that can be measured and can be expressed in dollars. Examples include cash, investments, accounts receivable, inventory, supplies, land, buildings, equipment, and vehicles.

Assets are reported on the balance sheet usually at cost or lower. Assets are also part of the accounting equation: Assets = Liabilities + Owner's (Stockholders') Equity.

Some valuable items that cannot be measured and expressed in dollars include the company's outstanding reputation, its customer base, the value of successful consumer brands, and its management team. As a result these items are not reported among the assets appearing on the balance sheet.

assign

In cost accounting this term means to allocate, apply, apportion, or spread manufacturing overhead costs to the production output.

In terms of accounts receivable, assign means to pledge accounts receivable to a lender as collateral for a loan.

assigned accounts receivable

Accounts receivable that serve as the collateral for a loan.

assignee

The lender (bank) that receives an asset as collateral for a loan.

assignor

The borrower who provides to a lender an asset as collateral for a loan.

audited financial statements

Financial statements that bear the report of independent auditors attesting to the financial statements' fairness and compliance with generally accepted accounting principles.

auditor's report

A written opinion of an independent certified public accountant that a company's financial statements are a fair representation of the company's financial performance and financial position. The auditor's report is required for each corporation whose stock is publicly-traded.

authorized number of shares of stock

The number of shares of stock that a corporation may issue. The amount is specified in the corporation's articles of incorporation.

average accounts receivable

The average balance in the account Accounts Receivable during a period of time. Since the amount reported in the Accounts Receivable account is the ending balance on one specific day, it is necessary to compute an average balance when relating this account to Sales (the balance of which reports the sales for a period of time).

average collection period

Same as the Days Sales in Accounts Receivable

average cost of inventory

See weighted-average cost flow assumption and moving-average cost of inventory.

average inventory

The average amount of inventory during a period of time. Since the amount reported in the Inventory account is the ending balance on one specific day, it is necessary to compute an average balance when relating this account to the cost of goods sold (which covers a period of time).

Accounting Terms (B)

b

A symbol that indicates the variable cost rate and also the slope of a straight line. For example, in the equation of the straight line, y = a + bx, "b" represents the variable cost rate per unit of "x".

bad debts expense

This is an operating expense resulting from making sales on credit and not collecting the customers' entire accounts receivable and bad debts expense balances.

balance per bank

A phrase used in reconciling the bank statement. It refers to the ending balance shown on the bank statement.

balance per books

The amount appearing in the general ledger. When reconciling the bank statement, the balance per books is the balance of the Cash account in the general ledger that pertains to the bank account.

balance sheet

One of the main financial statements. The balance sheet reports the assets, liabilities, and owner's (stockholders') equity at a specific point in time, such as December 31. The balance sheet is also referred to as the Statement of Financial Position. To learn more, see Explanation of Balance Sheet.

balance sheet account
Asset, liability, and owner's equity accounts. Also referred to as permanent or real accounts.

bank balance
The amount in a bank account according to the bank's records.

bank errors
Errors made by the bank on a company's bank account. These are usually infrequent but could include an incorrect amount of a check or deposit or a check or deposit recorded in the wrong account.

bank overdraft
A negative balance in the bank's records for the company's checking account.

bank rec
A shortened version of the term *bank reconciliation* or *bank statement reconciliation.*

bank reconciliation
The process of comparing the amounts in the Cash account in the general ledger to the amounts appearing on the bank statement. The objective is to be certain that there is consistency between the amounts and that the company's amounts are accurate and complete.

bank service charge expense
This is an administrative expense which reports the fees incurred by a company for the expenses associated with its checking account transactions.

bank statement
Usually refers to a statement from the bank showing the activity in a company's checking account. The statement includes the deposits received by the bank, checks paid by the bank, bank service charge, and other amounts transferred into and out of the checking account.

bank statement reconciliation
See bank reconciliation.

basic accounting equation
See accounting equation.

basis point
One hundredth (1/100) of a percentage point. In other words, one percentage point is equal to 100 basis points. The difference between an interest rate of 6.5% and 6.75% is 25 basis points.

batch-level activities
Activities involving a batch of products—as opposed to individual items. An example of a batch activity is the setting up of a machine to produce a batch of 1,000 identical items.

batch-level cost

A cost associated with a batch of items, but not directly traceable to an individual item within the batch. For example, the cost to set up a machine to run a batch of 5,000 items is a batch-level cost. This cost must then be allocated to the 5,000 items included in the batch.

batch size

In activity-based costing, this refers to the number of items that will be produced after a machine has been setup.

bearer bond

A bearer bond is a bond that is not registered in its owner's name. The person holding the bond is presumed to be the owner of the bond. The interest on a bearer bond is received by clipping one of the dated interest coupons which are attached to the bond and presenting it to a bank for collection. This is the reason a bearer bond is also referred to as a coupon bond. Today, bearer bonds are almost nonexistent.

Big Four

The four largest public accounting firms in the U.S.: Deloitte, Ernst & Young, KPMG, PricewaterhouseCoopers. Typically, these four firms perform the audits of the largest publicly-traded corporations.

bill

An invoice or other document received from a vendor, supplier, etc. usually for goods or services received. Also a verb to indicate that a customer's sales invoice should be prepared for goods or services.

bill of materials

A listing of the materials included in a product. A bill of material could be thought of as a bakery's recipe for producing one of its products.

bill payable

An amount owed on bill or invoice from a vendor or supplier of goods or services.

biweekly

Usually means every two weeks. For example, if an employee is paid every other Thursday, the employee is paid biweekly. The person paid biweekly will receive 26 paychecks per year. (People paid two times per month – on the 15th and on the last day of the month – are said to be paid semimonthly and will receive 24 paychecks per year.)

blue-collar worker

A term often used when referring to production workers and other workers who are paid with an hourly pay rate. These workers' compensation is referred to as "wages" (as opposed to salaries).

board-designated restriction

An action by a nonprofit organization's board of directors to earmark an asset for a specified purpose. Since this is not a donor-imposed restriction, the designated asset is classified and reported as part of *unrestricted net assets.*

board of directors

Individuals elected by the common stockholders of a corporation to represent the stockholders and to establish the policies of the corporation. The board of directors appoints the **officers** of the corporation and declares dividends for the common and preferred stock.

boards of accountancy

These agencies establish the educational requirements and the eligibility of candidates desiring to sit for the Uniform CPA Exam. There is a board of accountancy in each of the 50 U.S. states plus five other jurisdictions. Each board of accountancy also controls the licensing of certified public accountants (CPAs) within its jurisdiction. For more information, see the CPA Requirements section of our Explanation of Accounting Careers.

BOM

See bill of materials.

bond

A formal written promise to pay interest every six months and the principal amount at maturity.

bond call price

The price at which the holder of a bond must sell the bond to the issuer. For example, a corporation may have the right to redeem/buy back its bonds by paying the bondholder 110% of the bond's face amount.

bond coupon rate

The stated interest rate appearing on the face of the bond. Also referred to as the nominal rate or the stated interest rate.

bond discount

See discount on bonds payable.

bond indenture

A document that discloses various conditions and terms of the company's bonds. It would include the call price, collateral, ramifications if interest is not paid, etc.

bond interest expense

The amount of interest expense incurred during the time interval shown in the heading of the income statement that pertains to a company's bonds payable. Bond interest expense also includes the amortization of the premium or discount on bonds payable and the amortization of the bond issue costs for the same period of time.

bond interest rate

The interest rate stated on a bond. This is also referred to as the face interest rate, nominal interest rate, and coupon rate.

bond issue costs

Bond Issue Costs is a contra liability account reported along with Bonds Payable. Bond Issue Costs include the professional fees and registration fees associated with the issuance of bonds. The amount in the account Bond Issue Costs will be amortized (systematically written off) to interest expense over the life of the bonds.

bond premium

See premium on bonds payable.

bond sinking fund

A restricted asset for the purpose of retiring a bond.

bonds payable

Generally a long term liability account containing the face amount, par amount, or maturity amount of the bonds issued by a company that are outstanding as of the balance sheet date.

book balance

The balance in a business record such as a general ledger account.

book depreciation

The depreciation computed for financial reporting purposes—as opposed to income tax depreciation. To learn more, see Explanation of Depreciation.

book of original entry

Also known as a journal.

book value

The book value of an *asset* is the amount of cost in its asset account less the accumulated depreciation applicable to the asset. The book value of a *company* is the amount of owner's or stockholders' equity. The book value of bonds payable is the combination of the accounts Bonds Payable and Discount on Bonds Payable or the combination of Bonds Payable and Premium on Bonds Payable.

book value of a company

The amount of owner's equity or stockholders' equity reported on a company's balance sheet. This is *not* an indication of the company's fair market value.

book value of an asset

The book value of an asset is the asset's cost minus the accumulated depreciation since the asset was acquired. This net amount is *not* an indication of the asset's fair market value. The book value of an asset is also referred to as the asset's carrying value.

book value per share of stock

A corporation’s total stockholders’ equity (excluding preferred stock) divided by the number of shares of common stock outstanding.

bookkeeper

Usually a person without a four-year or five-year accounting degree employed to record routine financial transactions for smaller companies.

bookkeeping

The recording of a company’s transactions into the accounts contained in the general ledger. It is usually associated with the accounting tasks prior to the preparation of the trial balance. To learn more, see Explanation of Bookkeeping.

books

A term to mean the company’s general ledger or accounting records.

borrow

To receive money in exchange for a promise to repay the amount to the lender.

borrower

The person or business that receives a loan from a bank or other lender.

bottom line

In accounting this term means a company’s net income, which is the bottom line of the income statement.

bounced check

See not sufficient funds (NSF) check.

break-even analysis

To learn more, see Explanation of Break-even Point.

break-even point

To learn more, see Explanation of Break-even Point.

budget

A detailed plan with dollar amounts. Examples of budgets used in business include the cash budget, sales budget, production budget, department budgets, the master budget, and the capital expenditures budget. Some budgets are designed to be flexible budgets, while others are static budgets.

budget variance

The difference between the actual amount and the budgeted amount.

budgetary slack

Budgetary slack means providing a cushion in a budget in order to avoid an unfavorable variance at the end of the budget year. The budgetary slack might be achieved by entering budget expense amounts that are larger than expected and/or entering budget revenue amounts that are smaller than expected.

Budgetary slack is also known as budget slack, a controller's reserve, or a controller's cushion.

budgeted balance sheet

A balance sheet which is a projection of the amounts at a future date. It should be based on the projected, budgeted transactions.

budgeted capacity

The estimated volume in a future period that will be used for allocating indirect manufacturing costs.

budgeted income statement

An estimated income statement for a future period of time that is based on projected or budgeted transactions.

buildings

Buildings is a noncurrent or long-term asset account which shows the cost of a building (excluding the cost of the land). Buildings will be depreciated over their useful lives by debiting the income statement account Depreciation Expense and crediting the balance sheet account Accumulated Depreciation.

burden rate

A factory or manufacturing overhead rate used to allocate, apply, assign, or spread indirect product costs to items manufactured. Under traditional cost accounting, the burden rate might be a percentage of direct labor cost, or an hourly dollar amount for each direct labor hour or machine hour.

bx

In the equation of a straight line, y = a + bx, "bx" is the total variable cost resulting from the variable cost rate "b" multiplied times the quantity "x".

byproduct

A product that emerges with other products in a common process; however, this product does not have a significant value. (If it had significant value, it would be a joint product.)

Accounting Terms (C)

call premium

The difference between the call price of a bond or preferred stock and its stated or par value.

call price

The amount at which the holder of preferred stock or bonds must sell the stock or bonds back to the issuing corporation. The call price is disclosed in the indenture. The call price might be the face or par amount plus one year's interest or dividend.

callable bond

A bond that is callable by the issuer at a certain price. The price and other conditions are disclosed in the bond's indenture.

callable preferred stock

Preferred stock that is callable by the issuer at a certain price. The price and other conditions are disclosed in the preferred stock's indenture.

capital

A reference to stockholders' equity. See paid-in capital. Also an adjective that references property, plant and equipment used in a business; for example, capital expenditures and capital budgeting.

capital budgeting

The formal planning for significant expenditures, such as property, plant and equipment.

capital expenditures

Amounts spent for property, plant and equipment.

capital lease

A lease that "in substance" is a purchase and financing arrangement. When a lease meets certain criteria, the asset being "rented" is recorded as an asset and a liability is also recorded. A lease that is truly a rental arrangement is known as an operating lease.

capital maintenance approach in determining net income

Under this method, net income is determined by analyzing the change in owner's equity. The alternative is the *transaction approach* in which each transaction is recorded, sorted and stored.

capital maintenance approach to net income

A measurement of net income arrived at by comparing the amount of total equity at the end of a period to the amount of total equity at the beginning of the period. For example, if Al Capone had $5 million of equity at the end of the year, but had only $1 million at the beginning of the year, the government could conclude that he earned $4 million during the year. This method is in contrast to the transaction approach which computes net income by subtracting the expense transactions from the revenue transactions.

capital market

A structured market for trading stocks and bonds such as the New York Stock Exchange or NASDAQ.

Capital market can also include less structured markets such as private placements.

capital stock

A heading that includes common stock and preferred stock.

capitalize

To include in the cost of an asset. For example, the interest incurred by a company when it constructs its own building is added to the cost of the building's components. This is referred to as capitalizing the interest, or capitalization of interest.

carrying amount

Also referred to as book value or carrying value; the cost of a plant asset minus the accumulated depreciation since the asset was acquired. This net amount is not an indication of the asset's fair market value. Also used in reference to bonds payable: the face amount in Bonds Payable plus Premium on Bonds Payable or minus Discount on Bonds Payable and minus the unamortized issue costs.

carrying cost of inventory

This phrase has two connotations. One is the cost of holding inventory. In this case the carrying cost is the cost of capital tied up in inventory, the cost of storage, insurance, and obsolescence. Often this is expressed as an annual percentage rate, such as 20% of the cost of the inventory. This is used in the formula for determining the optimum ordering (or manufacturing) quantity of an item. See economic order quantity (EOQ) model.

Another connotation of this term is the cost at which the inventory is reported in the company's general ledger accounts and on its balance sheet. To learn more, see Explanation of Inventory and Cost of Goods Sold for a discussion of the factors that determine the amounts at which inventory is reported.

carrying value

See carrying amount.

cash

A current asset account which includes currency, coins, checking accounts, and undeposited checks received from customers. The amounts must be unrestricted. (Restricted cash should be recorded in a different account.)

cash account

The general ledger account Cash that reports currency, coins, undeposited checks, and the checking accounts of a company. (Could also be a reference to a customer required to pay cash for purchases.)

cash and cash equivalents

A balance sheet heading or grouping that includes both cash and those marketable assets that are very close to their maturity dates.

cash basis of accounting

An accounting method wherein revenues are recognized when cash is received and expenses are recognized when paid. This method is inferior to the accrual basis of accounting where revenues are recognized when they are earned and expenses are matched to revenues or the accounting period when they are incurred (rather than paid). The cash basis of accounting is usually followed by individuals and small companies, but is not in compliance with accounting's matching principle.

cash discount

See sales discount.

cash flow

Actual changes in cash as opposed to accounting revenues and expenses.

cash flow net of tax

The cash amounts received after deducting the related income taxes and also the cash amounts paid after deducting the cash saved when the amounts are income tax deductible.

cash flow statement

One of the main financial statements (along with the income statement and balance sheet). The cash flow statement reports the sources and uses of cash by operating activities, investing activities, financing activities, and certain supplemental information for the period specified in the heading of the statement. The cash flow statement is also known as the statement of cash flows.

cash from financing activities

The second section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

cash from operating activities

The first section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

cash method of accounting

See cash basis of accounting.

cash realizable value

See net realizable value.

cash receipt

The collection of money (currency, coins, checks). Not to be confused with revenues.

cash receipts journal

A special journal (or specialized journal) used to record money received. In a manual system this will allow one entry to the Cash account for the month (or shorter periods) instead of debiting the Cash account for every receipt.

cash short and over

A miscellaneous expense account used to record the difference between the amount of cash needed to replenish a petty cash fund and the amount of petty cash receipts at the time the petty cash fund is replenished.

cash surrender value (CSV)

The amount of cash that could be received if a whole life insurance policy were canceled.

cashier's check

A check drawn on a bank. A cashier's check leaves no doubt that the funds represented by the check are real. A bank money order or a certified check would also assure the payee that the funds are in the bank.

CD

See certificate of deposit.

CEO

See chief executive officer.

certificate of deposit

Also known as a CD. A bank time deposit (savings deposit) that cannot be withdrawn until a specified date. For example, a CD might mature in 6, 9, 12, or 18 months. If the amount deposited in a CD needs to be withdrawn prior to its maturity date, a penalty is assessed by the bank.

certified management accountant

A professional certification awarded to an accountant who has successfully completed the CMA Exam and has achieved the required work experience. The certified management accountant is recognized as a person with a strong proficiency in both management and financial accounting.

certified public accountant

A designation awarded by one of 50 U.S. states or five jurisdictions to a college graduate who has passed the rigorous Uniform CPA Exam and has met the required work experience. See the Explanation of Accounting Careers.

CFO

See chief financial officer.

change in accounting estimate

Accounting estimates include the estimated salvage value and the estimated useful life of depreciable assets, estimated percentage of bad debts expense, estimated percentage of units to be repaired or replaced during a warranty period, and routine estimates of monthly expenses for utilities and other expenses. When a change is needed to one of these estimates, the change can affect the current and future periods only. Previous periods are not restated for changes in estimates. (Corrections of errors require a restatement of a prior period amount.)

change in net assets

The “bottom line” on the statement of activities. The change in net assets results from revenues, expenses, and the release of assets from restrictions. It is computed for an organization’s three classes of net assets as well as for total net assets during the period appearing in the heading of the statement of activities.

chart of accounts

A listing of the accounts available in the accounting system in which to record entries. The chart of accounts consists of balance sheet accounts (assets, liabilities, stockholders’ equity) and income statement accounts (revenues, expenses, gains, losses). The chart of accounts can be expanded and tailored to reflect the operations of the company. To learn more, see Explanation of Chart of Accounts.

checkbook

The record of checks issued or written, deposits, bank charges, bank credits and the resulting balance. Also referred to as the check register.

checking account

The bank account on which checks are written or drawn. A bank refers to checking accounts as demand deposits.

check printing charges

A fee for the printing of checks ordered by a company. Often the amount is deducted automatically from a company’s checking account by the company that printed the checks.

cheque

Another name for check.

chief executive officer (CEO)

Usually the top ranking officer of the corporation who is charged with executing the policies set by the board of directors.

chief financial officer (CFO)

The top ranking financial person in the corporation.

chief operating officer (COO)

A top ranking corporation official usually reporting to the chief executive officer and responsible for the operations of the corporation.

Circular E

A publication by the U.S. Internal Revenue Service (IRS) to assist employers with federal payroll taxes. The complete title of the publication is Publication 15 (Circular E), Employer's Tax Guide. It is available at www.irs.gov.

classified balance sheet

A balance sheet with classifications (groupings or categories) such as current assets, property plant and equipment, current liabilities, long term liabilities, etc. To learn more, see Explanation of Balance Sheet.

clear

See cleared.

cleared

A term used to describe checks written by a company that have been received and paid by the bank on which they were drawn or written. The check number and amount will appear on the company's checking account statement.

clearing account

A general ledger account which serves to summarize similar transactions. For example, all of the closing entries involving operating expenses might be posted to an operating expense clearing (or summary) account.

closely-held corporation

A corporation with a limited number of stockholders and whose stock is usually not publicly traded.

closing entries

These journal entries are made after the financial statements have been prepared at the end of the accounting year. Most of the closing entries involve the income statement accounts (revenues, expenses, gains, losses, and summary/clearing accounts) whose balances will be transferred to the owner's capital account or the corporation's retained earnings account. A closing entry also transfers the owner's drawing account (a temporary balance sheet account) balance to the owner's capital account. The closing entries will mean that the temporary accounts (income statement accounts and drawing account) will start the new accounting year with zero balances.

CMA Exam

The Certified Management Accountant (CMA) Exam is a 13-hour, four-part exam on business analysis, management accounting and reporting, strategic management, and business application. The exam is administered through IMA, the acronym for the Institute of Management Accountants. Learn more about the CMA Exam in the Explanation of Accounting Careers.

coefficient of correlation

In regression analysis this is a statistic designated as r and ranging from -1 to +1. It indicates the percentage of correlation between the dependent variable and the independent variable(s). When this statistic is squared it produces the coefficient of determination, which indicates the percentage change in the dependent variable that is explained by the change in the independent variable(s). Correlation does not necessarily mean there is a cause-and-effect relationship.

coefficient of determination

In regression analysis this is a statistic (designated as r-squared) indicating the percentage of the change occurring in the dependent variable that is explained by the change in the independent variable(s). The percent change does not necessarily mean there is a cause-and-effect relationship.

COGS

The acronym for cost of goods sold.

collection period

The average time for a company's accounts receivable to be collected. See days sales in accounts receivable.

commissions expense

Under the accrual basis of accounting this income statement account reports the amount of commissions expense that pertains to the revenues earned by the company during the accounting period shown in the heading of the income statement.

commitments

Commitments are items that are not reported as liabilities as of the balance sheet date. Some of these items are reported in the notes to the financial statements. Examples include noncancelable contracts to rent space in the future or to purchase items at specified prices.

common costs

Costs that are common to several products, processes, activities, departments, territories, etc. Often common costs are subsequently allocated to each of the joint products, joint processes, etc. in order to determine the cost of each.

common-size balance sheet

A company's balance sheet that shows each item's amount after it has been divided by the amount of total assets. In other words, current assets will be shown as a percentage of total assets. This will allow comparisons between companies of different size.

common-size financial statement

See common-size balance sheet and common-size income statement.

common-size income statement

A company's income statement which reports each item as a percentage of net sales.

common stock

The type of stock that is present at every corporation. (Some corporations have preferred stock in addition to their common stock.) Shares of common stock provide evidence of ownership in a corporation. Holders of common stock elect the corporation's directors and share in the distribution of profits of the company via dividends. If the corporation were to liquidate, the secured lenders would be paid first, followed by unsecured lenders, preferred stockholders (if any), and lastly the common stockholders.

common stock account

The stockholders' equity account that reports the par or stated value of the issued shares of common stock. If the common stock does not have a par or stated value, this account will report the amount received when the shares of common stock were issued.

common stock dividend distributable

A cash dividend that has been declared by the board of directors, but not yet paid.

comparability

A quality of accounting information that facilitates the comparison of financial reporting of one company to the financial reporting of another company.

comparative balance sheet

A balance sheet with at least two columns of amounts. The column of amounts that is closest to the words will be the most recent amounts. The column furthest from the words will contain the oldest amounts. The older amounts provide a reference point from which to make comparisons.

comparative financial statements

Financial statements that show more than the current year's amounts. For example, it is generally accepted that a corporation's income statement will show the most recent three years of results. This provides the reader with two years of past amounts as a frame of reference for the most recent year. Comparative balance sheets typically show the most recent two years.

comparative income statement

An income statement with at least two columns of amounts. The column of amounts that is closest to the words will contain the amounts for the most recent period of time. The columns furthest from the words will be the amounts from older periods of time. The older amounts provide a frame of reference for understanding the recent amounts.

compensated absences

A term used in accounting that refers to employees' time off with pay for vacations, holidays, and sick days. Companies that are obligated to pay for these days off are required by the matching principle to record the expense for these fringe benefits when the employees are working, since the benefits are a part of the employees' compensation.

The expense is recorded each accounting period that an employee works by debiting expense (fringe benefit expense, compensated absences expense, etc.) and crediting a liability account (fringe benefits payable, compensated absences payable, etc.) When the employees actually take time off, the liability account is debited instead of an expense account.

To learn about the details in accounting for compensated absences you should read FASB Standard No. 43, ***Accounting for Compensated Absences***. The standard is available at www.fasb.org by selecting FASB Pronouncements in the left panel of the home page.

compensating balances

A bank account balance that a corporation agrees to maintain with a current or potential lender. For example, a corporation may agree to keep $1 million in its checking account at a bank in exchange for the bank agreeing to lend up to $10 million to the corporation at 1% below the prime lending rate. At a minimum, compensating balances must be disclosed in the notes to the corporation's financial statements.

compilation

Often referred to as write-up work, a compilation refers to financial statements prepared by an accountant without reviewing or auditing the amounts. Often the accountant merely takes a client's amounts and presents them in the income statement and balance sheet format and does not provide any assurances regarding the amounts.

compiled financial statements

Financial statements prepared by an accountant based on the amounts provided by a client. The accountant does not review or audit the amounts provided and therefore does not provide any assurances regarding the validity of the amounts.

compound interest

Interest on interest. For example, if $1,000 is deposited in an account earning interest of 6% per year the account will earn $60 in the first year. In year two the account balance will earn $63.60 (not $60.00) because 6% interest is earned on $1,060. Similarly the bank paying the interest will incur interest on interest.

compound journal entry

A journal entry with more than the minimum of one debit and one credit. Example: a debit to Cash of $500 and a credit to Sales of $475 and a credit to Sales Tax Payable of $25.

compounding of interest

See compound interest.

comprehensive income

Comprehensive income consists of two components:

- Net income (or loss) from the income statement, and
- Other comprehensive income (some additional items that are not reported on the income statement).

Other comprehensive income includes the following:

- Unrealized gains/losses on *some* investment securities and financial instruments.
- Foreign currency translation adjustments
- Unrealized gains/losses on postretirement benefit plans

comptroller

The British term for controller.

conceptual framework

One of the first efforts begun in the 1970s by the Financial Accounting Standards Board to articulate and organize into a cohesive framework all of the accounting rules that had been developed in the past. It was hoped that future accounting rules would evolve from this framework.

condensed balance sheet

A highly summarized balance sheet

condensed financial statements

Financial statements (such as the income statement and balance sheet) that summarize much of the detail into a few major lines of information.

condensed income statement

A highly summarized income statement

conformity rule

See inventory conformity rule.

conservatism

This accounting guideline states that if doubt exists between two acceptable alternatives (in other words the accountant needs to break a tie), the accountant should choose the alternative that will result in a lesser asset amount and/or a lesser profit. A classic example is inventory where the net realizable value (NRV) is less than the actual cost. The accountant must decide whether to leave the inventory at cost or to reduce the inventory amount to its NRV. Conservatism directs the accountant to reduce the inventory to the lower amount (NRV). This results in a lower asset amount and a debit to an income statement account, such as Loss from Reducing Inventory to LCM.

consigned goods

Merchandise that is not owned by the party in possession of the goods. For example, a craftsperson might have produced 100 ornate wood items. In order to sell the items, the person asks a local merchant to take five of the items on consignment. This means that the merchant has possession of the five items and will attempt to sell them for a commission, but the merchant does not own the items. Those five items are consigned goods. (When the merchant sells one of the items, the merchant might be required to remit 80% of the selling price to the craftspersons and can keep 20% as a commission.) The merchant is the consignee and the craftsperson is the consignor.

consignee

The party receiving goods to be sold. See consigned goods.

consignment

Sending merchandise to another party (an agent, consignee) in order to sell the merchandise. Also see consigned goods.

consignor

The party who delivered its goods to another party (consignee). The objective is for consignee to sell the goods for the consignor. Also see consigned goods.

consistency

A quality of accounting information that facilitates comparing a company's reporting of one accounting period to another. For example, the reader of a company's financial statements can assume that the company is using the same inventory cost flow assumption this period as it used last period or last year. (If the company did change, it must be disclosed to the reader.)

consistent

See consistency.

consolidated financial statements

Financial statements that reflect the total economic entity. For example, on a consolidated income statement a corporation having several subsidiaries would report the total of all of its companies' sales that were made to customers outside of its group. (Sales to companies within its group of related companies would be excluded as well as the purchases within its group.) A consolidated balance sheet would report the combined assets except for claims against companies within its group. Liabilities would be combined except for amounts owed to companies within its group.

constant-dollar

A dollar adjusted for inflation. If an asset such as land was purchased for $10,000 many years ago when the consumer price index (CPI) was 100 and today the CPI is 400, today's constant-dollar amount would be $40,000. However, generally accepted accounting principles (specifically the monetary unit assumption) assumes that the CPI is unchanging. Therefore the land will be reported at its original, unadjusted amount of $10,000.

constraints

In financial accounting this term often refers to the accounting guidelines or principles of conservatism and materiality.

construction work-in-progress

This is a long term asset account that accumulates the cost of a project that has not yet been placed into service. When the project is finished and placed into the service, the cost is removed from this account and is recorded in a plant asset account.

consumer price index

A government index that tracks the changes in prices in order to measure general inflation. This index can be used by small companies to obtain the benefits of LIFO without tracking individual units in inventory. See the income tax code or a tax professional for more information.

contingent gain

A potential gain that is not recognized by accountants in the financial statements until it actually occurs. For example, Company P is suing Company D over a patent infringement. Company P has a contingent gain. Because of conservatism, accountants usually do not report or disclose contingent gains (but will report or disclose contingent losses).

contingent liability

A *potential* liability dependent upon some future event occurring or not occurring. For example, a company is named as a defendant in a $1 million lawsuit. Does that mean the company automatically has a liability of $1 million? What if the lawsuit has no merit and can easily be defended? If it is *probable* that the company will lose and the amount can be estimated, a journal entry is prepared to debit Loss from Lawsuit and to credit Lawsuit Payable. If it is *possible* but not probable that the company will lose, the journal entry is not made but instead there will be a footnote disclosure. If the lawsuit is *remote* (a nuisance suit without any merit), there is no need for a journal entry and no need to disclose the lawsuit. Accountants usually consider product warranties to be a contingent liability that is both probable and can be estimated and is therefore recorded with a journal entry.

contingent loss

A *potential* loss that is dependent upon some future event occurring or not occurring. If the loss is *probable* and the amount can be estimated, then the loss and a liability are recorded with a journal entry. If the loss is only *reasonably possible* (not probable), then a journal entry is not recorded but a disclosure should be made in the notes to the financial statements. If the loss is *remote*, then neither a journal entry nor a disclosure is required.

continuing operations

The operating activities of a company, excluding the major segments of the company that are being discontinued.

continuous budget

See rolling budget.

contra account

An account with a balance that is the opposite of the normal balance. For example, Accumulated Depreciation is a contra asset account, because its credit balance is contra to the debit balance for an asset account. Another example is the owner's drawing account. This is an owner's equity account and as such you would expect a credit balance. However, the drawing account has a debit balance. Other examples include (1) the allowance for doubtful accounts, (2) discount on bonds payable, (3) sales returns and allowances, and (4) sales discounts. The contra accounts cause a reduction in the amounts reported. For example net sales is gross sales minus the sales returns, the sales allowances, and the sales discounts. The net realizable value of the accounts receivable is the accounts receivable minus the allowance for doubtful accounts.

contra asset account

An asset account which is expected to have a credit balance (which is contrary to the normal debit balance of an asset account). The contra asset account is related to another asset account. For example, the contra asset account Allowance for Doubtful Accounts is related to Accounts Receivable. The contra asset account Accumulated Depreciation is related to a constructed asset(s), and the contra asset account Accumulated Depletion is related to natural resources.

The net of the asset and its related contra asset account is referred to as the asset’s book value or carrying value.

contra equity account

An owner’s or stockholders’ equity account with a debit balance instead of the normal credit balance. Examples include the owner’s drawing account, a dividend account, and the treasury stock account.

contra expense account

An expense account which is expected to have a credit balance instead of the typical debit balance.

contra inventory account

A general ledger inventory account that has a credit balance instead of an asset’s usual debit balance. An example is the account Reduction of Inventory to the Net Realizable Value.

contra liability account

A liability account with a debit balance. Discount on Bonds Payable is a contra account associated with the liability account Bonds Payable.

contra owner’s equity account

See contra equity account.

contra revenues account

A revenues account with a debit balance instead of the usual credit balance. Examples include sales returns, sales allowances, and sales discounts.

contractual interest rate

The interest rate specified or stated in a note payable or in a bond payable. Often this rate is fixed and will not change during the life of the note or bond.

contributed capital

Sometimes used as a heading in place of paid-in capital.

contribution approach income statement

An income statement that subtracts all variable costs and expenses from revenues in order to show the contribution margin. From that is subtracted the fixed costs and expenses to arrive at net income. To learn more, see Explanation of Break-even Point.

contribution margin

The result of subtracting all variable expenses from revenues. It indicates the amount available from sales to cover the fixed expenses and profit.

contribution margin per unit

Selling price per unit minus variable costs per unit, or revenues per unit minus expenses per unit.

contribution margin ratio

This ratio indicates the percentage of each sales dollar that is available to cover a company's fixed expenses and profit. The ratio is calculated by dividing the contribution margin (sales minus all variable expenses) by sales.

contributions

The revenue classification used by nonprofit organizations to account for the amounts received as donations. It is also an expense classification for the donations made to another nonprofit organization. Contributions may be in the form of cash, securities, other property, as well as unconditional promises to give assets at a later date.

Contributions made by a donor without conditions attached are referred to as unrestricted contributions. Contributions with donor-imposed restrictions are either temporarily restricted or permanently restricted.

You can learn more about contributions by reading FASB Statement No. 116 at www.FASB.org.

control account

A general ledger account containing the correct total amount without containing the details. For example, Accounts Receivable could be a control account in the general ledger. Each day the *total* of the day's credit sales and the day's collections are posted to this account. However, the details involving specific customers' accounts will be found in a subsidiary ledger.

controller

The chief accounting officer of a company. This person would head up the accounting department.

controller's cushion

See budgetary slack.

controller's reserve

See budgetary slack.

conversion costs

The combination of a manufacturer's direct labor and factory overhead.

convertible bond

A bond (long term note) that can be exchanged by the holder for a specified number of shares of stock in the company. The convertibility feature usually allows for the bond to have a lower interest rate when it is issued. The holder of the bond enjoys the potential for a gain if the stock price increases.

convertible preferred stock

Preferred stock that can be exchanged by the holder for a specified number of shares of common stock of the same company.

COO

See chief operating officer.

copyright

An exclusive right granted by the federal government to publish and sell various works. In accounting a copyright is recorded at its cost and is reported on the balance sheet as an intangible asset.

corporation

A legal entity organized under state laws that is considered separate from its owners. Ownership is evidenced by shares of stock.

correcting entry

A journal entry to correct an erroneous amount previously entered in the general ledger.

correlation

The relationship between two variables. There can be correlation without a cause-and-effect relationship. Also see coefficient of correlation.

COS

The acronym for *cost of sales* or for the *cost of services.*

cost

In accounting, cost is defined as the cash amount (or the cash equivalent) given up for an asset. Cost includes all costs necessary to get an asset in place and ready for use. For example, the cost of an item in inventory also includes the item's freight-in cost. The cost of land includes all costs to get the land ready for its use. Also see cost principle.

cost accounting

The accounting focused on determining the cost per unit of a manufacturer in order to value inventory and cost of goods sold. It is also used to determine unit costs of items processed in service businesses, such as a bank's cost to process a check or deposit.

cost behavior

The change in total costs in response to the change in some activity. For example, some of the costs of owning and operating a vehicle will increase in total with an increase in miles driven. These are referred to as variable costs and include gasoline and tires. Some other costs will not change in total with a reasonable increase in miles driven. These costs are referred to as fixed costs and include insurance and parking. Other costs might be part variable and part fixed. These are referred to as mixed costs and an example might be depreciation.

cost center

Usually a department within a company that is responsible for its costs but not revenues or profit.

cost flow assumption

An assumption that determines the order in which costs should flow out of a balance sheet account (e.g. Inventory, Investments, Treasury Stock) when the item is sold. For an illustration of the cost flow assumption, see Explanation of Inventory and Cost of Goods Sold.

cost method of recording treasury stock

The method of accounting for treasury stock whereby the cost of the stock that is repurchased by the issuing corporation is recorded and is reported in the contra stockholders' equity account Treasury Stock.

cost object

A cost object is often a product or department for which costs are accumulated or measured. For example, a product is the cost object for direct materials, direct labor and manufacturing overhead. The factory maintenance department is a cost object for the cost of the maintenance employees and the maintenance supplies. Later the factory maintenance department costs will be assigned to products, which are also cost objects.

A cost object can also be a customer, a machine, a group of machines, a group of employees, etc.

cost of capital

A corporation's cost of capital is its weighted average after-tax cost of its debt, preferred stock, common stock, retained earnings, and other components of stockholders' equity. The cost of capital is usually the minimum return that a company should accept on its investments.

cost of carrying inventory

The incremental cost of storing or holding inventory. It is an annual percentage that includes the cost of rent, insurance, cost of capital, deterioration and obsolescence.

cost of goods available for sale

This is the sum of the beginning inventory of merchandise plus the net cost of the merchandise purchased including freight-in.

cost of goods purchased

For a merchandiser this is the cost of merchandise purchased after deducting purchase returns, purchase allowances, and purchase discounts but after adding freight-in.

cost of goods sold

Cost of goods sold is usually the largest expense on the income statement of a company selling products or goods. Cost of Goods Sold is a general ledger account under the *perpetual inventory system*.

Under the *periodic inventory system* there will not be an account entitled Cost of Goods Sold. Instead, the cost of goods sold is computed as follows: cost of beginning inventory + cost of goods purchased (net of any returns or allowances) + freight-in - cost of ending inventory.

This account balance or this calculated amount will be matched with the sales amount on the income statement.

cost of products sold

See cost of goods sold.

cost of sales

See cost of goods sold.

cost principle

The accounting guideline requiring amounts in the accounts and on the financial statements to be the actual cost rather than the current value. Accountants can show an amount less than cost due to conservatism, but accountants are generally prohibited from showing amounts greater than cost. (Certain investments will be shown at fair value instead of cost.)

cost ratio

In estimating the ending inventory under the retail method the cost ratio is the cost of goods available divided by the retail value of the goods available.

cost-volume-profit (CVP)

The analysis of how profits change as volume changes. The calculation of the break-even point is a part of cost-volume-profit analysis.

coupon bond

See bearer bond.

CPA

See certified public accountant.

CPA Exam

More formally known as the *Uniform CPA Examination*. This rigorous, 14-hour, computer-based exam consists of questions developed by the American Institute of Certified Public Accountants. The exam is in English only and application must be made through one of 55 boards of accountancy. Learn more about the CPA Exam at our Accounting Career Center.

cr.

The abbreviation of the accounting and bookkeeping term *credit*.

credit (as in debit and credit)

To enter an amount on the right side of an account. Normal entries to revenue accounts are credits. Liabilities normally have credit balances. To learn more, see Explanation of Debits and Credits.

credit (as in debt, not cash)

Allowing a person or company to purchase goods or services without paying cash at the time of purchase.

credit balance

A balance on the right side (credit side) of an account in the general ledger.

credit line

See line of credit.

credit memo

A document issued to a customer by a seller which reduces the seller's accounts receivable and its net sales. It also reduces the buyer's accounts payable and net purchases.

A document issued by a bank that increases a depositor's bank balance.

credit memorandum

See credit memo.

credit sales

Sales made on account. Sales where the customer is allowed to pay at a later date. Noncash sales.

credit terms

The terms which indicate when payment is due for sales made on account (or credit). For example, the credit terms might be 2/10, net 30. This means the amount is due in 30 days; however, if the amount is paid in 10 days a discount of 2% will be permitted. Other terms might be net 10 days, due upon receipt, net 60 days, etc.

creditor

Someone who has granted credit. If a bank lends a company money, the bank is a creditor. If a supplier sold merchandise to a company on credit, the supplier is a creditor.

crossfoot

A word that means to add column totals across to see if the sum will equal the grand total. In the table below each of the columns A through Total was “footed” (added or summed) in order to get each column’s total. Note that the Total Column contains the total amount for each item. To crossfoot means to add the totals shown in Columns A + B + C to verify that it sums to the Total Column. In the following example, crossfooting means to add the following column totals: 20 + 15 + 16 to verify that it equals the total of the Total Column, which is listed as 51.

Item	A	B	C	**Total**
Red	7	6	7	**20**
Blue	4	6	3	**13**
Yellow	9	3	6	**18**
Total	**20**	**15**	**16**	**51**

CSV

See cash surrender value.

cumulative preferred stock

This preferred stock feature that assures the owner that any omitted dividends on this stock will be made up before the common stockholders will receive a dividend. Any omitted dividends on cumulative preferred stock are referred to as *dividends in arrears* and must be disclosed in the notes to the financial statements.

current assets

Cash and other resources that are expected to turn to cash or to be used up within one year of the balance sheet date. (If a company’s operating cycle is longer than one year, an item is a current asset if it will turn to cash or be used up within the operating cycle.) Current assets are presented in the order of liquidity, i.e., cash, temporary investments, accounts receivable, inventory, supplies, prepaid insurance.

current liabilities

Obligations due within one year of the balance sheet date. (If a company’s operating cycle is longer than one year, an item is a current liability if it is due within the operating cycle.) Another condition is that the item will use cash or it will create another current liability. (This means that if a bond payable is due within one year of the balance sheet date, but the bond will be retired by a bond sinking fund (a long-term restricted asset) the bond will not be reported as a current liability.)

current maturity of long-term debt

See current portion of long-term debt.

current portion of long-term debt

The principal portion of an obligation that must be paid within one year of the balance sheet date. For example, if a company has a bank loan of $50,000 that requires monthly interest and principal payments, the next 12 monthly principal payments will be the current portion of the long-term debt. That amount is reported as a current liability and the remaining principal amount is reported as a long-term liability.

current ratio

The ratio of current assets to current liabilities. This ratio is an indicator of a company's ability to meet its current obligations. To learn more, see Explanation of Financial Ratios.

current value

The present fair market value.

current year's net income

Often this account appears as a line in the retained earnings section of stockholders' equity (balance sheet) and will show the year-to-date net income. The reason is that some accounting software will not put the current year's net income into the Retained Earnings account until the accounting year is finished.

customer deposits

A liability account on the books of a company receiving cash in advance of delivering goods or services to the customer. The entry on the books of the company at the time the money is received in advance is a debit to Cash and a credit to Customer Deposits.

CVP

See cost-volume-profit (CVP).

cycle counting

Spreading the physical counting of inventory throughout the year. For example, a company may physically count a different 10% of its inventory each month instead of counting 100% of its inventory once per year.

Accounting Terms (D)

days' sales in accounts receivable

This indicates (on average) how many days of credit sales have not yet been collected. If the credit terms are net 30 days, you would expect this to be at least 30 days. To learn more, see Explanation of Financial Ratios.

days' sales in inventory

This indicates (on average) how many days it takes to sell the merchandise held in inventory. To learn more, see Explanation of Financial Ratios.

DCF

See discounted cash flow model.

death spiral

The repeated elimination of products without a corresponding decrease in overhead costs. As a result the amount of overhead allocated to each unit of product increases. If selling prices are increased to cover the higher per unit allocated costs, fewer units might be sold. With fewer unit sales and no reduction in overhead costs, the remaining products will be assigned greater per unit overhead costs. If selling prices are increased to cover these still higher unit costs, there could be a further decline in sales.

debenture bond

An unsecured bond. For example, a bond not secured by a lien on the issuer's property.

debit (as in debit and credit)

The accounting term that means an entry will be made on the left side of an account. To learn more, see Explanation of Debits and Credits.

debit balance

A balance on the left side of an account in the general ledger. Typically expenses, losses, and assets have debit balances.

debit card

Usually a plastic card that is used in place of writing a check. The amount of the transaction is immediately deducted from the user's checking account.

debit memorandum

A form used at a bank to inform its customer that the customer's account is being reduced for a fee or other charge.

debt extinguishment

To eliminate debt such as a company's repurchase or retirement of its outstanding bonds.

debt financing

Taking out a loan or issuing bonds in order to acquire an asset or another business.

debt issue costs

See bond issue costs.

debt ratio

The ratio of total liabilities to total assets. For example, a company with total assets of $800,000 and total liabilities of $200,000 will have a debt ratio of 0.25 to 1, or 25% ($200,000 divided by $800,000).

debt service

The total of interest and principal payments required to be paid on loans payable.

debt to equity ratio

The ratio of total liabilities to stockholders' equity. The higher the proportion of debt to equity, the more risky the company appears to be. An indicator of the amount of financial leverage at a company. It indicates the proportion of the company's assets provided by creditors versus owners. To learn more, see Explanation of Financial Ratios.

debt to total asset ratio

Total liabilities divided by total assets. This indicates how much of a corporation's assets are financed by lenders/creditors as opposed to purchased with owners' or stockholders' funds. If a high proportion of the assets are financed by creditors, the corporation is considered to be leveraged.

debtor

The person that owes money. If a bank lent you money, the bank is the creditor and you are the debtor.

decentralization

Pushing authority and decision making down to the managers and employees who are closer to the work.

declaration date

The date on which the board of directors of a corporation declares a dividend on the corporation's stock. On this date an accounting entry is made to debit Retained Earnings and to credit Dividends Payable.

declining-balance method of depreciation

A depreciation technique where a constant percentage (such as 200%, 150%, or 125%) is applied to the book value of an asset. (As an asset is depreciated its book value declines.) This technique results in greater depreciation in the early years of an asset's life and smaller depreciation in the later years of the asset's life (compared to constant depreciation amounts using straight-line depreciation). To learn more, see Explanation of Depreciation for an illustration.

deferral

In accounting this means to defer or to delay recognizing certain revenues or expenses on the income statement until a later, more appropriate time. Revenues are deferred to a balance sheet liability account until they are earned in a later period. When the revenues are earned they will be moved from the balance sheet account to revenues on the income statement.

Expenses are deferred to a balance sheet asset account until the expenses are used up, expired, or matched with revenues. At that time they will be moved to an expense on the income statement.

deferral-type adjusting entry

A journal entry that adjusts an amount already recorded on the books of a company because part of the amount pertains to a future accounting period. To learn more, see Explanation of Adjusting Entries.

deferred charge

See deferred expense.

deferred debits

See deferred expense.

deferred expense

A cost that has been recorded in the accounting records and reported on the balance sheet as an asset until matched with revenues on the income statement in a later accounting period.

deferred income taxes

Often a liability representing the differences between the income tax expense associated with the revenues and expenses reported on a corporation's income statements and the actual income tax appearing on the corporation's income tax returns.

deferred revenues

A balance sheet liability account that reports amounts received in advance of being earned. For example, if a company receives $10,000 today to perform services in the next accounting period, the $10,000 is unearned in this accounting period. It is deferred to the next accounting period by crediting a liability account such as Unearned Revenues. Next period (when it is earned) a journal entry will be made to debit the liability account and to credit a revenue account.

deficit

This term is used in place of retained earnings when the balance in the retained earnings account is negative (a debit balance).

defined benefit pension plan

A retirement plan that specifies the amount that a retiree will receive, such as 1% of the person's recent salary times the years of service. The employer's obligation is to contribute enough money to meet those payments.

defined contribution pension plan

A retirement plan that does not specify the amount that a retiree will receive. Rather, the employer's obligation is to contribute a specific amount into a fund to be used for payments to retirees.

delivery equipment

A long term asset account containing the cost of delivery equipment acquired by a company and used in its business. The account will appear on the balance sheet under the heading of Property, Plant and Equipment. There will be a related contra asset account Accumulated Depreciation: Delivery Equipment where the depreciation expense is accumulated.

delivery expense

This account shows the amount of delivery expense incurred (occurring) during the accounting period shown in the heading of the income statement. The title of this account could also be Freight Out or Transportation Out.

demand deposits

This term refers to checking account balances. On a bank's balance sheet, demand deposits are reported as current liabilities.

departmental overhead rate

Rates based on a department's direct and indirect overhead costs and some measure of the department's activity, such as the department's machine hours. Departmental rates are more accurate than plant-wide rates when a company manufactures diverse products requiring a variety of processes.

dependent variable

An item that is dependent on another item. For example, your wages would be a dependent variable and the hours you work would be the independent variable. This relationship is often expressed as $y = a + bx$, where y is the dependent variable and x is the independent variable.

depletion

The systematic allocation of the cost of a natural resource from the balance sheet to the income statement.

depletion expense

Amount of depletion charged to expense on the income statement for the period indicated in its heading. The amount is also credited to the contra asset account Accumulated Depletion.

depositor

A person or business that has a checking account or savings account at a bank.

deposits

A liability account in a bank's general ledger that indicates the amounts owed to bank customers for the balances in the customers' individual checking, savings, and certificate of deposit accounts.

deposits in transit

A company's receipts that appear on the company's records but do not yet appear on the bank statement. For example, a retail store's receipts of March 31 are deposited after banking hours on March 31 or on the morning of April 1. Those receipts are in the company's general ledger Cash account on March 31, but are not on the March 31 bank statement. As a result they are said to be "in transit" on March 31. On the bank reconciliation a deposit in transit is an adjustment (an addition) to the balance per bank.

depreciable cost

The amount of an asset's cost that will be depreciated. It is the cost minus the expected salvage value. For example, if equipment has a cost of $30,000 but is expected to have a salvage value of $3,000 then the depreciable cost is $27,000.

depreciated

An asset's cost that has been assigned to Depreciation Expense.

depreciation

The systematic allocation of the cost of an asset from the balance sheet to Depreciation Expense on the income statement over the useful life of the asset. (The depreciation journal entry includes a debit to Depreciation Expense and a credit to Accumulated Depreciation, a contra asset account). The purpose is to allocate the cost to expense in order to comply with the matching principle. It is not intended to be a valuation process. In other words, the amount allocated to expense is not indicative of the economic value being consumed. Similarly, the amount not yet allocated is not an indication of its current market value. To learn more, see Explanation of Depreciation.

depreciation - accelerated

See accelerated depreciation.

depreciation - double declining balance

See double declining balance method of depreciation.

depreciation - straight line

See straight-line method of depreciation.

depreciation - sum of the years' digits

See sum of the years' digits method of depreciation.

depreciation expense

The income statement account which contains a portion of the cost of plant and equipment that is being matched to the time interval shown in the heading of the income statement. (There is no depreciation expense for land.)

depreciation expense: equipment
The income statement account which contains a portion of the cost of equipment that is being expensed during the time interval shown in the heading of the income statement.

depreciation methods
To learn more, see Explanation of Depreciation.

differential cost
See incremental cost.

differential revenue
The difference in total revenues between alternative actions or plans.

direct allocation method
A method used in allocating the costs of manufacturing service departments (factory administration, maintenance, etc.) directly to the producing departments in the factory. Under this method, no service department cost will be allocated to another service department.

direct cost
A cost that can be traced to a cost object. For example, the flour used in baking bread is a direct cost of a bakery's bread.

The wages and salaries of the employees working exclusively in a manufacturer's maintenance department are *direct costs of the maintenance department*. (However, these costs are *indirect product costs*, since they will need to be allocated to the products manufactured.)

direct costing
A method where only the variable manufacturing costs are assigned to inventory and the cost of goods sold. Fixed manufacturing costs are viewed as expenses of the period in which they are incurred. This method is not allowed for external financial statements, but can be used internally. External financial statements must have fixed manufacturing costs allocated to the products.

direct labor efficiency variance
A variance arising in a standard costing system that indicates the difference between 1) the standard cost of the direct labor that should have been used (the standard hours times the standard rate) for the good output, and 2) the actual hours of direct labor used at its standard rate per hour. To learn more, see Explanation of Standard Costing.

direct labor price variance
See direct labor rate variance.

direct labor quantity variance
See direct labor efficiency variance.

direct labor rate variance

A variance arising in a standard costing system that indicates the difference between the standard cost of direct labor for the good output (standard hours times standard rate) and the standard cost of the actual hours of direct labor used (actual hours times standard rate). To learn more, see Explanation of Standard Costing.

direct labor usage variance

See direct labor efficiency variance.

direct materials

Raw materials that are a traceable component of a manufactured product. For example, the direct material of a baseball bat is the wood. Flour, sugar, and vegetable oil are direct materials of a company that manufactures dessert products.

direct materials efficiency variance

See direct materials usage variance.

direct materials inventory

That component of a product that has not yet been placed into the product or into work-in-process inventory. This account often contains the standard cost of the direct materials on hand. A manufacturer must disclose in its financial statements the actual cost of materials on hand as well as its actual cost of work-in-process and finished goods.

direct materials price variance

A variance arising in a standard costing system that indicates the difference between the actual cost of direct materials and the standard cost of direct materials. Recognizing this variance at the time the direct materials are put into the direct or raw materials inventory is preferred over recognizing the variance at the time the materials are placed into production (work-in-process). To learn more, see Explanation of Standard Costing.

direct materials quantity variance

See direct materials usage variance.

direct materials usage variance

A variance arising in a standard costing system that indicates the difference between the standard cost of direct materials that should have been used (standard quantity times standard cost) for the good output and the actual quantity of direct materials used at their standard cost. To learn more, see Explanation of Standard Costing.

direct method

The direct method could refer to the method of preparing the statement of cash flows.

The direct method could also refer to the method of allocating a manufacturing facility's service departments to its production departments.

direct write-off method

A method for recognizing bad debts expense arising from credit sales. Under this method there is no allowance account. Rather, an account receivable is written-off directly to expense only after the account is determined to be uncollectible. This method is required for income tax purposes. See allowance method for bad debts expense on the income statements.

disclosure

See full disclosure principle.

discontinued operations

Operations of an entire division, subsidiary, or segment of a company where a formal plan exists to eliminate it from the company. (It involves more than pruning a product line of certain models of products.)

The revenues, gains, expenses, and losses pertaining to the business segment are removed from the company's continuing operations and are reported separately on the company's income statement. The amounts that pertain to discontinued operations are reported near the end of the income statement but before the amounts for extraordinary items and the cumulative effect of a change in an accounting principle. The amounts will be shown on a per share basis, if the company's stock is publicly traded.

discount on bonds payable

A contra liability account that reports the amount of unamortized discount associated with bonds that are outstanding. The discount on bonds payable originates when bonds are issued for less than the bond's face or maturity amount. The debit balance in this account will be amortized to bond interest expense over the life of the bonds and results in more interest expense than interest paid. To learn more see Explanation of Bonds Payable.

discount on notes payable

A contra liability account arising when the proceeds of a note payable is less than the face amount of the note. The debit balance in this account will be amortized to interest expense over the life of the note.

discount on notes receivable

A contra asset account arising when the present value of a note receivable is less than the face amount of the note. The credit balance in this account will be amortized to interest revenue over the life of the note.

discount rate

In accounting this is the rate used to discount future cash flows in order to determine their present value.

discounted cash flow model

A process which discounts future cash flows to the present in order to reflect the time value of money. Examples of the discounted cash flow model are net present value and internal rate of return.

discounted cash flow technique

See discounted cash flow model.

disposal of fixed assets

The sale, retirement, or exchange of property, plant and equipment.

dividend

A distribution of part of a corporation's past profits to its stockholders. A dividend is not an expense on the corporation's income statement.

dividend declaration date

See declaration date.

dividend payment date

The date a corporation pays a dividend to its shareholders. On this date the accounting entry will be a debit to Dividends Payable and a credit to Cash.

dividend payout ratio

The percentage resulting from dividing dividends per share by earnings per share.

dividend yield

The percentage resulting from dividing the dividends per share by the market price per share.

dividends declared

A temporary account that is debited when cash dividends have been declared (instead of debiting the Retained Earnings account. At the end of the accounting year, the balance in this account is transferred to the Retained Earnings account.

dividends payable

A current liability account that reports the amounts of cash dividends that have been declared by the board of directors but not yet distributed to the stockholders.

dividends in arrears

Past omitted dividends on cumulative preferred stock. Generally these omitted dividends were not declared and, therefore, do not appear on the corporation's balance sheet as a liability. However, they must be disclosed in the notes to the balance sheet.

divisions

Segments of a business. For example, a corporation may have a consumer division and an industrial division in order to improve its effectiveness in marketing its goods.

dollar-value LIFO retail method

A method used by retailers to achieve the LIFO cost flow without tracking individual units. A further advantage is that pools of products are used. This will likely mean less liquidation of LIFO cost layers that would occur with the tracking of individual units.

dollar-value retail method

A method used by retailers for estimating the cost of ending inventory without tracking the individual units of product.

donated capital

Part of stockholders' equity representing the fair market value of an asset at the time it was received as a gift. For example, a corporation may be given a large tract of land from a community if the corporation constructs a manufacturing facility in the community.

donor

A person or organization that gives or donates money, property, services, etc.

donor-imposed condition

A requirement that the receiving nonprofit organization must return an asset to the donor in the event that some future and uncertain event does or does not occur.

donor-imposed restriction

Either a temporary restriction or a permanent restriction imposed by the donor of an asset when it is contributed to a nonprofit organization.

donor restriction

See donor-imposed restriction.

double-declining balance method of depreciation

An accelerated method of depreciation, where two times the straight-line rate is applied to the book value of an asset. The result is more depreciation expense in the early years and less in the later years of the asset's life compared to the straight-line method. To learn more, see Explanation of Depreciation.

double entry accounting

The 500 year-old accounting system where every transaction is recorded into at least two accounts. To learn more, see Explanation of Debits and Credits.

downward demand spiral

See death spiral.

dr.

The abbreviation for the accounting and bookkeeping term *debit.*

draw

The withdrawal of business cash or other assets by the owner for the personal use of the owner. Withdrawals of cash by the owner are recorded with a debit to the owner's drawing account and a credit to the cash account.

drawing account

The contra owner's equity account that reports the amount of withdrawals of business cash or other assets by the owner for personal use during the current accounting year. At the end of the accounting year, the balance in the drawing account is transferred (closed) to the owner's capital account.

dues

See membership dues.

duplicate payment

In accounting and bookkeeping this term is used to describe paying a vendor more than once for the amount owed.

Accounting Terms (E)

early payment discount

Often a 1% or 2% reduction in the amount owed if an invoice is paid within 10 days of the invoice date instead of the customary 30 days.

earned

Under accrual accounting an item has been "earned" and is reported as revenue when a service has been performed or the ownership to a product has been transferred from the seller to the buyer (not when cash is received).

earnings per share (EPS)

This financial statistic is the net income of a corporation after income tax (less any preferred dividends) divided by the weighted average number of shares of common stock outstanding during the same period of time.

earnings quality

See quality of earnings.

EBITDA

The acronym for earnings before interest, taxes, depreciation, and amortization. This measure is used by some companies as a supplementary disclosure, since EBITDA does not comply with U.S. GAAP (generally accepted accounting principles). Some people use EBITDA when attempting to estimate the value of a company.

economic entity assumption

An accounting principle/guideline that allows the accountant to keep the sole proprietor's business transactions separate from the owner's personal transactions even though a sole proprietorship is not legally separate from the owner.

economic life

Also referred to as the useful life. This differs from the physical life of an asset. For example, a computer may have a physical life of 50 years, but its economic or useful life might be five years.

economic lot size

The optimum purchase (or production) quantity which minimizes the combined total cost of carrying inventory and processing additional purchase orders (or production setups).

economic order quantity (EOQ) model

A formula that calculates the optimum quantity to be purchased (or produced) so as to minimize the combined total cost of carrying inventory and processing additional purchase orders (or production setups). The formula for the EOQ model is the square root of [(2 X Units of Annual Demand X Cost to Place an Order or Setup) divided by Carrying Cost per Unit].

effective interest rate

See yield to maturity.

effective interest rate method of amortization

The preferred method for systematically moving bond discount or premium from the balance sheet over to interest expense on the income statement over the life of the bond. This method is superior to the straight-line method of amortization, because it causes interest expense to be in tandem with the book value of the bonds. In other words, under this method bond interest expense on the income statement will decrease when the book value of the bonds decreases on the balance sheet. Bond interest expense will increase as the book value of the bonds increases. To learn more, see Explanation of Bonds Payable.

efficiency variance

See direct labor efficiency variance and variable manufacturing overhead efficiency variance.

EFT

See electronic funds transfer.

e.g.

For example.

eighty/twenty rule

It is common for a small quantity to account for most of the value. Examples: 20% of the people may have 80% of the wealth; 20% of the members do 80% of the work; 20% of the items in inventory account for 80% of the sales; 20% of your customers generate 80% of your sales; 20% of your customers cause 80% of your headaches, etc.

This rule allows managers to monitor 80% of the value by monitoring approximately 20% of the items.

electronic funds transfer (EFT)

A method of payment used in place of a paper check.

employee fringe benefits

Benefits given to employees that are in addition to wages and salaries. Examples include health, dental, life, vision, and disability insurances, employer's portion of social security and Medicare tax, paid absences (sick days, holidays, vacation days), pension or retirement contributions, unemployment tax, worker compensation insurance, profit sharing, and other benefits. These benefits often are equal to 50% of the wages and salaries.

employer payroll taxes

Employer payroll taxes include an employer's portion of Social Security and Medicare taxes and the state and federal unemployment taxes.

Employer's Tax Guide

A publication by the U.S. Internal Revenue Service (IRS) to assist employers with federal payroll taxes. The complete title of the publication is Publication 15 (Circular E), Employer's Tax Guide. It is available at www.irs.gov.

endowment

See endowment fund.

endowment fund

Usually a permanently restricted asset for which the principal portion must be retained indefinitely. The earnings from an endowment fund could be unrestricted or temporarily restricted.

entity as a whole

The phrase used by FASB Statement 117 that describes the required focus of a nonprofit's external financial statements. Previously the external financial statements focused on individual funds.

EOM

End of month.

EOQ

See economic order quantity (EOQ) model.

EPS

See earnings per share.

equipment

Equipment is a noncurrent or long-term asset account which reports the cost of the equipment. Equipment will be depreciated over its useful life by debiting the income statement account Depreciation Expense and crediting the balance sheet account Accumulated Depreciation (a contra asset account).

equipment rental expense

The expense incurred during the time interval indicated on the income statement for using rented equipment.

equity

The difference between assets and liabilities, such as stockholders' equity, owner's equity, or a nonprofit organization's net assets.

Also used to indicate an owner's interest in a personal asset. For example, the owner of a $200,000 house with a $75,000 mortgage loan is said to have equity of $125,000.

equity financing

Using capital stock (common stock or preferred stock) instead of debt in order to finance an investment such as a plant asset.

equity section of the balance sheet

The part of a balance sheet with the heading stockholders' equity or owner's equity. The total amount of this section is the amount of reported assets minus the amount of reported liabilities.

equivalent units

See equivalent units of production.

equivalent units of production

A term used in cost accounting to arrive at the cost per unit. The term is associated with the units that are not completed at the end of an accounting period. For example, if 500 units are completed as far as materials, but are only 40% completed as far as direct labor and manufacturing overhead, the equivalent units are 500 for materials and 200 (40% of 500) for direct labor and manufacturing overhead.

escrow

Money set aside for a specific purpose. An individual's monthly mortgage payment might include $300 per month for the real estate taxes due at the end of the year. The $300 is said to be put into escrow each month.

estimates

Approximate amounts. Accountants use estimates for depreciation expense, warranty expense, bad debts expense, monthly accruals for utilities, bonuses, income taxes, etc. Also see change in accounting estimate.

estimating inventory

To learn more, see Explanation of Inventory and Cost of Goods Sold.

exchange of dissimilar nonmonetary assets

The exchange or trade-in of a long-term asset for a completely different long-term asset. For example, exchanging an antique car for land.

exchange of similar nonmonetary assets

The exchange or trade-in of a long-term asset for a similar long-term asset. For example, trading the old delivery truck for a new delivery truck; trading a two-family rental unit toward an eight-family rental unit.

ex-dividend

The day after the record date for a cash dividend on shares of stock. Theoretically, the market price of the stock should drop on this day by the amount of the dividend.

exempt employee

An employee that is not entitled to overtime wages or salaries. Examples of exempt employees include executives, managers and other highly-paid employees.

expanded accounting equation

See Explanation of Accounting Equation.

expected value

The sum of future amounts multiplied by their respective probabilities of occurrence.

expenditure

A payment. The expenditure might be for a significant long term asset (capital expenditure), a short term asset (prepaid insurance), a reduction in a liability, or for an immediate expense such as rent.

expenses

Costs that are matched with revenues on the income statement. For example, Cost of Goods Sold is an expense caused by Sales. Insurance Expense, Wages Expense, Advertising Expense, Interest Expense are expenses matched with the period of time in the heading of the income statement. Under the accrual basis of accounting, the matching is NOT based on the date that the expenses are paid.

Expenses associated with the main activity of the business are referred to as operating expenses. Expenses associated with a peripheral activity are nonoperating or other expenses. For example, a retailer's interest expense is a nonoperating expense. A bank's interest expense is an operating expense.

Generally, expenses are debited to a specific expense account and the normal balance of an expense account is a debit balance. When an expense account is debited, the account credited might be Cash (if cash was paid at the time of the expense), Accounts Payable (if cash will be paid after the expense is recorded), or Prepaid Expense (if cash was paid before the expense was recorded.) To learn more, see Explanation of Income Statement.

expenses and losses

A classification on a single-step income statement for both operating and nonoperating expenses and losses that pertain to the time interval shown in the heading of the income statement.

expenses by function

Classifying expenses according to the type of work such as selling, administration, general, and financing.

expired costs

Costs that have been used up or consumed. Expired costs are reported as expenses. (Costs that have not yet expired are reported as assets.)

exploding the bills of materials

Multiplying the individual items contained in each bill of material times the number of units expected to be produced during a specified time period. The result is the total quantity of each input that will be needed for the expected production.

extension or extend

In accounting this refers to the multiplication of *quantity* times *price*, or *number of units* times *price or cost per unit*.

external financial reporting

Financial statement and other financial information distributed to people outside of a company.

external reporting
See external financial reporting.

extinguishment of debt
To eliminate debt such as a company's repurchase or retirement of its outstanding bonds.

extraordinary repair
A major repair such as an engine overhaul, which will extend the useful life of the asset. The amount should be recorded in the asset account and then depreciated over the remaining life of the asset. This should not be confused with an extraordinary item.

Accounting Terms (F)

factoring accounts receivable
The sale of the accounts receivable (usually for a fee) to a third party known as a factor.

factory burden
Also referred to as manufacturing overhead, factory overhead, indirect manufacturing costs, or manufacturing support costs. To learn more, see Explanation of Manufacturing Overhead.

factory overhead
Also referred to as manufacturing overhead, indirect manufacturing costs, factory burden, and manufacturing support costs. To learn more, see Explanation of Manufacturing Overhead.

FAF
See Financial Accounting Foundation.

fair market value
The amount that would be agreed upon by two independent persons. The amount to be received in the ordinary course of business in an arm's length transaction.

FAS
Free Alongside Ship. Terms indicating that the seller's price includes delivery of goods at a ship's pier. Title to the goods will transfer to the buyer alongside the ship.

FASB
See Financial Accounting Standards Board.

FASB interpretation
An official pronouncement by the Financial Accounting Standards Board that involves a previously issued FASB Standard. FASB Interpretations are part of the generally accepted accounting principles.

FASB pronouncements

The statements, standards, interpretations and other financial reporting guidelines issued by the Financial Accounting Standards Board. The FASB pronouncements are available at www.FASB.org.

FASB Statement 116

The statement of the Financial Accounting Standards Board with the title *Accounting for Contributions Received and Contributions Made*. This statement was originally issued in June 1993 and applies to both nonprofit organizations and to for-profit businesses. This statement can be read at no cost at *www.FASB.org*.

FASB Statement 117

The statement of the Financial Accounting Standards Board entitled *Financial Statements of Not-for-Profit Organizations*. This statement was originally issued in June 1993 and can be read at no cost at *www.FASB.org*.

FASB statements of financial accounting concepts

This series of output by the Financial Accounting Standards Board is part of the board's conceptual framework project. The original goal in the 1970's was to articulate the definitions, practices, and rules that were used in accounting. It was hoped that from this structured compilation new rules will flow more easily and logically. However, this series of statements is not viewed as part of the generally accepted accounting principles.

Seven concepts statements have been issued and can be read at www.fasb.org under the tab entitled Standards.

FASB statements of financial accounting standards

These are the official rules that have been released by the Financial Accounting Standards Board. These are part of the generally accepted accounting principles. Before a standard is released, the public had been able to review a discussion memorandum and an exposure draft and to make comments. To read these accounting pronouncements, go to www.fasb.org and select the Standards tab at the top of the page.

favorable variance

A difference between an actual cost and a budgeted or standard cost, and the actual cost is the lesser amount. In the case of revenues, a favorable variance occurs when the actual revenues are greater than the budgeted or standard revenues.

federal income tax withholdings payable

This current liability account reports the amount a company owes the U.S. government as of the balance sheet date for the federal income taxes withheld from its employees' salaries and wages.

Federal Insurance Contributions Act (FICA)

A reference used to indicate the combination of the Social Security tax and the Medicare tax. For the year 2024, the *employee's portion* of the FICA tax is 7.65% (the Social Security tax of 6.2% plus the Medicare tax of 1.45%) on the first $168,600 of an employee's salary and wages. On an employee's salary and/or wages in excess of $168,600 the employee's portion of the FICA tax is 1.45% (consisting of only the Medicare tax). In addition, certain employees will be subject to a 0.9% Medicare surtax. The surtax will apply to wages, salaries, and a self-employed person's net income that are in excess of specified amounts. See IRS.gov for details on the Medicare surtax.

In the year 2024, the *employer's portion* of the FICA tax is 7.65% (the Social Security tax of 6.2% plus the Medicare tax of 1.45%) on each employee's first $168,600 of salary and wages. On each employee's salary and wages in excess of $168,600 the employer's portion is the Medicare tax of 1.45%. Therefore, the *combined employee and employer FICA tax* for 2024 is 15.3% (7.65% + 7.65%) on each employee's first $168,600 of salary and wages and then 2.9% (1.45% + 1.45%) on each employee's salary and wages in excess of $168,600.

To learn more, see Explanation of Payroll Accounting.

federal unemployment tax

A payroll tax paid solely by the employer and usually calculated as 0.6% times each employee's first $7,000 of annual wages or salaries. (The tax rate is 6.0% but a credit of up to 5.4% is usually given for contributions to a state unemployment fund.)

fees earned

An income statement account that reports the amount of service revenues earned during the time interval indicated in the heading of the income statement. (Under the accrual basis of accounting, fees earned are reported in the time period in which they are earned and not in the period in which the company receives payment.)

FEI

Financial Executives Institute.

FG Inventory

See inventory: finished goods.

FICA

See Federal Insurance Contributions Act (FICA).

FICA expense: delivery

Under the accrual method of accounting, this account reports the employer's portion of the Social Security and Medicare tax that pertains to the period indicated in the heading of the income statement, whether or not the company has paid/remitted the FICA taxes within this time period. Since this account involves the delivery function of the business, the expense should be reported in the operating expense section of the company's income statement.

FICA expense: selling & admin

Under the accrual method of accounting, this account reports the employer's portion of the Social Security and Medicare tax that pertains to the period indicated in the heading of the income statement, whether or not the company has paid/remitted the FICA taxes within this time period. Since this account involves the selling and administrative functions of the business, the expense should be reported in the operating expense section of the company's income statement.

FICA expense: warehouse

Under the accrual method of accounting, this account reports the employer's portion of the Social Security and Medicare tax that pertains to the period indicated in the heading of the income statement, whether or not the company has paid/remitted the FICA taxes within this time period. Since this account involves the warehouse functions of the business, the expense should be reported in the same section of the company's income statement as the warehouse salaries and wages are reported.

FICA tax payable

This current liability account reports the amount a company owes (must remit) for its employees' Social Security and Medicare taxes as of the date of the balance sheet.

FIFO

See first in, first out (FIFO).

FIFO cost flow assumption

See first in, first out (FIFO).

financial accounting

Refers to the accounting associated with the preparation of the main financial statements: income statement, balance sheet, statement of cash flows, statement of retained earnings, statement of stockholders' equity.

Financial Accounting Foundation (FAF)

This organization oversees the Financial Accounting Standards Board (FASB). It selects the members of the FASB and raises funds to assist in paying for its operations.

Financial Accounting Standards Board (FASB)

A nongovernment group of seven members assisted by a large research staff which is responsible for the setting of accounting standards, rules, and principles. Go to www.fasb.org for more information.

financial leverage

Using debt (such as loans and bonds) to acquire more assets than would be possible by using only owners' funds. Also referred to as trading on equity.

financial ratios

See the Explanation, Quiz, Q&A, and Puzzles for the topic Financial Ratios.

financial reporting

Includes the main financial statements (income statement, balance sheet, statement of cash flows, statement of retained earnings, statement of stockholders' equity) plus other financial information such as annual reports, press releases, etc.

financial statement analysis

Analyzing financial statements by using financial ratios, horizontal analysis, and vertical analysis. To learn more, see Explanation of Financial Ratios.

financial statements

Usually financial statements refer to the balance sheet, income statement, statement of cash flows, statement of retained earnings, and statement of stockholders' equity.

The balance sheet reports information as of a date (a point in time). The income statement, statement of cash flows, statement of retained earnings, and the statement of stockholders' equity report information for a period of time (or time interval) such as a year, quarter, or month.

To learn more, see Explanation of Balance Sheet.

To learn more, see Explanation of Income Statement.

To learn more, see Explanation of Cash Flow Statement.

financial statements of nonprofits

The financial statements of nonprofits include the statement of financial position, the statement of activities, the statement of cash flows, notes to the financial statements, and the statement of functional expenses. To learn more, see our Explanation of Nonprofit Accounting.

financing activities

The third section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

finished goods inventory

See inventory: finished goods (FG).

first in, first out (FIFO)

A cost flow assumption where the first (oldest) costs are assumed to flow out first. This means the latest (recent) costs remain on hand. To learn more, see Explanation of Inventory and Cost of Goods Sold.

first in, still here (FISH)
A parody of FIFO used to describe a very slow-moving item in inventory.

fiscal year
An accounting year that ends on a date other than December 31. For example, a school district might have a fiscal year of July 1, 2023 through June 30, 2024. A retailer might have a fiscal year consisting of the 52 or 53 weeks ending on the Saturday nearest to the first day of February.

FISH
See first in, still here (FISH).

501(c)(3)
The section of the U.S. Internal Revenue Service (IRS) code which includes public charities such as religious, scientific, educational, and certain other organizations. Under section 501(c)(3) a nonprofit can be approved as tax exempt and its donors' contributions will qualify as income tax deductible.

fixed assets
A term used when referring to property, plant, and equipment. Fixed assets other than land are depreciated.

fixed costs
See fixed expenses.

fixed expenses
Expenses which do not change in response to reasonable changes in sales or other activity.

fixed manufacturing overhead applied
The fixed manufacturing costs (e.g., property tax, rent, and depreciation on factory) that have been assigned to (absorbed by) the products manufactured via a predetermined rate. Ideally, by the end of the accounting year the amount applied will equal the amount actually incurred.

fixed manufacturing overhead budget variance
A variance arising in a standard costing system that indicates the difference between the actual amount of fixed manufacturing overhead incurred and the budgeted amount of fixed manufacturing overhead. To learn more, see Explanation of Standard Costing.

fixed manufacturing overhead incurred
The actual cost incurred for manufacturing costs that does not change as production volume changes. Examples include the property tax, rent, and depreciation of the factory building and equipment, and the salaries of the manufacturing management.

fixed manufacturing overhead volume variance
A variance arising in a standard costing system that indicates the difference between the standard amount of fixed manufacturing overhead for the good units produced (standard hours times standard rate) and the budgeted amount of fixed manufacturing overhead. To learn more, see Explanation of Standard Costing.

fixed overhead budget variance
Also referred to as the fixed overhead spending variance. The difference between the actual fixed overhead incurred and the amount of fixed overhead that had been budgeted.

fixed overhead spending variance
Also referred to as the fixed overhead budget variance. The difference between the actual fixed overhead incurred and the amount of fixed overhead that had been budgeted.

fixed rate loan
A loan in which the interest rate does not change over the life of the loan.

flexible budget
A budget that flexes with volume. Under a flexible budget the budgeted amount of manufacturing overhead will increase if the company produces more units than planned. The flexible budget will decrease if the company actually produces fewer units than planned.

float
The time between when a check is written and when the check clears the bank account on which it is drawn.

flow-through contributions
See pass-through contributions.

FOB
Free on Board. See FOB destination and FOB shipping point.

FOB destination
Terms indicating that the seller will incur the delivery expense to get the goods to the destination. With terms of FOB destination the title to the goods usually passes from the seller to the buyer at the destination. This means that goods in transit should be reported as inventory by the seller, since technically the sale does not occur until the goods reach the destination.

FOB shipping point
Terms indicating that the buyer must pay to get the goods delivered. (The buyer will record freight-in and the seller will not have any delivery expense.) With terms of FOB shipping point the title to the goods usually passes to the buyer at the shipping point. This means that goods in transit should be reported as a purchase and as inventory by the buyer. The seller should report a sale and an increase in accounts receivable.

foot

A word that means to add a column of numbers as in “Foot the amounts listed in column A.” Also see crossfoot.

footnotes

See notes to financial statements.

for-profit organization

A sole proprietorship, partnership, or corporation organized for the purpose of earning profits and enhancing the financial position of the owners.

Form 990

Form 990 is the Internal Revenue Service (IRS) form entitled *Return of Organization Exempt from Income Tax*. This federal form must be filed annually by tax exempt organizations. However, some organizations such as churches are exempt from filing, and small organizations are allowed to file Form 990-EZ. The information provided on Form 990 is public information and is available from the website *guidestar.org*. You can learn more about Form 990 and Form 990-EZ at *IRS.gov*.

Form 10-K

The annual report to the Securities and Exchange Commission (SEC), a U.S. government agency. The Form 10-K must be filed by corporations whose stock is publicly-traded on a U.S. stock exchange. The report contains the corporation’s financial statements (including footnotes) and a significant amount of other financial and nonfinancial information.

401(k) expense: delivery

Under the accrual method of accounting, this account reports the employer’s expense for the company’s 401(k) plan associated with the employees in the delivery department during the period indicated in the heading to the income statement. This expense should be reported in the operating expense section of the company’s income statement.

401(k) expense: selling & admin

Under the accrual method of accounting, this account reports the employer’s expense for the company’s 401(k) plan associated with the employees in the selling and administrative departments during the period indicated in the heading to the income statement. This expense should be reported in the operating expense section of the company’s income statement.

401(k) expense: warehouse

Under the accrual method of accounting, this account reports the employer’s expense for the company’s 401(k) plan associated with the employees in the warehouse department during the period indicated in the heading to the income statement. This expense should be reported in the operating expense section of the company’s income statement.

401(k) payable

This current liability account reports the amount a company owes (is required to remit) for its employees’ 401(k) program as of the date of the balance sheet.

free cash flow

The cash flow from operating activities minus the amount of capital expenditures. Other variations are also used. To learn more, see Explanation of Cash Flow Statement.

free cash flow per share

The amount of free cash flow divided by the weighted average number of common shares of stock outstanding during the year.

free on board (FOB)

See FOB destination and FOB shipping point.

freight-in

The shipping cost to be paid by the buyer of merchandise purchased when the terms are *FOB shipping point*. Freight-in is considered to be part of the cost of the merchandise and should be included in inventory if the merchandise has not been sold.

freight-out

Delivery expense to be paid by the seller when its merchandise is sold with terms of *FOB destination*. This is an operating expense and is not included in the cost of merchandise.

fringe benefit rate

A percentage of an hourly wage rate (or salary) that represents the employer's additional costs of employee benefits such as paid vacation days, paid sick days, insurance (health, dental, life, worker compensation), retirement plans, federal and state employer payroll taxes (Social Security, Medicare, unemployment insurance), cafeteria, daycare, etc.

fringe benefits

Compensation for employees that is in addition to salaries and wages. Examples include paid absences (vacation, sick, holiday), insurances (health, dental, vision, life), pensions, profit sharing contributions, employer matching of Social Security and Medicare taxes, unemployment taxes, worker compensation insurance, continuing education costs, etc. Generally, the cost of fringe benefits should be expensed when they are earned by the employee, not in the period in which they are paid.

full costing

See absorption costing.

full disclosure principle

An accounting guideline that requires information pertinent to an investing or lending decision to be included in the notes to financial statements or in other financial reports.

fully depreciated

An asset having accumulated depreciation equal to its depreciable cost (cost minus estimated salvage value). The use of an asset after it is fully depreciated will mean no depreciation expense for those accounting periods.

functional and natural matrix

The description of the required reporting of expenses by some nonprofits. The expenses will be presented on lines based on the nature of the expense (salaries, fringe benefits, rent, utilities, postage, professional fees) and in columns based on the function (Program #1, Program #2, Management and General, Fundraising). The matrix format is encouraged for all nonprofits but it is required only for voluntary, health and welfare organizations. See the statement of functional expenses.

functional basis

See functional expense classification.

functional expense classification

Sorting and reporting expenses according to the type of activity for which the expense was incurred. The functional expense classifications for a nonprofit organization would be Program #1, Program #2, Management and General, Fundraising.

Businesses have functions such as manufacturing, selling, and general and administrative.

(Sorting and reporting expenses by the type of expense such as salaries, rent, utilities, etc. is known as natural expense classifications.)

fundraising expenses

A subgroup of a nonprofit's supporting activities expenses. This functional expense classification is used for the fundraising activities including fundraising campaigns, mailings for funds from supporters, and other solicitations for contributions. It may also include an allocated portion of the executive director's salary and benefits plus other management and general expenses.

funds flow statement

A financial statement that reported the changes in a company's working capital. The funds flow statement has been replaced by the statement of cash flows.

furniture and fixtures

Long-term assets that are reported under the classification of property, plant, and equipment on a company's balance sheet. These assets are depreciated over their useful life.

FUTA

Federal Unemployment Tax Act. See federal unemployment tax.

future value of 1 table

A table of factors that shows what the future value of $1 will grow to if invested at the rate shown in the column heading and compounded for the number of periods indicated in the row.

future value of an annuity due

The amount that a recurring equal amount deposited at the *beginning* of each period will grow to under compounded interest. An *annuity due* is also known as an *annuity in advance*.

future value of an ordinary annuity

The amount that a recurring equal amount deposited at the *end* of each period will grow to under compounded interest. An *ordinary annuity* is also known as an *annuity in arrears*.

Accounting Terms (G)

GAAP

See generally accepted accounting principles (GAAP).

gain contingency

See contingent gain.

gain on retirement of bonds

The result of a corporation buying back its own bonds for an amount that is less than the carrying value of the bonds. The amount of the gain is computed by subtracting the amount spent to repurchase the bonds from the bonds' carrying value. The carrying value is usually the face amount of the bonds being retired *plus* the unamortized premium associated with the bonds being retired (or minus the bonds' unamortized discount) *minus* the bonds' unamortized issue costs.

gain on sale of assets

This is a non-operating or "other" item resulting from the sale of an asset (other than inventory) for more than the amount shown in the company's accounting records. The gain is the difference between the proceeds from the sale and the carrying amount shown on the company's books.

gain on sale of automobile

The amount by which the proceeds from the sale of an automobile used in the business exceeded its carrying amount at the time it is sold.

gain on sale of equipment

The amount by which the proceeds from the sale of equipment (that had been used in the business) exceeded its carrying amount at the time it is sold.

gain on sale of investments

The amount by which the proceeds from the sale of investments exceeded the carrying amount of the investments that were sold. It is reported as a non-operating or "other" item on a multiple-step income statement.

gain on sale of land

The amount by which the proceeds from the sale of land exceeded the carrying amount of the land sold. It is reported as a non-operating or "other" item on a multiple-step income statement.

gain on sale of truck

A non-operating item that results from the sale of a long-term asset at an amount greater than the carrying amount (book value) of the truck at the time it is sold.

gain or loss on the sale of a long-term asset

A non-operating item that results from the sale of a long-term asset for more (gain) or less (loss) than its carrying amount or book value.

gains

Gains result from the sale of an asset (other than inventory). A gain is measured by the proceeds from the sale minus the amount shown on the company's books. Since the gain is outside of the main activity of a business, it is reported as a nonoperating or other revenue on the company's income statement. To learn more, see Explanation of Income Statement.

garnishment

In payroll processing, the withholding of money from an employee's wages or salary as ordered by a court. The money is then remitted by the employer to the agency specified by the court. To learn more, see Explanation of Payroll Accounting.

garnishment payable

This current liability account reports the amount a company must remit to a court or other agencies for amounts withheld from its employees' salaries and wages.

general journal

A book of original entry that requires that both the account being debited and the account being credited be listed along with the respective amounts. Because of accounting software and special journals there are relatively few entries made into the general journal.

general journal entry

The journal entry recorded in the general journal (as opposed to the sales journal, cash journal, etc.).

general ledger

That part of the accounting system which contains the balance sheet and income statement accounts used for recording transactions.

general ledger account

An account in the general ledger, such as Cash, Accounts Payable, Sales, Advertising Expense, etc. To learn more, see Explanation of Chart of Accounts.

generally accepted accounting principles (GAAP)

The general guidelines and principles, standards and detailed rules, plus industry practices that exist for financial reporting. Often referred to by its acronym GAAP. To learn more see Explanation of Accounting Principles.

going concern assumption

An accounting guideline which allows the readers of financial statements to assume that the company will continue on long enough to carry out its objectives and commitments. In other words, the accountants believe that the company will not liquidate in the near future. This assumption also provides some justification for accountants to follow the cost principle.

good output

A phrase used in standard costing. The production that is acceptable (not rejected products) and which is assigned manufacturing costs of direct materials, direct labor, and manufacturing overhead.

goods in transit

Merchandise that has been shipped by a supplier but the merchandise has not yet reached the customer's location. Goods in transit that were shipped FOB Shipping Point should be included in the customer's purchases and inventory. Goods in transit that were shipped FOB Destination should be reported in the supplier's inventory.

goodwill

Goodwill is a long-term (or noncurrent) asset categorized as an intangible asset. Goodwill arises when a company acquires another entire business. The amount of goodwill is the cost to purchase the business minus the fair market value of the tangible assets, the intangible assets that can be identified, and the liabilities obtained in the purchase.

The amount in the Goodwill account will be adjusted to a smaller amount if there is an impairment in the value of the acquired company as of a balance sheet date. (Private companies may opt to amortize goodwill generally over a 10-year period and thereby minimize the cost and complexity involved with testing for impairment.)

gross

The amount before deductions. For example, gross pay is the amount before withholding deductions. Gross sales is the amount before sales returns and allowances and sales discounts.

gross margin

A term that is sometimes used interchangeably with gross profit. Others use the term to mean the percentage of gross profit dollars divided by net sales dollars.

gross profit

Net sales revenues minus the cost of goods sold.

gross profit method of estimating inventory

To learn more, see Explanation of Inventory and Cost of Goods Sold.

gross profit percentage

Dollars of gross profit divided by the dollars of net sales. Also known as gross margin.

gross profit ratio
See gross profit percentage.

gross salaries
An employee's pretax compensation that is based on annual or monthly amounts rather than an hourly rate. Management employees are usually paid salaries. To learn more, see Explanation of Payroll Accounting.

gross sales
Sales before deducting sales returns, sales allowances, and sales discounts.

gross wages
An employee's pretax compensation based on hours worked times an hourly rate of pay. Production workers and nonmanagement employees are usually paid wages. To learn more, see Explanation of Payroll Accounting.

Accounting Terms (H)

health insurance expense: delivery
Under the accrual method of accounting, this account reports the employer's portion of the health insurance cost incurred by the company during the period indicated in the heading of the income statement, whether or not the company has paid/remitted the insurance premiums within this time period. Since this account involves the delivery function of the business, the health insurance expense should be reported in the operating expense section of the company's income statement.

health insurance expense: selling & admin
Under the accrual method of accounting, this account reports the health insurance expense that the company has incurred for the employees in the selling and administrative departments of the company during the period indicated in the heading of the income statement.

health insurance expense: warehouse
Under the accrual method of accounting, this account reports the employer's portion of the health insurance cost incurred by the company during the period indicated in the heading of the income statement, whether or not the company has paid/remitted the insurance premiums within this time period. Since this account involves the warehouse function of the business, the health insurance expense should be reported in the same section of the company's income statement as the warehouse salaries and wages are reported.

held-to-maturity securities

Bonds and other debt securities that a company intends to hold until the securities mature. In addition to intent, the company must have the financial ability to be able to hold them until they mature.

high-low method

A technique used to determine the variable rate (slope of a total cost line) of an independent variable and the fixed amount by using just two points: the highest point and the lowest point. For example, if at the highest volume of processing items there were 10,000 items processed at a total cost of $35,000 and at the lowest volume there were 6,000 items processed at a total cost of $27,000, the high-low method indicates the variable rate was $2 per unit. ($35,000 – $27,000) divided by (10,000 – 6,000). The fixed amount will be $15,000 [$27,000 – $2(6,000)].

historical cost

The original cost incurred to acquire an asset (as opposed to replacement cost, current cost, or cost adjusted by a general price index). If a company purchased land in 1980 for $10,000 and continues to hold that land, the company's balance sheet in the year 2024 will report the land at $10,000 (even if the land is now worth $400,000).

holding costs

In the EOQ model, the holding costs are the incremental costs of storing or holding an item in inventory for one year.

holding gain

A gain that occurs by holding an asset. For example, if a company bought land for $20,000 many years ago and today the company continues to hold the land and its value is now $175,000, the company has a holding gain of $155,000. However, the company cannot record the holding gain on its financial statements because of the cost principle and the revenue recognition principle. On the other hand, if the company sells the land for $175,000 a holding gain of $155,000 will appear on its income statement as the company also records the $175,000 on its balance sheet and removes the land's original cost of $20,000.

holding loss

A loss that occurs by holding an asset. Holding losses might be recorded on the income statement or they might not be recorded depending on the asset and the amounts.

holiday, vacation, sick days expense: delivery

Under the accrual method of accounting, this account reports the amount of holiday pay, vacation pay, and sick day pay that the delivery employees have *earned* during the accounting period indicated in the heading of the income statement. In effect, the company is accruing this expense when the employees are working—by debiting this account and crediting a liability account, such as Holiday, Vacation, Sick Days Payable. When employees take time off with pay for holidays, vacation or sick days, the liability account is debited.

Since this account involves the delivery function of the business, this expense should be reported in the same section of the company's income statement as the delivery salaries and wages are reported.

holiday, vacation, sick days expense: warehouse

Under the accrual method of accounting, this account reports the amount of holiday pay, vacation pay, and sick day pay that the warehouse employees have *earned* during the accounting period indicated in the heading of the income statement. In effect, the company is accruing this expense when the employees are working—by debiting this account and crediting a liability account, such as Holiday, Vacation, Sick Days Payable. When employees take time off with pay for holidays, vacation or sick days, the liability account is debited.

Since this account involves the warehouse function of the business, this expense should be reported in the same section of the company's income statement as the warehouse salaries and wages are reported.

holiday, vacation, sick days payable

This current liability account reports the amount a company's employees have earned in holiday pay, vacation pay, and sick days but have not yet taken as of the date of the balance sheet.

horizontal analysis

One component of financial statement analysis. This method involves financial statements reporting amounts for several years. The earliest year presented is designated as the base year and the subsequent years are expressed as a percentage of the base year amounts. This allows the analyst to more easily see the trend as all amounts are now a percentage of the base year amounts.

hurdle rate

A target rate. For example, companies may decide to invest only in projects that generate an internal rate of return that is in excess of 12%. The 12% figure becomes the hurdle rate.

Accounting Terms (I)

IASB

See International Accounting Standards Board (IASB).

IFRS

See International Financial Reporting Standards (IFRS).

illusory profits

See phantom profits.

IMA

The acronym for Institute of Management Accountants, an international organization dedicated to enhancing management accounting and financial management. It offers various programs and networking opportunities. IMA also awards the Certified Management Accountant designation to members who have successfully passed its CMA Exam and have met its experience requirements. Learn more about IMA.

impairment

A decrease in the value of a long term asset to an amount that is less than the amount shown under the cost principle.

impairment of long-lived assets

See Statement of Financial Accounting Standard No. 121. Under this standard if the undiscounted future cash flows from the asset (including sale amount) are less than its carrying amount, a loss is recognized. The amount of the impairment loss is measured by subtracting the asset's fair value from its carrying value.

implicit interest rate

An interest rate that is not explicitly stated. For example, instead of paying $100 cash a person is allowed to pay $9 per month for 12 months. The interest rate is not stated, but the implicit rate can be determined by use of present value factors.

imprest amount

A constant or unchanging amount that is often used when referring to petty cash. For example, if the petty cash account in the general ledger has an imprest balance of $100, the account balance will be a constant $100. The journal entry to replenish an imprest petty cash fund involves debiting each of the expenses involved and crediting cash (not Petty Cash) for the amount necessary to get the actual cash on hand equal to the imprest amount. Any difference in these amounts is entered into the account Cash Short and Over.

imputed interest

An interest rate that is not explicit. For example, if a business lends its majority owner $100,000 at 0% interest, the IRS might determine that a fair interest rate would be 6% and not 0%. The IRS will impute interest of 6%.

in-kind

Goods or services provided instead of money.

in-process inventory

See inventory: work-in-process (WIP).

income

This term is used in several ways. Some use the word interchangeably with revenues. Others use the word to signify a net amount, such as income from operations (revenues minus expenses in the company's main operating activities). Still others use it when referring to nonoperating revenues, such as interest income.

income from operations

The result of subtracting operating expenses from gross profit. Income from operations is the amount before non-operating items (such as gains and losses on the sale of assets, interest revenue, and interest expense).

income statement

One of the main financial statements (along with the balance sheet, the statement of cash flows, and the statement of stockholders' equity). The income statement is also referred to as the profit and loss statement, P&L, statement of income, and the statement of operations. The income statement reports the revenues, gains, expenses, losses, net income and other totals for the period of time shown in the heading of the statement. If a company's stock is publicly traded, earnings per share must appear on the face of the income statement. To learn more, see Explanation of Income Statement.

income statement account

A revenue, expense, gain, or loss account.

income summary account

A temporary account to which the income statement accounts are closed. This account is then closed to the owner's capital account or a corporation's retained earnings account. This and other summary accounts can be thought of as a clearing account.

income tax code

The United States Internal Revenue Code which contains the federal laws and regulations pertaining to federal taxes.

income tax depreciation

The depreciation computed on the tax return according to the income tax code and regulations. This amount is usually different from the depreciation used on the financial statements (book depreciation).

income tax expense

The amount of income tax that is associated with (matches) the net income reported on the company's income statement. This amount will likely be different than the income taxes actually payable, since some of the revenues and expenses reported on the tax return will be different from the amounts on the income statement. For example, a corporation is likely to use straight-line depreciation on its income statement, but will use accelerated depreciation on its income tax return.

income taxes payable

A current liability account which reflects the amount of income taxes currently due to the federal, state, and local governments.

incremental cost

The additional cost of an additional quantity. It is similar to marginal cost, except that marginal cost refers to the cost of the next unit. Incremental cost might be the additional cost from the next 200 units.

incremental income tax rate

The combined federal and state income tax rate that applies to an additional amount of taxable income.

incremental revenue

The additional revenues from an additional quantity. It is similar to marginal revenue, except that marginal revenue refers to the revenue from the next unit. Incremental revenue might be the additional revenues from the next 200 units.

incurred

A word used by accountants to communicate that an expense has occurred and needs to be recognized on the income statement even though no payment was made. The second part of the necessary entry will be a credit to a liability account.

indenture

A document that discloses important information on bonds or preferred stock. Included in the indenture would be the call price, the actions that can occur if the company fails to pay the interest or dividend, etc.

independent contractor

Someone who performs a task for a company, but is not an employee. The IRS has criteria to assist in distinguishing between an independent contractor and an employee.

independent variable

A driver of a change in the amount of a dependent variable. The independent variable is usually represented by “x”, the dependent variable by “y”, the rate of change by “b”, and the fixed amount by “a” as in y = a + bx. For example, a salesperson’s weekly compensation consisting of $250 plus 5% of sales will be y = $250 + .05x.

indirect cost

A cost or expense that is not directly traceable to a department, product, activity, customer, etc. As a result indirect costs and expenses are often allocated to the department, product, etc. For example, a manufacturing department that molds plastic has some costs that are directly traceable to it, such as the wages and fringe benefits of the direct labor working exclusively in that department. However, the heat for the entire building appears only on one utility bill. The heating bill is an indirect cost to the molding department. Generally it will be assigned to all departments based on the number of square feet each department occupies.

indirect factory cost

See indirect manufacturing costs.

indirect labor

Usually this refers to manufacturing employees who are not classified as direct labor. Material handlers, mechanics, setup workers, clean up workers are a few examples of indirect labor.

indirect manufacturing costs

Also referred to as manufacturing overhead, factory burden, factory overhead, and manufacturing support costs. To learn more, see Explanation of Manufacturing Overhead.

indirect materials

For a manufacturer these would include factory supplies and other materials considered to be manufacturing overhead.

indirect method of SCF

The most common method of preparing the statement of cash flows. Under this method the starting point is the net income reported on the income statement. To learn more, see Explanation of Cash Flow Statement.

industry practices

Industries that are regulated by the government often have prescribed reporting requirements that carry over to the generally accepted reporting formats for financial reporting. For example, utilities’ balance sheets present the utility plant as the first asset instead of current assets. Insurance and securities firms will have financial reports that differ from the formats used by manufacturers.

inelastic demand

The situation where the number of units sold is not influenced by a change in selling price. In other words, a price increase does not have a corresponding decrease in the number of units sold.

information

Relevant or meaningful data.

insolvent

The inability to pay liabilities as they become due. Some consider a company to be insolvent when its current liabilities exceed its current assets.

Institute of Management Accountants

See IMA.

insurance

A contract to provide coverage or protection in exchange for a payment or “premium.” Examples of insurance protection include liability, property, business interruption, life, disability, etc. The company paying the premiums for the protection will have insurance expense and possibly an asset, Prepaid Insurance (if the premiums are paid in advance). The insurance company would have insurance premium revenues and possibly a liability, Unearned Insurance Premiums (if the premiums were paid in advance).

insurance expense

The amount of insurance that was incurred/used up/expired during the period of time appearing in the heading of the income statement. The amount of insurance premiums that have not yet expired should be reported in the current asset account Prepaid Insurance.

intangible assets

Some examples of intangible assets include copyrights, patents, goodwill, trade names, trademarks, mail lists, etc. These assets will be reported at cost (or lower) on the balance sheet after property, plant and equipment. Trade names and trademarks that were developed by a company (as opposed to buying them from another company at a significant cost) may not appear on the balance sheet, even though they might be a company’s most valuable asset.

interest earned

An amount earned by a company on its interest bearing bank accounts or other investments. The amount should be reported as Interest Revenues, Interest Income, or Investment Revenues in the accounting period in which the interest is earned.

interest expense

This account is a non-operating or “other” expense for the cost of borrowed money or other credit. The amount of interest expense appearing on the income statement is the cost of the money that was *used* during the time interval shown in the heading of the income statement, **not** the amount of interest *paid* during that period of time.

interest income

See interest revenues.

interest payable

This current liability account reports the amount of interest the company owes as of the date of the balance sheet. (Future interest is not recorded as a liability.)

interest receivable

The current asset that represents the amount of interest revenue that was reported as earned, but has not yet been received.

interest revenues

Under the accrual basis of accounting, the Interest Revenues account reports the interest earned by a company during the time period indicated in the heading of the income statement. Interest Revenues account includes interest earned whether or not the interest was received or billed. Interest Revenues are nonoperating revenues or income for companies not in the business of lending money. For companies in the business of lending money, Interest Revenues are reported in the operating section of the multiple-step income statement.

interim financial statement

Financial statements issued between the official annual financial statements. For example, quarterly financial statements are interim financial statements.

internal rate of return

The rate that will discount all cash flows to a net present value of zero.

Internal Revenue Service (IRS)

The U.S. government agency responsible for federal income tax regulations.

International Accounting Standards Board (IASB)

The independent organization based in the UK which develops the International Financial Reporting Standards (IFRS). The IASB has been working with the Financial Accounting Standards Board (FASB), which is based in the U.S., to “converge” each organization’s reporting standards. The goal is to ultimately have a single set of global accounting standards.

International Financial Reporting Standards (IFRS)

The accounting and reporting standards developed by the International Accounting Standards Board (IASB). IFRS are used by business entities in most countries. The most notable exception is the U.S. where business entities follow U.S. GAAP, which is the generally accepted accounting standards promulgated by the Financial Accounting Standards Board. There is a goal to move toward the IFRS as the global standard; however, the transition is proving to be difficult.

interperiod tax allocation

Income tax allocations arising from differences between income tax rules and generally accepted accounting rules. For example, depreciation for income tax purposes is based on the income tax code and may require that equipment be depreciated on the income tax return over a 7-year period. However, accounting principles require that for financial statements the equipment be depreciated over its useful life. The useful life might be more than 7 years or it might be less than 7 years. These “timing” differences lead to interperiod tax allocation.

interpretations

See FASB Interpretation.

intraperiod tax allocations

The allocation of one year’s income tax expense to the various sections of the income statement. For example, extraordinary items must be reported after income tax on the income statement, while operating revenues are reported before income tax.

inventoriable cost

Cost that is considered to be part of the cost of merchandise. For a retailer, the inventoriable cost is the cost from the supplier plus all costs necessary to get the item into inventory and ready for sale, e.g. freight-in. For a manufacturer the product costs include direct material, direct labor, and the manufacturing overhead (fixed and variable).

inventory

A current asset whose ending balance should report the **cost** of a merchandiser’s products awaiting to be sold. The inventory of a manufacturer should report the **cost** of its raw materials, work-in-process, and finished goods. The cost of inventory should include all costs necessary to acquire the items and to get them ready for sale.

When inventory items are acquired or produced at varying costs, the company will need to make an assumption on how to flow the changing costs. See cost flow assumption.

If the net realizable value of the inventory is less than the actual cost of the inventory, it is often necessary to reduce the inventory amount.

To learn more, see Explanation of Inventory and Cost of Goods Sold.

inventory carrying costs

The cost to hold an item in inventory. Includes the cost of capital tied up in inventory, the cost of space and insurance, and the cost of items becoming obsolete while being held in inventory. This is an important component of the economic order quantity model.

inventory conformity rule

Generally, this rule requires that the cost flow assumption used for tax purposes be the same cost flow assumption used for the financial statements. Consult a tax professional about this and other tax matters.

inventory cost flow assumption

The method used for removing costs from the inventory of goods. The *cost flow* can be different from the *physical flow* of goods. For example, in the U.S. the LIFO cost flow can be used even if the oldest goods are shipped to the buyer.

inventory extension

The multiplication of a quantity times its cost. For example, if 100 items are in inventory at a cost of $3.46 each, the inventory extension is $346.

inventory: FG

See inventory: finished goods (FG).

inventory: finished goods (FG)

The products in a manufacturer’s inventory that are completed and are awaiting to be sold. You might view this account as containing the cost of the products in the finished goods warehouse. A manufacturer must disclose in its financial statements the amount of finished goods, work-in-process, and raw materials.

inventory holding costs

See inventory carrying costs.

inventory: materials

A part of a manufacturer’s inventory that includes direct and indirect materials. Also referred to as stores.

inventory shrinkage

Inventory that is less than the expected amount. It might be associated with theft or damage.

inventory turnover ratio

This ratio relates the costs in inventory to the cost of the goods sold. To learn more about this ratio, see Explanation of Financial Ratios.

inventory valuation

The dollar amount associated with the goods in a company’s inventory. Initially the cost per unit is the cost to get the inventory items in place and ready for use. However, under certain circumstances the may have to be reduced to a lower amount.

Since inventory items are constantly being purchased and sold and since the cost of the items purchased often changes, a company must select a cost flow assumption.

The inventory valuation is critical because it also affects the cost of goods sold amount that is matched with sales on the income statement.

Learn more about Inventory and Cost of Goods Sold.

inventory: WIP

See inventory: work-in-process (WIP).

inventory: work-in-process (WIP)

That part of a manufacturer's inventory that is in the production process and has not yet been completed and transferred to the finished goods inventory. This account contains the cost of the direct material, direct labor, and factory overhead placed into the products on the factory floor. A manufacturer must disclose in its financial statements the cost of its work-in-process as well as the cost of finished goods and materials on hand.

investing activities

The second section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

investment centers

A decentralized division of a corporation which is responsible for and has control over its costs, revenues, and investments.

investment in another company

An asset account which reports the carrying amount of a company's investment in another enterprise.

investment revenues

The amounts earned on money invested. Often this is interest and dividends earned on a company's investment in stocks and bonds of other companies.

investment securities

An asset account in a bank's general ledger that indicates the amount at which the bank is reporting or carrying its investments.

investments

The long term asset category of a classified balance sheet which appears immediately after the current assets. Listed in this category would be a bond sinking fund, funds held for construction, the cash surrender value of a life insurance policy owned by the company, and long term investments in stocks and bonds.

invoice

A bill issued by a seller of merchandise or by the provider of services. The seller refers to the invoice as a sales invoice and the buyer refers to the same invoice as a vendor invoice.

IRR

See internal rate of return.

IRS

See Internal Revenue Service (IRS).

IRS Publication 15

A publication by the U.S. Internal Revenue Service (IRS) to assist employers with federal payroll taxes. The complete title of the publication is Publication 15 (Circular E), Employer's Tax Guide. It is available at www.irs.gov.

Accounting Terms (J)

J. Ott, Capital

This is an owner's equity account. The balance in this account reflects the owner's investment in this sole proprietorship plus the net income and minus the owner's draws since the company began. (The current year net income and draws may not yet be recorded in this account. The net income may still be in the temporary revenue and expense accounts and the draws may still be in J. Ott, Drawing, also a temporary account. The temporary accounts will be closed to J. Ott, Capital after the year's financial statements are prepared.)

J. Ott, Drawing

This is a contra owner's equity account, because it has a debit balance if draws were made. Even though it is a balance sheet account, it is a temporary account. At the end of each year the account's debit balance is closed to J. Ott, Capital.

JIT

See just-in-time (JIT).

job cost record

See job order cost sheet.

job costing

See job order costing.

job order cost sheet

This is a record on an individual job (product, batch) within the job costing system. For items in process this is a subsidiary record to the general ledger account inventory: work-in-process (WIP).

job order costing

The cost accounting system where costs are recorded by individual job (versus process costing system). The job order system can use standard costs or actual costs.

job order system

See job order costing.

joint cost

A common cost. Often refers to the costs prior to the point where several products emerge from a common process.

joint product

The products with significant value that emerge at a split-off point in a process. When a joint product has little value it is referred to as a byproduct.

journal

The record of journal entries appearing in order by date. Some refer to the journal as the book of original entry, since the entries are first recorded in a journal. From the journal the entries will be posted to the designated accounts in the general ledger. With manual systems there are likely to be a sales journal, purchases journal, cash receipts journal, cash disbursements journal, and the general journal. With computerized accounting systems, it is likely that the general journal will be used sparingly. The software is likely to record the other transactions automatically as invoices are entered, checks are prepared, receipts processed, etc.

journal entry

The entry made in a journal. It will contain the date, the account name and amount to be debited, and the account name and amount to be credited. Each journal entry must have the dollars of debits equal to the dollars of credits.

journalize

To record accounting entries into a journal.

just-in-time (JIT)

An effort to have materials delivered by suppliers just as the materials are needed, thereby eliminating the need for the buyer to store inventories of component parts. Obviously, the buyer is relying on the dependability of the supplier.

Accounting Terms (K)

k

A symbol that represents 1000.

kiting

This activity, which involves playing the float, is sometimes used when a company is facing an overdrawn checking account. Assume that a company has a checking account at NY Bank that is about to overdraw. To prevent the NY Bank checking account from overdrawing, the company deposits one of its checks drawn on its PA Bank. However, its PA Bank checking account does not have sufficient funds to cover the check that the company deposited in the NY Bank. To avoid its PA Bank checking account from overdrawing, the company deposits into its PA Bank checking account a check drawn on its NY Bank checking account. Of course there are not sufficient funds in the NY Bank account, so the company deposits into its NY Bank account a check drawn on its PA Bank account. This pattern will require the writing and depositing of many checks until the company gets some money or until the scheme is detected. Banks have reduced the opportunity for kiting by clearing checks more quickly and by not paying checks until deposited checks have been in an account for several days.

Accounting Terms (L)

labor efficiency variance

See direct labor efficiency variance.

labor rate variance

See direct labor rate variance.

labor variances

See direct labor efficiency variance and direct labor rate variance.

land

A long-term asset account that reports the cost of real property exclusive of the cost of any constructed assets on the property. Land usually appears as the first item under the balance sheet heading of Property, Plant and Equipment. Generally, land is not depreciated.

land improvements

A long-term asset which indicates the cost of the constructed improvements to land, such as driveways, walkways, lighting, and parking lots. Land Improvements will be depreciated over their useful life by debiting the income statement account Depreciation Expense and by crediting the balance sheet account Accumulated Depreciation: Land Improvements.

landlord

The owner of property that often receives rent from tenants.

last in, first out (LIFO)

A cost flow assumption where the last (recent) costs are assumed to flow out of the asset account first. This means the first (oldest) costs remain on hand. To learn more, see Explanation of Inventory and Cost of Goods Sold.

lawsuit payable

A liability account that reports the amount payable as of the balance sheet date. For the account to show a balance, a loss/obligation must be probable and the amount can be estimated. If the lawsuit is remote or only possible, it will not be shown as a liability. If the lawsuit is possible but not probable, it should be disclosed in the notes.

lead time

The time from when goods are ordered until the time when the goods are received.

learning curve

An expectation that as a task is repeated there will be significant time reductions during the early repetitions. The time savings will dissipate after continuous performance. This is important to consider when setting the direct labor standard cost.

lease

A legal agreement to pay rent to the lessor for a stated period of time. Sometimes the lease is in substance a purchase of an asset and a financing arrangement. For example, if a company agrees to lease a forklift truck for 60 months and the agreement cannot be canceled without purchasing the asset, it is possible the arrangement is more than a mere rental of equipment. See capital lease and operating lease.

leaseback

A company might construct a building and then sell the building to an investor who in turn leases the building back to the company.

leasehold improvements

Additions or changes to a rented building that are made by the tenant rather than by the landlord. The tenant will record the cost of these changes in the long term asset account Leasehold Improvements. The cost of these additions or changes should be depreciated over the remaining life of the lease.

least squares regression method

A mathematical technique that determines the best-fitting line through a series of points. This is used in regression analysis.

ledger

A “book” containing accounts. For example, there is the *general* ledger that contains the balance sheet and income statement accounts. There is a *subsidiary* ledger that contains the detailed, customer account balances for the general ledger account Accounts Receivable.

legal capital

The par value of common and preferred stock.

lend

To loan money for a limited time in exchange for the borrower's promise of repayment and interest compensation.

lender

Usually a bank, finance company, or person that makes a loan to another party, who is referred to as the borrower.

lessee

The person paying rent for using but not owning the asset.

lessor

The party owning an asset and receiving rent from another party (the lessee).

letter of credit

This is granted by banks only to very creditworthy customers. It states that the bank will guarantee amounts that its customer incurred when purchasing goods. A letter of credit might be necessary for a U.S. company wishing to purchase significant amounts of goods on a buying trip to the Pacific rim.

leverage

Using debt in order to control more assets. Also known as financial leverage.

liabilities

Obligations of a company or organization. Amounts owed to lenders and suppliers. Liabilities often have the word "payable" in the account title. Liabilities also include amounts received in advance for a future sale or for a future service to be performed. To learn more, see Explanation of Balance Sheet.

lien

Usually a claim on an asset that is pledged as collateral. The lien is usually filed with a government office.

LIFO

See last in, first out (LIFO).

LIFO conformity rule

A rule that requires that the same inventory cost flow be used on the financial statements as is used on the income tax return.

LIFO liquidation of layer

See liquidation of LIFO layer.

LIFO reserve

Usually the difference between the cost of inventory at LIFO versus the cost of inventory at FIFO.

limited liability company

A business organization different from a sole proprietorship, partnership, and corporation. As the name implies it provides the limited liability protection usually associated with a corporation. To learn more about this business structure, you should discuss this with a tax and legal professional.

line of credit

The amount that a bank commits to lend a borrower during a specified purpose.

linear programming

A mathematical tool to optimize profits (contribution margin) given a limited amount of inputs and other constraints.

liquidation of LIFO layer

The reduction in inventory quantities resulting in the removal of older layers of costs. With continuously higher costs, the older layers are likely to be low costs under LIFO. Removing these old, low costs will cause an increase in profits and in taxable income. Therefore, it is important to be intentionally removing the low costs since this is likely to create an income tax payment that could have been avoided by not liquidating the old costs. If the liquidation of LIFO layers results in a significant increase in net income, this should be disclosed.

liquidity

The ability to generate cash.

liquidity ratios

Financial ratios such as current ratio, quick ratio, receivables turnover ratio, and inventory turnover ratio. To learn more, see Explanation of Financial Ratios.

LLC

See limited liability company.

loan amortization schedule

A multicolumn listing of each payment required during the period of a loan. Each payment is detailed by the amount of interest, the principal payment, and the remaining unpaid principal balance. The interest portion of the payment is based on the unpaid principal balance after the previous payment. Usually the total payment remains constant and each period the interest portion of the payment decreases and the principal portion of the payment increases.

loans receivable

An asset account in a bank's general ledger that indicates the amounts owed by borrowers to the bank as of a given date.

lock-box system

Usually involves a company's customers remitting amounts to a bank account close to the customers in order for the company to have collected funds sooner. For example, a company with its headquarters in the Midwest, might have a bank account in New York for its east coast customers to mail in amounts owed. Similarly, the company may also have its west coast customers remit to a bank account in California. The company would have access to bank funds several days sooner with such an arrangement instead of all remittances being mailed to the Midwest.

long-lived assets

Long-term assets including property, plant, equipment and intangible assets. Buildings, furnishings, fixtures, office equipment, and vehicles are common examples of long-lived assets which are depreciated by nonprofit and by for-profit organizations.

long-term assets

Noncurrent assets. Assets that are not intended to be turned into cash or be consumed within one year of the balance sheet date. Long-term assets include long-term investments, property, plant, equipment, intangible assets, etc.

long-term investments

The balance sheet classification that is reported immediately after current assets and before property, plant, and equipment.

long-term liabilities

Obligations of the enterprise that are *not* payable within one year of the balance sheet date. Two examples are bonds payable and long term notes payable.

loss

The result of the sale of an asset for less than its carrying amount; the write-down of assets; the net result of expenses exceeding revenues.

loss contingency

See contingent loss.

loss from labor strike

This loss is not an extraordinary item, since it is not unusual in nature. However, it can appear as a separate line item in the main portion of the income statement. It will be reported at its gross amount (not net of the tax savings).

loss from lawsuit

A non-operating or "other" reduction in net income resulting from a judgment against the company. It is shown in the accounting period when the amount is determined to be *probable* and *the amount can be estimated*. This means that the loss is likely to be shown earlier than the date that the payment is made. If the "loss" is only *possible* (not probable) it is disclosed in the notes to the financial statements rather than a reduction on the income statement and a liability on the balance sheet. If the "loss" is remote it is neither noted nor entered on the financial statements.

loss from reducing inventory to NRV

An income statement account used to record the amount that the asset Inventory is reduced during the accounting period because the net realizable value of the inventory is less than its cost.

loss on sale of assets

This is a non-operating or "other" item resulting from the sale of an asset (other than inventory) for less than the amount shown in the company's accounting records.

loss on sale of computer

A non-operating item resulting from the sale of this long-term asset for less than its carrying amount (or book value).

loss on sale of equipment

A non-operating item resulting from the sale of this long-term asset for less than its carrying amount (or book value).

loss on sale of land

A non-operating item resulting from the sale of this long-term asset for less than its carrying amount (or book value).

loss on sale of truck

A non-operating item resulting from the sale of this long-term asset for less than its carrying amount (or book value).

losses

Losses result from the sale of an asset (other than inventory) for less than the amount shown on the company's books. Since the loss is outside of the main activity of a business, it is reported as a nonoperating or other loss. To learn more, see Explanation of Income Statement. The term losses is also used to report the writedown of asset amounts to amounts less than cost. It is also used to refer to several periods of net losses caused by expenses exceeding revenues.

lost opportunity

The benefit foregone by choosing another course of action. Also known as the opportunity cost. The lost opportunity is sometimes measured by the lost contribution margin (sales minus the related variable costs).

lower of cost or net realizable value

In the context of inventory this means that the inventory should be reported at the lower of its cost or its net realizable value (NRV). The rule is associated with the conservatism guideline or principle.

Net realizable value is defined as the expected selling price in the ordinary course of business minus the cost of completion, disposal, and transportation.

Accounting Terms (M)

m

One of the symbols used to represent 1000. Others include k and the Roman numeral M. (Note: Some magazines are now using m to indicate million.)

M

The Roman numeral that represents 1000. Other symbols that are sometimes used to represent 1000 include k and m. (Note: Sometimes M is also used to indicate million.)

make or buy decision

A decision whether to make some products or equipment in-house versus purchasing the products or equipment from another company. As in any decision, one must compare the relevant costs and other opportunities. It is possible that the cost to make an item will involve an increase in only some costs and will, therefore, be less costly than purchasing the item from another company.

major repairs

An example is the major overhaul of a truck's engine that will extend the useful life of the truck. This expenditure is recorded on the balance sheet in an asset (or in a contra asset) account and then depreciated over the remaining life of the truck. (Ordinary repairs are recorded immediately as an expense.)

management accounting

See managerial accounting.

management and general expenses

A subgroup of the supporting activities of a nonprofit organization. This functional expense classification is used to report the overall management of the nonprofit organization other than the direct expenses of operating its programs and fundraising. For example, the accounting and budgeting expenses are part of management and general expenses.

management's discussion and analysis

A section of a publicly traded corporation's annual report to the SEC (form 10-K). This section contains extensive information from management about the corporation's financial condition and its operations.

managerial accounting

The field of study within accounting that is devoted to information needed by the management of the company (as opposed to financial accounting to external parties). Topics covered in managerial accounting include cost behavior, product costing for manufacturers, budgeting, amounts needed for decision making, transfer pricing, capital budgeting, etc.

manual system

The accounting or bookkeeping system that does not utilize computer software for entering transactions into journals and ledgers.

manufacturing cell

Often a U-shaped arrangement of the various machines involved in manufacturing a product. This layout eliminates the need to move the item being manufactured from one area or department of the factory to another. In addition to saving the handling cost, it may save space and reduce inventory levels.

manufacturing costs

Direct materials, direct labor and manufacturing overhead costs. Also referred to as product costs, production costs, and inventoriable costs.

manufacturing overhead

Manufacturing costs other than direct materials and direct labor. See Explanation of Manufacturing Overhead.

manufacturing support costs

Also referred to as factory burden, factory overhead, indirect manufacturing costs, and manufacturing support costs. To learn more, see Explanation of Manufacturing Overhead.

margin of safety

A term used in break-even analysis to indicate the amount of sales that are above the break-even point. In other words, the margin of safety is the amount by which a company's sales could decrease before the company will become unprofitable.

marginal cost
The cost of the next unit.

marginal revenue
The revenue from the next unit.

markdown
A reduction in the original selling price.

markdown cancellation
The elimination of part or all of a markdown.

market interest rate
Also referred to as the current interest rate, the yield-to-maturity, and the effective interest rate. The market interest rate is always changing whereas the stated interest rate does not change.

market share
A company's sales in a market as compared to the total sales in that market. For example, General Motors share of the U.S. market has decreased from more than 50% in the 1960's to its present market share of less than 30%.

marketable debt securities
This term is often associated with an investment in the bonds issued by another corporation if the bonds are traded on a bond exchange.

marketable equity securities
This term is often associated with an investment in the common stock (and/or preferred stock) of a corporation when the stock is publicly traded.

marketable securities
Investments in common stock, preferred stock, corporate bonds, or government bonds that can be readily sold on a stock or bond exchange. These investments are reported as a current asset if the investor's intention is to sell the securities within one year.

markup
This could be the difference between cost and the selling price. For example, a retailer may markup its cost by 50% to arrive at a selling price. In the retail method of costing inventory, markup is used to mean the "additional" markup from the original selling price. For example, an item with a cost of $10 might normally be priced at $15. However, because of the shortage of this item and because of high demand, the retailer sets a selling price of $17. Sometimes markup means the $7, but sometimes it means the additional markup of $2.

markup cancellation

A reduction of a markup. In the retail method of estimating inventory, it could mean the elimination of part or all of the additional markup. For example, if an item with a cost of $10 would normally be priced at $15, but instead is priced at $17 due to supply and demand considerations, the “additional” markup was $2. If the retailer reduces the price to $15.50 there would be a markup cancellation of $1.50.

Mary Smith, Capital

The owner’s equity account that contains the amount invested in the sole proprietorship by Mary Smith plus the net income since the company began minus the draws made by Mary Smith since the company began. The current year net income might be in the temporary revenue and expense accounts and the current year draws might be in the drawing account. However, after the financial statements for the year are prepared the current year net income and draws will be transferred to this account.

Mary Smith, Drawing

This contra owner’s equity account has a debit balance that represents the current year draws made by the owner, Mary Smith. After the year’s financial statements have been prepared, the balance in this temporary account will be transferred to Mary Smith, Capital.

matching principle

The principle that requires a company to match expenses with related revenues in order to report a company’s profitability during a specified time interval. Ideally, the matching is based on a cause and effect relationship: sales causes the cost of goods sold expense and the sales commissions expense. If no cause and effect relationship exists, accountants will show an expense in the accounting period when a cost is used up or has expired. Lastly, if a cost cannot be linked to revenues or to an accounting period, the expense will be recorded immediately. An example of this is Advertising Expense and Research and Development Expense.

materiality

The accounting guideline that permits the violation of another accounting guideline if the amount is insignificant. For example, a profitable company with several million dollars of sales is likely to expense immediately a $200 printer instead of depreciating the printer over its useful life. The justification is that no lender or investor will be misled by a one-time expense of $200 instead of say $40 per year for five years. Another example is a large company’s reporting of financial statement amounts in thousands of dollars instead of amounts to the penny.

materials inventory

One component of a manufacturer’s inventory. Sometimes referred to as Stores or Raw Materials. (Other components of a manufacturer’s inventory are work-in-process and finished goods.)

materials price variance

See direct materials price variance.

materials quantity variance
See direct materials usage variance.

materials usage variance
See direct materials usage variance.

matrix format
See functional and natural matrix.

Matt Jones, Capital
The owner's equity account that contains the amount invested in the sole proprietorship by Matt Jones plus the net income since the company began minus the draws made by Matt Jones since the company began. The current year net income might be in the temporary revenue and expense accounts and the current year draws might be in the temporary drawing account. However, after the financial statements for the year are prepared the current year net income and draws will be transferred to this account.

Matt Jones, Current year net income
The net amount of revenues and gains minus expenses and losses for the sole proprietorship owned by Matt Jones. After the financial statements are prepared for the year, this amount will be transferred to Matt Jones, Capital.

Medicare tax
One component of the FICA tax (the other component is Social Security). This payroll tax is withheld from employees' payroll checks and is also matched by the employer. The employee and the employer each pay the Medicare tax of 1.45% of all wages and salaries. As a result, the employer must remit to the federal government 2.9% of its employees' wages and salaries.

Beginning in 2013 there is a Medicare surtax of 0.9% that is applied to an employee's wages and salaries in excess of specified amounts. It also applies to a self-employed person's net income. See IRS.gov for details.

membership dues
Regular fees or charges often paid to an organization at regular intervals. For example, a state CPA organization might have annual dues of $200.

memo entry
An entry without debit or credit amounts. For example, assume that a corporation has 100,000 shares of $0.50 par value common stock before a 2-for-1 stock split. At the time of the split a memo entry would be entered in the records stating that after the 2-for-1 stock split, the corporation has 200,000 shares of $0.25 par value common stock outstanding. No dollar amounts would be posted to the accounts in the general ledger.

merchandise
Goods sold by a retailer, wholesaler, distributor, manufacturer, etc.

merchandise in transit
See goods in transit.

merchandise inventory
The current asset which reports the cost of a retailer's, wholesaler's, or distributor's goods purchased to be resold, which have not yet been sold as of the balance sheet date.

merchandiser
A business that sells goods from inventory. The business could be a retailer, wholesaler, distributor, manufacturer, etc.

MICR
Magnetic ink character recognition.

mid-month convention
This term is usually associated with assets that are depreciated. In the month that an asset is acquired or disposed, it is assumed to have occurred in the middle of the month.

mid-year convention
The practice where an asset purchased within a year is assumed to have been purchased at the mid-point of the year. For example, an asset purchased during the calendar year 2024 is assumed to have been purchased on July 1, 2024.

MIS
Management information system.

miscellaneous expense
An income statement account for expense items that are too insignificant to have their own separate general ledger accounts.

mixed costs
Costs that have both a fixed and variable component. For example, the cost of operating an automobile includes some fixed costs that do not change with the number of miles driven (e.g., operating license, insurance, parking, some of the depreciation, etc.) Other costs vary with the number of miles driven (e.g., gasoline, oil changes, tire wear, etc.).

mixed expenses
Used in conjunction with cost or expense behavior. Mixed expenses consist of a constant or fixed portion and a variable portion. For example, sales salaries would be a mixed expense if each sales person's compensation is $2,000 per month plus 3% of the sales generated by the employee. Automobile expense is a mixed expense in relationship to miles driven. The automobile insurance, licensing, and parking are fixed expenses in that they do not vary with the miles driven. Gasoline and maintenance are considered variable because they will vary with miles driven.

mm

The symbol for 1,000,000.

MM

The Roman numerals that indicate 1,000,000.

monetary asset

An asset such as cash, accounts receivable, or a note receivable where the amount is a fixed, stated amount. Holding these assets during periods of inflation will result in a loss of purchasing power.

monetary unit assumption

An accounting guideline where the U.S. dollar is assumed to be constant (no change in purchasing power) over time. This allows an accountant to add one dollar from a transaction in 2010 to one dollar in 2024 and to show the result as two dollars. It also means that items that cannot be expressed in dollars do not appear in the financial statements. For example, how would you express on a company's balance sheet the value of loyal customers or a brilliant, aggressive management team?

money market account

A bank or investment account with a fluctuating interest rate. Usually the funds can be withdrawn on demand, even though the account is not a checking account.

mortgage

A lien on real estate to protect a lender. The loan made with such security is referred to as a mortgage loan.

mortgage bond

A bond (long-term debt) that is secured by a lien on real estate.

mortgage loan

A loan having the security of a lien on the borrower's real estate.

mortgage loan payable

A liability account whose balance is the unpaid principal balance as of the balance sheet date. The amount of principal required to be paid within 12 months of the balance sheet date is reported as a current liability. The unpaid principal balance not due within one year of the balance sheet date is reported as a long term liability.

mortgage loan receivable

An asset account used to record a loan to another party that has real estate as collateral.

moving average

An average that changes with an additional purchase. See perpetual moving average in Explanation of Inventory and Cost of Goods Sold.

multicollinearity

A situation where there is correlation between the independent variables used in explaining the change in a dependent variable. When this condition exists, you cannot have confidence in the individual coefficients of the independent variables.

multiple regression analysis

A statistical tool used to determine the coefficients of the two or more independent variables involved in estimating the amount of the dependent variable. It utilizes the least-squares method for determining the coefficients of the independent variables.

multiple-step income statement

An income statement that has more than one subtraction in arriving at net income. An income statement showing gross profit is an indication it is a multiple-step income statement.

Accounting Terms (N)

NAA

National Association of Accountants. This organization's name was changed to Institute of Management Accountants and currently is referred to as IMA.

National Association of Accountants (NAA)

This organization has changed its name to Institute of Management Accountants. It is currently using the name IMA to reflect the many backgrounds of its membership.

natural basis

See natural expense classification.

natural business year

The one-year period ending at an organization's typical low point of activity. For example, a school's natural business year is July 1 through June 30. It is practical to have the accounting and financial reporting year match the natural business year. An accounting and financial reporting year ending on a date other than December 31 is referred to as a fiscal year.

natural expense classification

Sorting and reporting expenses by the nature of the expense such as salaries, wages, rent, utilities, supplies, depreciation, advertising, and so on.

natural resources

Long term assets of a company such as minerals, oil reserves, timberland, stone quarries, etc. The term depletion is associated with natural resources.

negative owner's equity

A net debit balance for the total amount of owner's equity. It is the result of the reported amount of liabilities exceeding the reported amount of assets.

net

The result of two or more amounts being combined. For example, net sales is equal to gross sales minus sales returns, sales allowances, and sales discounts. The net realizable value of accounts receivable is the combination of the debit balance in accounts receivable and the credit balance in the allowance for doubtful accounts. The book value of equipment is also a net amount: the cost of the equipment minus the accumulated depreciation of the equipment.

net assets

The result of subtracting total liabilities from total assets. It is also the term used by not-for-profit organizations instead of owner's equity or stockholders' equity. To learn more see our Explanation of Nonprofit Accounting.

net assets with donor restrictions

Beginning in 2018, this is one of two classifications of net assets reported on the financial statements of a not-for-profit organization's financial statements. This classification is to be used instead of the following two classifications: *temporarily restricted net assets* and *permanently restricted net assets*. Beginning in 2018, the other classification of net assets reported on the financial statements of a not-for-profit organization is *net assets without donor restrictions*.

net assets without donor restrictions

Beginning in 2018, this is one of two classifications of net assets reported on the financial statements of a not-for-profit organization's financial statements. This classification replaces the previous classification *unrestricted net assets*. Beginning in 2018, the other classification of net assets reported on the financial statements of a not-for-profit organization is *net assets with donor restrictions*.

net book value

Same as *book value*. For example, an asset's net book value is equal to the asset's cost minus its accumulated depreciation.

net carrying amount

This term might be used to express the combined balances of two accounts. For example, if Equipment has a debit balance of $300,000 and the account Accumulated Depreciation on Equipment has a credit balance of $130,000, we might say that the equipment has a net carrying amount of $170,000. Similarly, if Bonds Payable has a credit balance of $1,000,000 and Premium on Bonds Payable has a credit balance of $8,000, the net carrying amount is $1,008,000. This is similar to book value.

net cash flow from financing activities

The third major section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

net cash flow from investing activities

The second major section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

net cash flow from operating activities

The first major section of the statement of cash flows. To learn more, see Explanation of Cash Flow Statement.

net credit sales

The net amount of gross sales on credit minus the sales returns, sales allowances, and sales discounts which pertain to the sales on credit.

net current assets

Current assets minus current liabilities. Also see working capital.

net income

This is the bottom line of the income statement. It is the mathematical result of revenues and gains minus the cost of goods sold and all expenses and losses (including income tax expense if the company is a regular corporation) provided the result is a positive amount. If the net amount is a negative amount, it is referred to as a net loss.

net income available for common stock

A corporation's net income after income taxes minus the dividends pertinent to the preferred shares of stock (if any).

net loss

The bottom line of the income statement when revenues and gains are less than the aggregate amount of cost of goods sold, operating expenses, losses, and income taxes (if the company is a regular corporation).

net method of recording accounts payable

The technique of recording accounts payable at the amount that will be paid after deducting any discount that is available for paying within the discount period. This has a theoretical advantage over the gross method because the liability is recorded at the amount that will be paid and the purchase is recorded at the cash equivalent amount.

net of tax

A gross amount minus the income tax associated with the gross amount. For example, a company may dispose of one of its business segments and show a gain (proceeds exceed carrying amount) of $10,000,000. However, if the gain will result in income taxes of $3,000,000, the gain net of tax is $7,000,000.

net operating income (NOI)

Also known as income from operations, which excludes discontinued operations, extraordinary items, and nonoperating items such as interest expense, investment income, gains, and losses.

net pay

Gross wages or gross salaries minus withholdings for payroll taxes and other items such as insurance, union dues, United Way, etc. Also referred to as "take home pay" or the amount the employee "cleared." To learn more, see Explanation of Payroll Accounting.

net payroll payable

This current liability account reports the "net" amount a company owes its employees as of the date of the balance sheet. The "net" amount is the amount of the employees' paychecks—their take-home pay, or the amount the employees cleared after deducting payroll taxes and voluntary deductions. To learn more, see Explanation of Payroll Accounting.

net present value

The net result of combining the discounted cash inflows and the discounted cash outflows of an investment, project, company, etc.

net purchases

The gross purchases of merchandise for resale minus purchase returns, purchase allowances, and purchase discounts.

net realizable value (NRV)

In the context of inventory, net realizable value or NRV is the expected selling price in the ordinary course of business minus the costs of completion, disposal, and transportation.

In the context of accounts receivable it is the amount of accounts receivable that is expected to be collected. This should be the debit balance in Accounts Receivable minus the credit balance in Allowance for Doubtful Accounts.

You could think of NRV as the cash realizable value.

net sales

Net sales is the gross amount of Sales minus Sales Returns and Allowances, and Sales Discounts for the time interval indicated on the income statement.

net working capital

See working capital.

next-in, first-out cost flow assumption

This is the expression for replacement cost, which is not an acceptable cost flow, since it violates the cost principle. However, an economist and decision makers would argue that the cost to replace the item is the relevant amount.

NIFO

See next-in, first-out cost flow assumption (NIFO).

NOI

See net operating income (NOI).

nominal account

See temporary accounts.

nominal interest rate

See contractual interest rate.

noncash expense

An expense reported on the income statement that did not require the use of cash during the period shown in the heading of the income statement. The typical example is depreciation expense. Also, the write-down of an asset's carrying amount will result in a noncash charge against earnings.

noncumulative preferred stock

Preferred stock where past, omitted dividends do not have to be paid before a dividend can be paid to common stockholders. In the case of noncumulative preferred stock, only its current year dividend needs to be paid in order for a corporation to pay a dividend to its common stockholders.

noncurrent assets

See long-term assets.

noncurrent liabilities

See long-term liabilities.

nonexempt employee

An employee that must be paid overtime pay when the employee's weekly hours exceed 40 hours. Some states may have additional requirements. Nonexempt employees include both hourly-paid and salary-paid who are not highly-paid.

nonmanufacturing overhead cost

See Explanation of Nonmanufacturing Overhead.

nonmonetary asset

Assets *other than* cash, accounts receivables, and notes receivables. Holders of nonmonetary assets could avoid holding losses during periods of inflation.

nonoperating expense

An expense outside of a company's main operating activities of buying and selling merchandise or providing services. For example, interest expense is a nonoperating expense.

nonoperating income/revenue

Income or revenue earned by a company that is outside of its main operating activities. For a retailer the interest earned on its temporary investments is a nonoperating revenue (or nonoperating income).

nonparticipating preferred stock

This term is associated with preferred stock that does not allow its holders to receive more than its stated dividend. The nonparticipating feature is typical in preferred stock. To learn more about preferred stock, see Explanation of Stockholders' Equity.

nonprofit organization

An organization without owners and with the main purpose of providing services needed by society. After application and approval by the U.S. Internal Revenue Service, a nonprofit organization may be granted tax exempt status.

nontrade receivables

Receivables other than Accounts Receivable. Examples include amounts due from employees and income tax refunds receivable.

no-par value stock

Stock without a par value.

normal account balance

The debit or credit balance that would be expected in a specific account in the general ledger. For example, asset accounts and expense accounts normally have debit balances. Revenues, liabilities, and stockholders' equity accounts normally have credit balances.

normal costing

The actual cost of direct materials, the actual cost of direct labor, and manufacturing overhead applied by using a predetermined annual overhead rate.

normal operating activities

Retailers' normal operating activities would include the purchase and sale of merchandise and selling and administrative expenses. A retailer's investing of its idle cash is a nonoperating activity. However, a bank's normal operating activities would include investing and lending of the money.

normal spoilage

Spoilage or waste that is likely to occur and cannot be avoided at a reasonable cost.

not-for-profit organization

See nonprofit organization.

not sufficient funds (NSF) check

A check often referred to as an NSF check, a rubber check, or a check that bounced. It is a check that was not paid by the bank of the issuer (writer) of the check because the checking account of the issuer did not have sufficient collected funds in the account.

notes payable

The amount of principal due on a formal written promise to pay. Loans from banks are included in this account.

notes receivable

An asset representing the right to receive the principal amount contained in a written promissory note. Principal that is to be received within one year of the balance sheet date is reported as a current asset. Any portion of the notes receivable that is not due within one year of the balance sheet date is reported as a long term asset.

notes to financial statements

Also referred to as footnotes. These provide additional information pertaining to a company's operations and financial position and are considered to be an integral part of the financial statements. The notes are required by the full disclosure principle.

NPV

See net present value.

NRV

See net realizable value.

NSF check

See not sufficient funds (NSF) check.

Accounting Terms (O)

OASDI

See old-age, survivor, and disability insurance (OASDI).

objectives of financial reporting

In the 1970's the Financial Accounting Standards Board (FASB) articulated three objectives of financial reporting. In summary, financial information should (1) be useful to investors and lenders, (2) be helpful in determining a company's cash flows, and (3) report the company's assets, liabilities, and owner's equity and the changes in them.

objectivity
Fair, unbiased, and objective; not subjective.

obsolescence
The process of becoming outdated or no longer being economically feasible (often caused by technology advances). For example, personal computers and computer chips from 2010 are obsolete even though they can be operated. Holding inventory of electronic components will often result in losses because of obsolescence.

OEM
The acronym for original equipment manufacturer.

off balance sheet financing
Obligations not reported as liabilities on the balance sheet.

office equipment
A long-term asset account reported on the balance sheet under the heading of property, plant, and equipment. Included in this account would be copiers, computers, printers, fax machines, etc.

office equipment expense
The cost to operate office equipment during a specified time interval.

office supplies expense
The amount of office supplies *used* during a specified time interval.

officers
Officers of a corporation are appointed by the board of directors to execute the policies that have been established by the board of directors. The officers include the chief executive officer (CEO), the chief operations officer (COO), chief financial officer (CFO), vice presidents, treasurer, secretary, and controller.

old-age, survivor, and disability insurance (OASDI)
U.S. social security system.

omitted dividends on preferred stock
See dividends in arrears.

on account
On credit; not for cash.

on consignment
Goods placed with another party without transferring ownership. See consigned goods.

on credit

On account. Goods purchased with terms of net 10 days, net 30 days, or 2/10, net 30 are goods purchased on credit. Goods sold with similar terms are sales on credit.

operating activities

The activities involved in earning revenues. For example, the purchase or manufacturing of merchandise and the sale of the merchandise including marketing and administration. In the statement of cash flows the operating activities section identifies the cash flows involved with these activities by focusing on net income and the changes in the current assets and current liabilities.

operating cycle

The average time it takes for a retailer's or manufacturer's inventory to turn to cash. If a manufacturer turns its inventory six times per year (every two months) and allows customers to pay in 30 days, its operating cycle is approximately three months.

operating expenses

Operating expenses are the costs of a company's main operations that have been used up during the period indicated on the income statement. For example, a retailer's operating expenses consist of its cost of goods sold and its selling, general and administrative expenses (SG&A).

operating income

A company's profit before nonoperating or other items. Other or nonoperating items include interest income, interest expense, and gains and losses on sale of assets used in the business, loss on lawsuit, etc.

operating lease

A rental agreement where ownership is not intended. An operating lease is not recorded in the general ledger accounts and therefore the asset and liability will not appear on the balance sheet. A lease that in substance is the purchase and financing of an asset is a capital lease.

operating loss

A company's loss before nonoperating or other items. Other or nonoperating items include interest income, interest expense, and gains and losses on sale of assets used in the business, loss on lawsuit, etc.

opportunity cost

The next best benefit foregone. The opportunity lost. Often measured as the contribution margin given up by not doing an activity. For example, if a sole proprietor is foregoing a salary and benefits of $50,000 at another job, the sole proprietor has an opportunity cost of $50,000. Accountants do not record opportunity costs in the general ledger or report them on the income statement, but they are costs that should be considered in making decisions.

order costs

In the EOQ model, order costs are the incremental costs of processing an order of goods from a supplier. Examples of order costs include the costs of preparing a requisition, a purchase order, and a receiving ticket, stocking the items when they arrive, processing the supplier's invoice, and remitting the payment to the supplier.

ordinary annuity

A series of equal amounts occurring at the end of each equal time interval. Also known as an annuity in arrears. An example is the monthly payments on a loan. Another example is the semiannual interest on a bond.

ordinary repairs

Repairs that do not improve an asset or extend the asset's life. These repairs are charged to Repairs Expense or Maintenance Expense when incurred. Major repairs such as a complete engine overhaul that extends the useful life of the engine would be reported differently.

organic growth

The internal growth of a company's existing businesses. Organic growth excludes the additional sales resulting from acquiring another company.

organization as a whole

See entity as a whole.

organization chart

A diagram depicting a company's hierarchy or chain of command, its business segments, functions, and departments.

organization-sustaining activities

Activities that are not specifically associated with a specific product or customer. For example, the costs of an audit and filing information with government agencies are examples of organization-sustaining activities.

other accrued expenses payable

Obligations that a company has incurred, but have not yet been routinely recorded in Accounts Payable. For example, if the interest on a bank loan is paid on the 10th of each month, then on the last day of each month approximately 20 days of interest expense is an accrued expense payable.

other assets

Long term assets that are not classified as investments, property, plant, equipment, or intangible assets. An example is bond issue costs that are amortized to expense over the life of the bonds.

other current assets

A balance sheet line to report short-term assets that are too insignificant to be identified separately.

other current liabilities

A balance sheet line to report short-term liabilities that are too insignificant to be identified separately.

outlier

A cost and/or volume of activity that is outside of an expected range.

output

Manufactured products that are often expressed in units, machine hours, etc.

outside supplier

Another company that supplies goods or performs services. Also known as a vendor.

outsourcing

Sending work to another organization instead of processing the work in-house. Often payroll is outsourced to a company that specializes in payroll processing.

outstanding checks

Checks which have been written, but have not yet cleared the bank on which they were drawn. In the bank reconciliation, outstanding checks are deducted from the balance per bank. To learn more, see Explanation of Bank Reconciliation.

outstanding shares of common stock

The issued shares of common stock minus the shares of treasury stock. The weighted average of the outstanding shares is used to compute the earnings per share.

overabsorbed

The term used by manufacturers to indicate that the manufacturing overhead applied or assigned to its production is greater than the amount actually incurred.

overapplied overhead costs

Assigning more manufacturing overhead to production than the amount that was actually incurred.

overdraws

A term that refers to a negative checking account balance. It arises when a company writes checks in excess of the amount it has on deposit in its checking account.

overhead application

Assigning manufacturing overhead costs to products being manufactured by using a manufacturing overhead rate.

overhead costs

Usually refers to manufacturing overhead costs such as factory supplies, factory depreciation, indirect factory labor, etc. To learn more, see Explanation of Manufacturing Overhead.

overhead variances

To learn more, see Explanation of Standard Costing.

overstates

Reports too much. If an error overstates the inventory and the company's net income, the amount of inventory and the amount of net income being reported is more than the correct amount.

overtime pay

Usually the pay for the hours worked in excess of 40 hours per week. Federal laws require payment for these hours for employees who are not able to control their hours. For example, a company is required to pay a production worker or office clerk for hours in excess of 40 per week, even if they are salaried. However, the company is not required to pay a company executive for hours in excess of 40 per week, since the executive can control his or her hours. To learn more, see Explanation of Payroll Accounting.

overtime premium

The additional amount given to employees for the overtime hours. Usually this is the "half-time" in time and one-half. For example, if an employee's hourly pay rate is $10 per hour and the employee works 41 hours in a week, the overtime premium is $5 per hour. The worker will earn $415 for the 41 hours. ($400 for 40 hours plus $10 + $5 for the one hour of overtime.)

owner's capital account

The account in which the owner's investment is recorded plus the net income earned by the company minus the draws made by the owner. Current year net income and draws will be in temporary accounts until the end of the year.

owner's capital account - beg of year

The balance of the owner's capital account excluding the current year's net income and current year's draws by the owner.

owner's drawing account

The contra owner's equity account used to record the current year's withdrawals of business assets by the sole proprietor for personal use. This is a temporary account with a debit balance. It will be closed at the end of the year to the owner's capital account.

owner's (stockholders') equity

The book value of a company equal to the recorded amounts of assets minus the recorded amounts of liabilities. To learn more, see Explanation of Balance Sheet.

owner's equity accounts

The owner's equity accounts are the owner's capital account and the owner's drawing account. During the year the income statement accounts (revenues, expenses, gains, losses), the owner's drawing account, and the income summary accounts are considered to be temporary owner's equity accounts, because at the end of the year the balances in these temporary accounts will be transferred to the owner's capital account.

Accounting Terms (P)

P & L

The abbreviation for profit and loss statement. Also known as the income statement. To learn more, see Explanation of Income Statement.

Pacioli

An Italian monk associated with debits, credits, and double-entry accounting approximately 500 years ago.

paid-in capital

The amount paid or contributed by stockholders in exchange for shares of a corporation's stock.

paid-in capital from treasury stock

A stockholders' equity account with a credit balance. The credit balance results when a corporation sells some of its treasury stock for an amount that exceeds the corporation's cost of the treasury stock that was sold.

paid-in capital in excess of par value

See paid-in capital in excess of par value - common stock, or paid-in capital in excess of par value - preferred stock.

paid-in capital in excess of par value - common stock

The stockholders' equity account that represents the amount paid to a corporation for its common stock that was in excess of the common stock's par value. This account is sometimes referred to as the premium on common stock (The par value of common stock is recorded in a separate stockholder's equity account.)

paid-in capital in excess of par value - preferred stock

The stockholders' equity account that represents the amount paid to a corporation for its preferred stock that was in excess of the preferred stock's par value. This account is sometimes referred to as the premium on preferred stock (The par value of preferred stock is recorded in a separate stockholder's equity account.)

paid-in capital in excess of stated value - common stock

The stockholders' equity account that reports the amount paid to a corporation that is in excess of the common stock's stated value. The stated value of each share issued is recorded in the Common Stock account.

paid sick days

An employee fringe benefit provided by an employer that allows employees to be paid for a limited number of days per year when the employees are ill.

paid vacation days

An employee fringe benefit provided by an employer that allows employees to be absent from work with pay. Often the number of paid vacation days allowed is based on the number of years of employment.

par value

A stated legal amount often appearing on preferred stock, bonds, and some common stock.

par value of bonds

The stated legal amount appearing on bonds.

par value of common stock

A stated legal amount for each share of common stock. The par value for every share of common stock issued must be recorded in the separate stockholders' equity account Common Stock.

par value of preferred stock

A stated legal amount for each share of preferred stock. The par value for every share of preferred stock issued must be recorded in the separate stockholders' equity account Preferred Stock.

participating preferred stock

Preferred stock where the dividend could be more than the original, stated dividend.

partnership

A form of business entity having partners. (Consult with an attorney about this form of entity versus alternatives.)

pass-through contributions

Contributions collected by Charity #1 who is merely acting as a collection agent for Charity #2. Also known as flow-through contributions.

past cost

Also referred to as a sunk cost. A past cost is not relevant to a decision.

payable

In accounting this word is often included in the title of liability accounts. It means the amount owed by a company as of the balance sheet date, even if the company did not yet receive an invoice from the supplier. For example, the electric utility furnishes electricity for the month of January, but does not read the meter until February 1 and sends the invoice or bill on February 4. The company pays the bill on March 1. The electricity used in January is a payable or obligation on January 31. To learn more, see Explanation of Adjusting Entries.

payback

In business decision-making, payback means the number of years before the cash invested in a project is returned. It involves the cash flows from the project but generally the cash flows are *not* discounted to reflect the time value of money.

payback period

The number of years needed to recover the cash amount invested in a project. The calculation uses cash flows rather than accounting income flows. Generally the cash flows are not discounted to reflect the time value of money.

payee

The person or organization to whom a check is written.

payroll accrual

See accrued payroll.

payroll tax liability

See payroll taxes payable.

payroll taxes

Payroll taxes include 1) the taxes withheld from employees' wages and salaries such as Social Security tax, Medicare tax, federal income tax, and state income tax, 2) the employers' matching of the Social Security and Medicare taxes, and 3) the employers' cost of federal and state unemployment taxes.

payroll taxes payable

A current liability that includes payroll taxes withheld from employees and payroll taxes that are levied on an employer but have not yet been remitted.

payroll withholdings

The amounts withheld for employees' checks for Social Security tax, Medicare tax, federal income tax, state income tax, and voluntary deductions such as United Way, union dues, 401(k) contributions, employees' portion of health insurance, etc. To learn more, see Explanation of Payroll Accounting.

PCAOB

See Public Company Accounting Oversight Board.

pension expense

Under the accrual method of accounting, this account reports the employer's expense for the company's pension plan during the period indicated in the heading on the income statement. Information on pensions can be found in an Intermediate Accounting textbook.

pension payable

A liability account that reports the amount a company owes as of the date of the balance sheet for the company's pension plan. Information on pensions can be found in an Intermediate Accounting textbook.

period cost

An amount that should be charged to the current accounting period as an expense.

periodic average

A weighted average cost used with the periodic inventory system. To learn more, see Explanation of Inventory and Cost of Goods Sold.

periodic FIFO

One of the cost flow assumptions associated with the periodic inventory system. The first (oldest) costs are removed from inventory first and are charged to the income statement as cost of goods sold. The recent costs remain in inventory. To learn more, see Explanation of Inventory and Cost of Goods Sold.

periodic LIFO

One of the cost flow assumptions associated with the periodic inventory system. The latest (recent) costs of goods purchased are removed from inventory first and are charged to the income statement as cost of goods sold. The oldest costs remain in inventory. To learn more, see Explanation of Inventory and Cost of Goods Sold.

periodic system of inventory

The system where the general ledger account Inventory is not updated during the year. Rather, the merchandise purchased is recorded in temporary purchases accounts. At the time a balance sheet is presented, the inventory account is adjusted to reflect the cost of the inventory on hand. To learn more, see Explanation of Inventory and Cost of Goods Sold.

periodicity

See time period assumption.

permanent accounts

Also referred to as real accounts. Accounts that do not close at the end of the accounting year. The permanent accounts are all of the balance sheet accounts (asset accounts, liability accounts, owner's equity accounts) except for the owner's drawing account.

permanently restricted net assets

This classification of net assets has been replaced by the FASB with the classification *net assets with donor restrictions*.

perpetual average

The moving average cost of inventory items under the perpetual inventory system. A new average cost per unit is developed after each purchase of an inventory item. To learn more, see Explanation of Inventory and Cost of Goods Sold.

perpetual FIFO

The first-in, first-out cost flow assumption under the perpetual inventory system. The first (oldest) costs are the first costs removed from inventory at the time that goods are sold. The most recent costs will remain in inventory. The results are the same as periodic FIFO. To learn more, see Explanation of Inventory and Cost of Goods Sold.

perpetual inventory

See perpetual system of inventory.

perpetual inventory method

See perpetual system of inventory.

perpetual LIFO

The last-in, first-out cost flow assumption under the perpetual inventory system. The last (most recent) costs *as of the time that goods are sold* are the first costs removed from inventory. The oldest costs as of the time of the sale will remain in inventory. The results will be different from periodic LIFO. To learn more, see Explanation of Inventory and Cost of Goods Sold.

perpetual system of inventory

The inventory system where purchases are debited to the inventory account and the inventory account is credited at the time of each sale for the cost of the goods sold. Hence, the balance in the inventory account is constantly or perpetually changing. Under this system there is a general ledger account Cost of Goods Sold. To learn more, see Explanation of Inventory and Cost of Goods Sold.

PERT

See program evaluation and review technique (PERT).

petty cash

A current asset account that represents an amount of cash for making small disbursements for postage due, supplies, etc.

petty cash receipt

Usually a simple form used by the petty cash custodian in order to document small payments from a petty cash box.

petty cash replenishment

A request by the petty cash custodian for a company check in order to return the amount of currency and coins in the petty cash box to the amount shown in the general ledger account.

petty cash voucher
See petty cash receipt.

phantom profits
Also referred to as illusory profits. Occurs because accountants use past costs rather than replacement costs. For example, in computing the cost of goods sold accountants often use the FIFO cost flow assumption. This results in the oldest costs being matched with sales. Economists prefer that the replacement cost of the inventory be matched with sales. The difference in profits from using FIFO instead of the replacement cost is referred to as phantom or illusory profits. Similarly, accountants depreciate the original cost of buildings and equipment. Economists prefer that the replacement cost be depreciated. With inflation the accounting profits are higher than the economists would report using replacement cost.

physical count
An actual count of the goods owned by the company. The actual counts are then compared to the quantities reported on the detailed inventory records. If a difference exists, the quantity shown on the inventory record should be changed to the physical count.

physical inventory
An actual count of the goods owned by the business.

physical life
The length of time that an asset would last. Instead of the physical life, accountants focus on the useful life. For example, a computer's physical life is perhaps 50 years. However, its useful life is likely to be only five years or less, because newer more efficient computers will cause companies to replace computers before the end of their physical life.

plant assets
Often referred to as fixed assets. This would include long term assets such as buildings and equipment used by a company. Plant assets (other than land) will be depreciated over their useful lives.

plant-wide overhead rate
A single overhead rate for assigning all of the manufacturing production and service department costs to products. This rate is less accurate than departmental rates if a company manufactures a diverse group of products.

pledged asset
An asset which serves as collateral for a loan.

p.o.
See purchase order.

POP
Point of purchase.

POS

Point of sale.

post balance sheet event

Also referred to as a subsequent event. An event occurring after the date of the balance sheet, but prior to the date that the balance sheet is actually released. For example, a balance sheet dated December 31 might be released on January 26 due to the time required to prepare adjusting entries, write footnotes, and perhaps be audited or reviewed by a CPA firm. In this example a significant event occurring after December 31 but before January 27 is a post balance sheet event. The event *could* require changing some of the amounts on the balance sheet dated December 31 and on the income statement for the year ending December 31. On the other hand, some events will not require changing any of the amounts on the balance sheet dated December 31 or the income statement for the year ending on December 31. The latter items if significant will likely require a disclosure in the notes to December 31 financial statements.

post-closing trial balance

A listing of all of the accounts in the general ledger with account balances after the closing entries have been posted. This means that the listing would consist of only the balance sheet accounts with balances. The income statement accounts would not be listed because they are temporary accounts whose balances have been closed to the owner's capital account.

postdated check

A check bearing a date in the future. The company receiving such a check should not report the check as cash until the date of the check.

posting

Recording an entry in an account in the general ledger or in a subsidiary ledger.

postretirement benefits

Benefits provided by a company to retirees. Typical examples of potential benefits are pensions, life insurance, and health insurance.

predetermined overhead rate

Usually an annual manufacturing overhead rate established just prior to an accounting year and based on budgeted amounts.

preferred stock

A class of corporation stock that provides for preferential treatment over the holders of common stock in the case of liquidation and dividends. For example, the preferred stockholders will be paid dividends before the common stockholders receive dividends. In exchange for the preferential treatment of dividends, preferred shareholders usually will not share in the corporation's increasing earnings and instead receive only their fixed dividend.

preferred stock account

The stockholders' equity account which reports the par value of the preferred shares of stock that have been issued. Amounts received that are greater than the par value are recorded in Paid-in Capital in Excess of Par—Preferred Stock.

preferred stock $100 par

The paid-in (or contributed) capital account that is credited $100 for each share of $100 par preferred stock that is issued. If the proceeds from the issuance or sale of one of the shares is greater than $100, the amount in excess of $100 is credited to Paid-in Capital in Excess of par - Preferred Stock. To learn more about preferred stock, see Explanation of Stockholders' Equity.

premium on bonds payable

A liability account with a credit balance associated with bonds payable that were issued at more than the face value or maturity value of the bonds. The premium on bonds payable is amortized to interest expense over the life of the bonds and results in a reduction of interest expense. To learn more see Explanation of Bonds Payable.

premium on common stock

See paid-in capital in excess of par value - common stock.

premium on preferred stock

See paid-in capital in excess of par value - preferred stock.

prepaid advertising

A current asset that reports the amount paid for advertising that has not yet taken place. When the advertising occurs the prepaid advertising is reduced and advertising expense is recorded.

prepaid asset

See prepaid expense.

prepaid association dues

See prepaid dues.

prepaid dues

A current asset that reports the amount paid for dues that have not yet expired. As the prepaid dues expire, the account Prepaid Dues is reduced and dues expense is increased.

prepaid expense

A current asset representing amounts paid in advance for future expenses. As the expenses are used or expire, expense is increased and prepaid expense is decreased.

prepaid insurance

A current asset which indicates the cost of the insurance contract (premiums) that have been paid in advance. It represents the amount that has been paid but has not yet expired as of the balance sheet date.

A related account is Insurance Expense, which appears on the income statement. The amount in the Insurance Expense account should report the amount of insurance expense expiring during the period indicated in the heading of the income statement.

prepaid rent

A current asset account that reports the amount of future rent expense that was paid in advance of the rental period. The amount reported on the balance sheet is the amount that has not yet been used or expired as of the balance sheet date.

prepayment-type adjusting entry

See deferral-type adjusting entry.

present value

Future amounts that have been discounted to the present.

present value factors

Factors that are used to convert future cash flows to their present value.

present value of 1 table

A table showing present value factors for various interest rates and numbers of years/periods for a single amount at a future point in time.

present value of a single amount

The discounted value of a single future amount.

present value of an annuity

The discounted value of a series of equal amounts occurring at future points with equal time intervals.

present value of an annuity due

The discounted value of a series of equal amounts occurring at the beginning of each equal time interval.

present value of an annuity due table

A table showing the present value factors to be applied to the constant amount occurring at the beginning of each equal time interval. Also known as the present value table for an annuity in advance.

present value of an ordinary annuity

The discounted value of a series of equal amounts occurring at the end of each equal time interval.

present value of an ordinary annuity table

A table showing the present value factors to be applied to the recurring equal amount occurring at the end of each equal time interval.

present value model

A term used to describe the net present value method and the internal rate of return. The model discounts future cash flows back to the present time.

present value table

See present value of an annuity due table, present value of an ordinary annuity table, and present value of 1 table.

price earnings ratio

The ratio of the market value of a share of common stock to the earnings per share of common stock. For example, if a corporation earned $3 per share and its stock is trading at $36, it’s price earnings ratio is 12.

price variance

In standard costing the difference between the actual cost and the standard cost of direct materials or direct labor. The price variance of direct labor is usually referred to as the labor rate variance.

primary activities

For a retailer, wholesaler, and distributor the primary activities would be the buying of merchandise and then the sale of that merchandise. A manufacturer’s primary activities would be the production and sale of products.

prime costs

The combination of direct materials and direct labor.

principal

In financial accounting this term refers to the amount of debt excluding interest. Payments on mortgage loans usually require monthly payments of principal and interest.

principal payment

A payment toward the amount of principal owed. Generally when a loan payment consists of only a principal and interest payment, the amount owed for interest is processed first and the remaining amount of the payment is applied to the principal balance.

principles and guidelines
General rules upon which more-detailed, specific accounting rules and standards are based. To learn more, see Explanation of Accounting Principles.

prior period adjustment
The most common example is the correction of an error from a prior year. When such a correction is made, it is reported in the current period's statement of retained earnings rather than in the current period's income statement.

pro forma financial statement
Financial statements based upon various assumptions.

pro forma income
Income based upon some assumptions.

pro rata
A Latin term that means in proportion. See prorate.

proceeds
The amount received from the sale of an asset, from the issuance of bonds or stock, or from a bank loan.

process costing system
The cost accounting system where similar units are mass produced. Costs are collected by department and are then assigned to the units produced.

procurement
Another word for purchasing.

product cost
In manufacturing, the product cost includes direct materials, direct labor, and manufacturing overhead. A retailer's product cost is the net cost from suppliers plus costs to get the product in place and ready for use (e.g. freight-in).

product warranty cost
The cost of repairing or replacing previously sold products during their warranty periods.

production costs
See manufacturing costs.

production department
A department that is directly involved in manufacturing products. Examples are the machining, finishing, and assembling departments.

production service department

A department within a factory that does not directly produce a product. Examples are the factory maintenance department, factory administrative department, and quality assurance department.

production volume variance

See fixed manufacturing overhead volume variance.

profit and loss statement

Also referred to as the P & L and the income statement. To learn more, see Explanation of Income Statement.

profitability

A word to describe whether a company is able to earn more revenues than expenses.

profit center

A division or department of a business whose managers are responsible for both revenues and expenses.

profit margin

Net income divided by net sales.

program evaluation and review technique (PERT)

A management tool that identifies the critical path—the path of sequential activities requiring the longest time to complete.

program expenses

The expenses directly incurred by a nonprofit organization in providing one of its programs.

program services

The activities provided by a nonprofit in carrying out one of its major programs.

promissory note

A formal, written promise to pay interest and to repay the principal amount.

property dividend

A dividend paid in assets other than cash.

property, plant, and equipment

A major classification on the balance sheet. It is the second long term asset section after current assets. Included are land, buildings, leasehold improvements, equipment, furniture, fixtures, delivery trucks, automobiles, etc. that are owned by the company. To learn more, see Explanation of Balance Sheet.

proprietor

An individual owner of a business that is not incorporated.

proprietorship

See sole proprietorship.

prorate

To assign or allocate on a logical basis. For example, the materials price variance in a standard costing system is prorated to the following categories: materials inventory, work-in-process inventory, finished goods inventory, and the cost of goods sold. The proration is based on each categories' amount of standard materials cost from the period of the variances.

provision for doubtful accounts

See Allowance for Doubtful Accounts.

public companies

Corporations whose stock is traded on stock exchanges. Also referred to as publicly-traded corporations.

Public Company Accounting Oversight Board (PCAOB)

An organization established by the U.S.'s Sarbanes-Oxley Act to oversee the auditors of corporations whose stock is publicly-traded. The PCAOB's board members are appointed by the Securities and Exchange Commission (SEC), a U.S. government agency.

Publication 15

A publication by the U.S. Internal Revenue Service (IRS) to assist employers with federal payroll taxes. The complete title of the publication is Publication 15 (Circular E), Employer's Tax Guide. It is available at www.irs.gov.

publicly traded stock

The term that refers to the stock of a corporation which is traded on the stock exchanges (as opposed to stock that is privately held among a few individuals).

purchase allowance

A reduction in the cost of goods purchased that is granted by a supplier without the physical return of the goods.

Also a general ledger account in which the purchase allowances are recorded under the periodic inventory method.

purchase commitments

A commitment to purchase a specific number of items in the future at a fixed price. If the agreement is noncancelable, the company must report a loss when the current cost of the items falls below the contracted price.

purchase discount

Often a 1% or 2% discount that a buyer may deduct from the amount owed to a supplier (if stated on the supplier's invoice) for paying in 10 days instead of the customary 30 days. The purchase discount is also referred to as an early-payment discount.

Also a general ledger account in which the purchase discounts are recorded under the periodic inventory method.

purchase order

Also referred to as a "p.o." A multi-copy form prepared by the company that is ordering goods. The form will specify the items being ordered, the quantity, price, and terms. One copy is sent to the vendor (supplier) of the goods, and one copy is sent to the accounts payable department to be later compared to the receiving ticket and invoice from the vendor.

purchase return

A reduction in the cost of goods purchased that is allowed by the supplier based on the authorized return of goods.

Also a general ledger account in which the purchase returns are recorded under the periodic inventory method.

purchases

A temporary account used in the periodic inventory system to record the *purchases of merchandise for resale*. (Purchases of equipment or supplies are *not* recorded in the purchases account.) This account reports the gross amount of purchases of merchandise. Net purchases is the amount of purchases minus purchases returns, purchases allowances, and purchases discounts.

purchases discounts

The temporary contra purchases account used in a periodic inventory system which represents the discounts allowed by paying within prescribed credit terms such as 1/10 (1% can be deducted from the amount owed if paid within 10 days). When the credit balance of this account is combined with the other purchases accounts, the result is the amount of net purchases.

purchases - net

The gross amount of purchases minus the amount of purchase returns, purchase allowances, and purchase discounts.

purchases returns and allowances

The temporary contra purchases account used in a periodic inventory system which represents the amounts of merchandise that were returned to suppliers and the amounts allowed as deductions by suppliers for goods not returned. When the credit balance of this account is combined with the other purchases accounts, the result is the amount of net purchases.

purpose restriction

One of the types of donor-imposed temporary restrictions. An example of a purpose restriction is a cash donation with a donor-imposed requirement that the money be used only to purchase a vehicle for one of its programs.

PV

Present value.

Accounting Terms (Q)

qualitative characteristics

In accounting the qualitative characteristics include relevance, reliability, comparability, and consistency. Qualitative characteristics are discussed in the Financial Accounting Standards Board's *Statement of Financial Accounting Concepts No. 2*.

quality of earnings

Earnings are said to be of a high quality if the accounting policies are conservative. One indication is that the cash flows from operating activities shown on the statement of cash flows consistently exceed the amount of net income shown on the income statement.

quantity variance

In standard costing, the quantity variance could be the direct materials' usage variance or the direct labor's efficiency variance. The quantity variance is the difference between the quantity of inputs that were actually used versus the quantity of inputs that should have been used to manufacture the period's output.

quarterly earnings

A corporation's reported net income and earnings per share for a three-month period.

quick assets

Assets such as Cash, Temporary Investments, and Accounts Receivable.

QuickBooks

The leading accounting and bookkeeping software for small businesses in the United States. QuickBooks is the registered trademark of Intuit Inc.

quick ratio

Also known as the acid test ratio. This ratio compares the amount of cash + marketable securities + accounts receivable to the amount of current liabilities. To learn more, see Explanation of Financial Ratios.

Accounting Terms (R)

r

The statistic known as the **coefficient of correlation**. The range of this statistic is -1 to +1. When this statistic is squared the result is the percentage change in the dependent variable y that is explained by the independent variable x.

r squared

A statistic known as the **coefficient of determination**. This statistic indicates the percent change in the dependent variable that is explained by the change in the independent variable(s).

R & D

See research and development costs.

R. Smith, Capital at Beginning of Year

The owner's equity account that contains the amount invested in the sole proprietorship by R. Smith plus the net income since the company began minus the draws made by R. Smith since the company began. The current year net income might be in the temporary revenue and expense accounts and the current year draws might be in the drawing account. However, after the financial statements for the year are prepared the current year net income and draws will be transferred to this account.

R. Smith, Current Year Net Income

The net amount of revenues and gains minus expenses and losses for the current year for the sole proprietorship owned by R. Smith. After the financial statements are prepared for the year, this amount will be transferred to R. Smith, Capital.

R. Smith, Drawing

This contra owner's equity account has a debit balance that represents the current year draws made by the sole proprietor, R. Smith. After the year's financial statements have been prepared, the balance in this account will be transferred to R. Smith, Capital.

ratio analysis

To learn more, see Explanation of Financial Ratios.

raw materials inventory

See direct materials inventory.

real account

Also known as a permanent account. Includes the balance sheet accounts (assets, liabilities, and owner's or stockholders' equity accounts) but excludes the owner's drawing account, which is a temporary account.

receipts

Cash received. Receipts are different from revenues.

receiving report

A document that indicates the quantity of goods received. This report is often matched in the accounts payable department with the purchase order and the vendor's invoice prior to paying the vendor.

reciprocal method

A technique using simultaneous equations to allocate a manufacturer's service departments' costs to both other service departments and to production departments.

reciprocal services

The situation where manufacturing service departments provide service to each other. For example, the factory maintenance department provides services to the factory administrative department and the factory administrative department provides services to the factory maintenance department.

reconciliation of bank statement

To learn more, see Explanation of Bank Reconciliation.

record date

The date that determines which stockholders are entitled to receive a corporation's declared dividend. No accounting entry is made on this date.

redemption of bonds payable

The repurchase of bonds by the issuer of the bonds.

regression analysis

A statistical tool that uses the least-squares method to estimate the fixed and variable components of mixed costs.

regression line

The best fitting line through a series of points as determined by the least-squares method.

relative sales value method of allocating cost

The allocation of common costs based on the sales value of the products that emerge. For example, a company develops a large parcel of land at a cost of $5 million dollars. Individual lots will be sold for $100,000 to $300,000. A reasonable way to allocate the $5 million of common cost is on the basis of each lot's expected selling price. As a result a $300,000 lot will have three times the cost allocated to it as will a $100,000 lot. This method will also result in a relatively uniform gross profit percentage on each lot sold.

relevance

A qualitative characteristic in accounting. Relevance is associated with information that is timely, useful, has predictive value, and is going to make a difference to a decision maker.

relevant cost

A current or future cost that will differ among alternatives. For example, if a company is deciding whether to expand its sales territory, the real estate tax and depreciation on the company's headquarters building is not relevant. The additional travel expenses to the new territory and the additional sales from the new territory are relevant to the decision.

relevant range

Usually used in describing fixed costs. We often state that fixed costs will not change as volume changes. However, if volume were to triple, there would likely be more fixed costs as the company will need more space and managers. Accordingly, we state that costs are fixed only in a relevant or reasonable range of activity.

reliability

A qualitative characteristic in accounting. It is achieved when information is verifiable, objective (not subjective) and you can depend on it.

reliable

Verifiable, objective (not subjective), and you can depend on it.

rent expense

Under the accrual basis of accounting, the account Rent Expense will report the cost of occupying space during the time interval indicated in the heading of the income statement, whether or not the rent was paid within that period. (Rent that has been paid in advance is shown on the balance sheet in the current asset account Prepaid Rent.) Depending upon the use of the space, Rent Expense could appear on the income statement as part of administrative expenses or selling expenses. If the rented space was used to manufacture goods, the rent would be part of the cost of the products produced.

rent revenue/income

Under accrual accounting it is the rent *earned* during the period indicated in the heading of the income statement, regardless of when the money is received from the tenant.

reorder point

The quantity on hand that will trigger an order to buy more items. A company's reorder point for Product X might be 80 units. When the quantity on hand gets down to 80, a purchase order is prepared to obtain more of these items.

repairs

Operating expenses made to return an asset to its previous condition (rather than to make the asset more than it was originally). The amount is charged to an account such as Repairs and Maintenance Expense in the period when the repair is made.

repairs and maintenance expense

The costs incurred to bring an asset back to an earlier condition or to keep the asset operating at its present condition (as opposed to improving the asset). For example, if a company truck is damaged, the cost to repair the damage is immediately debited to repairs and maintenance expense. Routine maintenance such as engine tune-ups, oil changes, radiator flushing, etc. is also debited to repairs and maintenance expense. (If an expenditure is made to improve the truck, such as adding a hydraulic lift to the truck or if an expenditure is a major repair that extends an asset's useful life, the amount is not expensed immediately; rather, the amount is recorded as an asset and is then depreciated over the truck's remaining useful life.)

replacement cost

The amount needed to replace an asset such as inventory, equipment, buildings, etc. If an asset's replacement cost is greater than the asset's carrying amount, the cost principle prohibits the use of the replacement costs in the financial statements distributed by a company. However, economists and decision makers believe that replacement cost is more relevant than the historical cost.

replenish

A term associated with petty cash. Replenish means to return the amount of actual cash in the petty cash box back to the amount appearing in the general ledger account Petty Cash. This is done whenever the amount of actual cash in the petty cash box is low and at the end of each accounting period. A check is written on the company's main checking account for the needed amount. This will be a credit to Cash. The petty cash vouchers (receipts, documentation) determine the general ledger accounts to be debited. Any difference in the amounts of debits and credits goes to the income statement account Cash Short and Over.

replenishing petty cash

See petty cash replenishment.

required rate of return

A term used in evaluating business investments. It represents the targeted rate that a company needs to earn. It is also referred to as the discount rate, because this rate is used to discount the future cash flows to the present value.

research and development costs

R & D costs. These are costs incurred to develop new products or processes that may or may not result in commercially viable items. The general rule is that research and development costs are to be expensed immediately when the costs are incurred.

residual

An amount remaining after another amount is subtracted. In the accounting equation, owner's equity is the residual of assets minus liabilities.

residual income (RI)

A division's operating income after deducting a charge for the cost of the corporation's capital being used by the division.

residual value

The remainder or difference. In depreciation the residual value is the estimated scrap or salvage value at the end of the asset's useful life. In the accounting equation, owner's equity is considered to be the residual of assets minus liabilities. In investment evaluations, the residual value is the profit minus the cost of capital.

restricted accounts

Accounts that have some restrictions. For example, an investment account and a cash account might be restricted for the construction of a new factory. The restrictions mean that these accounts be reported as a long-term asset, since the funds can only be used for the building and are not available for working capital purposes.

Another example is the restriction of retained earnings. This restriction will prohibit dividends from being declared from the restricted portion.

restricted cash

Cash that can be used only for the purpose intended.

restricted retained earnings

Retained earnings not available for dividends.

restricted support

Support that has been either temporarily or permanently restricted by the donor.

retail method of estimating inventory

A method for estimating the inventory of a retailer. This method requires that the retail amounts and the related cost amounts are available for beginning inventory and purchases. An illustration of this technique is available near the end of the Explanation of Inventory and Cost of Goods Sold. Intermediate accounting textbooks and accounting professionals will provide more of the complexities involving markdowns, discounts to employees, etc.

retained earnings

A stockholders' equity account that generally reports the net income of a corporation from its inception until the balance sheet date less the dividends declared from its inception to the date of the balance sheet.

retained earnings statement

A financial statement that reports the current year information contained in the general ledger account Retained Earnings. The statement will include the beginning balance, prior period adjustments, net income for the current period, dividends declared in the current period, and the ending balance. Also see statement of stockholders' equity and statement of retained earnings.

retirement of assets

Usually means to scrap a long-term plant asset and receive no proceeds from its disposal.

retirement of bonds

To repurchase bonds that the company had previously issued.

return on average common stockholders' equity

See return on stockholders' equity.

return on capital employed

A measurement of financial performance of a company's operating division that is not responsible for its financing and income taxes. The calculation is likely to be 1) the division's operating income before interest and income taxes divided by 2) the division's assets employed.

return on investment (ROI)

A financial ratio that expresses the income statement effect from employing an asset as a percentage of the asset's cost on the balance sheet.

return on stockholders' equity

The result of dividing a corporation's net income by the average amount of common stockholders' equity during the time interval when the net income was earned. To learn more about this ratio, see Explanation of Financial Ratios.

returned check

A check that is not paid by the bank on which it is written (drawn). Often the reason a check is not paid is that the account on which the check was drawn did not have a sufficient balance. In that case the check is returned as "NSF" or not sufficient funds. A check could also be returned unpaid because the account was closed or due to a stop payment order requested by the maker of the check.

revenue expenditure

An amount that is expensed immediately. For example, routine repair costs on equipment are revenue expenditures because they are charged directly to an income statement account such as Repairs and Maintenance Expense.

revenue recognition principle

The accounting guideline requiring that revenues be shown on the income statement in the period in which they are earned, not in the period when the cash is collected. This is part of the accrual basis of accounting (as opposed to the cash basis of accounting).

revenues

Fees earned from providing services and the amounts of merchandise sold. Under the accrual basis of accounting, revenues are recorded at the time of delivering the service or the merchandise, even if cash is not received at the time of delivery. Often the term *income* is used instead of revenues.

Examples of revenue accounts include: Sales, Service Revenues, Fees Earned, Interest Revenue, Interest Income. Revenue accounts are *credited* when services are performed/billed and therefore will usually have credit balances. At the time that a revenue account is credited, the account debited might be Cash, Accounts Receivable, or Unearned Revenue depending if cash was received at the time of the service, if the customer was billed at the time of the service and will pay later, or if the customer had paid in advance of the service being performed.

If the revenues earned are a main activity of the business, they are considered to be operating revenues. If the revenues come from a secondary activity, they are considered to be nonoperating revenues. For example, interest earned by a manufacturer on its investments is a nonoperating revenue. Interest earned by a bank is considered to be part of operating revenues. To learn more, see Explanation of Income Statement.

revenues and gains

This is the classification shown on a single-step income statement which reports the operating revenues, nonoperating revenues, and gains in one section of the income statement. Revenues and gains enhance the owner's equity.

revenues from service charges

An income statement account at a financial institution used to record and report the amounts earned from fees charged to customers.

reversing entry

A journal entry made on the first day of a new accounting period to undo the accrual type adjusting entries made prior to the preparation of the financial statements dated one day earlier. Reversing entries allow for an effortless way to avoid double-counting revenues or expenses that were accrued at the end of an accounting period.

revision of depreciation estimates

Usually a change in the estimated useful life of an asset or a change in the estimated salvage value. The change usually causes a change in the depreciation expense for the current year and subsequent years. The depreciation expense of previous years is not changed.

RI

See residual income (RI).

Robert Morgan, Capital

An owner's equity account that reports the amount the sole proprietor invested in the company plus earnings of the company not withdrawn by the owner.

ROCE

See return on capital employed.

ROI

See return on investment (ROI).

rolling budget

A rolling budget adds a future accounting period's budget to replace a budget for an accounting period that has past. For example, a company's 2024 annual budget will become a rolling budget if in February 2024 it adds the budget for January 2025 to replace the January 2024 budget. At that point the rolling budget will cover February 1, 2024 through January 31, 2025. After February 2024 occurs, the rolling budget will consist of the 12 monthly budgets of March 2024 through February 2025.

The rolling budget is also referred to as a rolling horizon budget, a continuous budget, or a perpetual budget.

rolling horizon budget

A budget that continuously shows the amounts for a full year into the future. As a month or quarter actually occurs, it is removed from the budget and is replaced by the budgeted amounts for a month or quarter in the future.

root cause

The underlying true cause of a cost occurring. In other words, the root cause is more than a mere correlation between an event and a cost. There is a real cause and effect relationship.

rubber check

See not sufficient funds check.

rule of 72

A technique for estimating the number of years or the interest rate necessary to double your money. Divide 72 by the interest rate and you will have the approximate number of years needed to double your money. If your money earns 4%, your money will double in 18 years (72 divided by 4). If you earn 8%, your money will double in 9 years (72 divided by 8).

Accounting Terms (S)

safety stock

An additional quantity of items held in inventory in order to minimize the chance of an item being out of stock.

salaried employee

A person whose pay is based on an annual amount (instead of being based on an hourly rate of pay multiplied by actual hours worked). For example, the officers of a corporation and the heads of departments within a company will likely be salaried employees. (On the other hand, production workers are likely to be paid an hourly wage rate for the hours worked.)

salaries expense

Under the accrual method of accounting, the account Salaries Expense reports the salaries that employees have earned during the period indicated in the heading of the income statement, whether or not the company has yet paid the employees. Salaries Expense will usually be an operating expense (as opposed to a nonoperating expense). Depending on the function performed by the salaried employee, Salaries Expense could be classified as an administrative expense or as a selling expense. If the employee was part of the manufacturing process, the salary would end up being part of the cost of the products that were manufactured.

salaries expense: delivery department

Under the accrual method of accounting, the account Salaries Expense - Delivery Dept reports the salaries that the employees in the delivery department have earned during the period indicated in the heading of the income statement, whether or not the company has paid the employees during this time period.

salaries expense: selling & admin department

Under the accrual method of accounting, the account Salaries Expense - Selling & Admin Dept reports the salaries that the employees in the selling and administrative department of the company have earned during the period indicated in the heading of the income statement, whether or not the company has paid the employees during this time period.

salaries payable

The current liability account which reports the amount of salaries earned by a company's employees, but which have not yet been paid by the company.

salary

The compensation usually associated with executives, managers, professionals, office employees, etc. whose pay is stated on an annual or on a monthly basis. (On the other hand, "wages" is usually associated with employees whose pay is stated on an hourly basis.) To learn more, see Explanation of Payroll Accounting.

salary and fringes

A phrase used to communicate the total compensation of a salaried employee. Fringe benefits (health insurance, vacation days, sick days, employer matching of Social Security and Medicare taxes, pension or 401-k contributions, etc.) are often a significant percentage of a person's salary.

sales

A revenue account that reports the sales of merchandise. Sales are reported in the accounting period in which title to the merchandise was transferred from the seller to the buyer.

sales allowance

An allowance granted to a customer who had purchased merchandise with a pricing error or other problem not involving the return of goods. If the customer purchased on credit, a sales allowance will involve a debit to Sales Allowances and a credit to Accounts Receivable.

sales commissions expense

A selling expense account shown on the income statement in order to match this expense to the related sales.

sales discounts

A contra revenue account that reports the discounts allowed by the seller if the customer pays the amount owed within a specified time period. For example, terms of "1/10, n/30" indicates that the buyer can deduct 1% of the amount owed if the customer pays the amount owed within 10 days. As a contra revenue account, sales discount will have a debit balance and is subtracted from sales (along with sales returns and allowances) to arrive at net sales.

sales forecast

A projection or estimate of the future quantities and selling prices of products and/or services.

sales journal

A special or specialized journal to record sales of merchandise to customers. In a manual system this saves a significant amount of recording time. In today's computerized environment, sales are recorded automatically when the sales invoice is generated.

sales mix

The proportion of products sold. For example, if a car company sells 100,000 low-profit cars and 400,000 medium-profit cars and 500,000 high-profit trucks, it has a sales mix of 10% + 40% + 50%. If the total number of units sold remains at 1,000,000 but the sales mix changes so that more of the low-profit cars are sold and fewer of the high-profit trucks are sold, the company's profits will be significantly less.

sales returns

Merchandise that was returned to the seller by a customer. This account is a contra sales account. When merchandise sold on credit is returned, this account is debited and Accounts Receivable is credited.

sales returns and allowances

A contra revenue account that reports 1) merchandise returned by a customer, and 2) the allowances granted to a customer because the seller shipped improper or defective merchandise. This of course will reduce the seller's accounts receivable and is subtracted from sales (along with sales discounts) to arrive at net sales.

sales revenues
See sales.

salvage value of fixed assets
The estimated scrap value at the end of the useful life of an asset used in the business. It is also referred to as residual value.

scattergraph
A plotting of points that represent both the volume and the associated cost. The y-axis indicates the amount of costs while the x-axis indicates the corresponding volumes.

SCF
Statement of Cash Flows. To learn more, see Explanation of Cash Flow Statement.

SEC
See Securities and Exchange Commission.

secondary activities
Also referred to as peripheral activities. A company's activities outside of its main activities of buying/producing and selling. Examples include a retailer's financing function involving interest revenue and interest expense, disposal of long term assets used in the business, lawsuit settlements, renting out unused space, etc.

secured bond
A bond with collateral.

secured creditor
A lender such as a bank who has placed a lien on a borrower's assets. As a result, the lender has collateral until the loan amount is repaid.

secured loan
A loan from a bank or other lender in which the borrower has pledged an asset as collateral in case the loan cannot be repaid in full.

Securities and Exchange Commission
Usually referred to as the SEC. The U.S. government agency which has regulatory power over the U.S. stock exchanges and the reporting requirements of the corporations whose stock is traded on those stock exchanges. The SEC relies on the Financial Accounting Standards Board, a non-government organization, to develop many of the accounting rules.

segregation of duties
See separation of duties.

self-employed

A person who is considered to be both the employer and the employee. For example, the sole owner of a sole proprietorship is self-employed.

self insurance

No insurance. If a company chooses to self insure for fire damage, it does not have insurance for fire damage. Companies with a chain of stores in various cities may decide not to have insurance, since their risk is spread over many stores in many locations.

selling and administrative expense

Also referred to as operating expenses. These expenses are reported in the period in which they were incurred, not the period in which they were paid.

selling expenses

Selling expenses are part of the operating expenses (along with administrative expenses). Selling expenses include sales commissions, advertising, promotional materials distributed, rent of the sales showroom, rent of the sales offices, salaries and fringe benefits of sales personnel, utilities and telephone usage in the sales department, etc.

Under the accrual basis of accounting, selling expenses appear on the income statement in the period in which they occurred (not the period in which they were paid).

selling, general and administrative expenses

Also referred to as SG&A. For a manufacturer these are expenses outside of the manufacturing function. (However, interest expense and other nonoperating expenses are not included; they are reported separately.) These expenses are not considered to be product costs and are not allocated to items in inventory or to cost of goods sold. Instead these expenses are reported on the income statement of the period in which they occur. These expenses are sometimes referred to as operating expenses.

semimonthly

Occurring twice per month. For example, if salaried personnel are paid on the 15th and the last day of the month, we would say they are paid semimonthly. People paid semimonthly will receive 24 paychecks during a year. (People paid every two weeks—such as every other Thursday—are said to be paid biweekly and will receive 26 paychecks during the year). Also see mixed costs.

semivariable costs

See mixed expenses.

semivariable expenses

See mixed expenses.

separation of duties

One of the steps in effective internal control. An example of separation of duties is to have the money handling be performed by someone who does not update the records. This means that the money counters at a church need to be different from the person who updates the church members' donation records. Requiring that two people be involved in a process instead of only one greatly reduces the odds of employee theft.

serial bond

A bond issued with a series (or staggering) of maturity dates.

service charge revenues

A revenue account in a bank's general ledger that indicates the amounts earned by the bank by servicing its customers' accounts at the bank.

service department

See production service department.

service mark

A trademark associated with a service rather than a product.

service revenues

Under the accrual basis of accounting, the Service Revenues account reports the fees earned by a company during the time period indicated in the heading of the income statement. Service Revenues include work completed whether or not it was billed. Service Revenues is an operating revenue account and will appear at the beginning of the company's income statement.

setup cost

The cost associated with setting up a piece of production equipment. This would include the cost of the setup mechanic, the cost of scheduling, record keeping, moving the starting material, and testing the first few units of output to be certain the equipment is set up properly.

setup time

The time required to set up a piece of production equipment.

SFAS

See Statement of Financial Accounting Standards.

SG&A

See selling, general and administrative expenses.

shareholder

See stockholder.

shareholders' equity

See stockholders' equity.

short-term asset
See current asset.

short-term liability
See current liabilities.

shrinkage
See inventory shrinkage.

simple journal entry
An accounting entry with only one account being debited and only one account being credited.

simple regression
Regression analysis with only one independent variable.

single payment
A term often used in present value calculations to distinguish a one-time cash amount from an annuity (or series of equal payments).

single-step income statement
The income statement format where the operating and nonoperating revenues are grouped and totaled and the operating and nonoperating expenses are grouped and totaled. Then there is one subtraction of the combined expenses from the combined revenues. An alternative format is the multiple-step income statement.

sinking fund
See bond sinking fund.

slope of cost line
Within a reasonable range of activity, the slope of the cost line is the variable rate, which is often denoted as "b" in the straight line y = a + bx.

Social Security taxes
One component of the payroll tax referred to as FICA. (The other component of the FICA tax is the Medicare tax.) The Social Security tax is levied by the U.S. government on both the employee and the employer. In 2024 the Social Security portion of FICA (excluding Medicare) to be withheld from the first $168,600 of each employee's annual salary or wages is 6.2%. In addition, the employer incurs Social Security expense of 6.2% and as a result must remit 12.4% of the first $168,600 of each employee's salary or wages. (Medicare taxes are an additional 1.45% for both the employee and the employer on every dollar of salary and wages plus there is a Medicare surtax, which you can learn about on IRS.gov.) To learn more, see Explanation of Payroll Accounting.

sold

Transfer of an asset's title from seller to buyer for a stated amount. The transfer/sale occurs at the shipping point (if terms are FOB shipping point), at the time when the item reaches the destination (if terms are FOB destination), or at some other agreed upon terms.

sole practitioner

A certified public accountant (CPA) who practices accounting in his or her own firm without another CPA as a partner or shareholder.

sole proprietorship

A simple form of business where there is one owner. Legally the owner and the sole proprietorship are the same. However, for accounting purposes the economic entity assumption results in the sole proprietorship's business transactions being accounted for separately from the owner's personal transactions.

source document

An original record containing the details to substantiate a transaction entered in an accounting system. For example, the source document for a purchase of merchandise is the supplier's invoice supported by the company's purchase order and a receiving ticket.

special journals

Journals other than the general journal. Special or specialized journals include the cash receipts journal, the cash disbursements journal, the purchases journal, and the sales journal.

spending variance

See variable manufacturing overhead spending variance and fixed manufacturing overhead budget variance. To learn more, see Explanation of Standard Costing.

split-off point

The point at which several products emerge from a common process.

spoilage

Waste, scrap, evaporation, etc. in the manufacturing of products. Normal spoilage is considered unavoidable and is part of the cost of producing the good output. Abnormal spoilage is considered avoidable and is not part of the cost of producing good output. The cost of abnormal spoilage should be expensed when it occurs.

spot price

The current price for a commodity or other item to be delivered immediately.

stage 1 allocation

In activity-based costing this refers to the allocation of costs to activities. For example, allocating the costs of setting up the manufacturing equipment to run a batch of product to the activity "setup costs" is a stage 1 allocation. This stage 1 cost is then allocated to cost objects such as a product or service. See stage 2 allocation.

stage 2 allocation
In activity-based costing this refers to the allocation of the cost of activities (determined by stage 1 allocations) to the cost objects such as products or services.

stakeholder
A stakeholder is anyone that has an interest or is affected by a decision. For example, some of the stakeholders of a state university include the students, students' families, alumni, professors, custodians, taxpayers, and the local community.

standard cost
The planned or expected costs. Often used in manufacturing for accounting for inventories and production. When actual costs differ from the standard costs, variances are reported. To learn more, see Explanation of Standard Costing.

standard cost per unit of input
A predetermined dollar amount that a pound of material or an hour of labor should cost during an accounting period.

standard cost per unit of product
A predetermined dollar amount that one unit of a finished product should cost during an accounting period.

standard cost system
To learn more, see Explanation of Standard Costing.

standard cost variances
To learn more, see Explanation of Standard Costing.

standard costing
See standard cost system.

state boards of accountancy
See boards of accountancy.

state income tax withholdings payable
This current liability account reports the amount a company owes the state governments as of the balance sheet date for the state income taxes withheld from its employees' salaries and wages.

state unemployment tax
Taxes assessed by states to cover unemployment benefits paid to unemployed workers who have been laid off or terminated by a company for specified reasons. This tax is paid by the employer but is computed by multiplying a percentage times the first $7,000 to $30,000+ (varies by state) of each employee's annual wages. To learn more, see Explanation of Payroll Accounting.

statement of activities

One of the main financial statements of a nonprofit organization. This financial statement reports the revenues and expenses and the changes in the amounts of each of the classes of net assets during the period shown in its heading. This statement is issued by a nonprofit instead of the income statement issued by a for-profit business. To learn more, see our Explanation of Nonprofit Accounting.

statement of cash flows

One of the main financial statements (along with the income statement and balance sheet). The statement of cash flows reports the sources and uses of cash by operating activities, investing activities, financing activities, and certain supplemental information for the period specified in the heading of the statement. The statement of cash flows is also known as the cash flow statement. To learn more, see Explanation of Cash Flow Statement.

statement of comprehensive income

The statement of comprehensive income covers the same period of time as the income statement, and consists of two major sections:

- *Net income* (taken from the income statement)
- *Other comprehensive income* (adjustments involving foreign currency translation, hedging, and postretirement benefits)

The sum of these two amounts is known as *comprehensive income*.

The amount of *other comprehensive income* is added/subtracted from the balance in the stockholders' equity account Accumulated Other Comprehensive Income.

statement of financial accounting standards

The title of the official pronouncement of the Financial Accounting Standards Board which establishes a new accounting standard.

statement of financial position

One of the main financial statements of a nonprofit organization. This financial statement reports the amounts of assets, liabilities, and net assets as of a specified date. This financial statement is similar to the balance sheet issued by a company. To learn more, see our Explanation of Nonprofit Accounting.

statement of functional expenses

One of the financial statements issued by a nonprofit organization which reports expenses according to both function and nature. To learn more, see our Explanation of Nonprofit Accounting.

statement of income

See income statement. To learn more, see Explanation of Income Statement.

statement of operations

See income statement. To learn more, see Explanation of Income Statement.

statement of retained earnings

A statement that shows the changes in retained earnings from one point to another.

statement of stockholders' equity

A financial statement that shows all of the changes to the various stockholders' equity accounts during the same period(s) as the income statement and statement of cash flows. It includes the amounts of comprehensive income not reported on the income statement.

static budget

A budget that does not flex for changes in volume or activity.

stock certificate

Paper evidence of ownership in a corporation. The certificate would indicate the type of stock (common, preferred), any restrictions pertaining to the sale of the stock, the number of shares, the par value, etc. Today, the larger corporations with many shareholders are likely to use electronic records instead of issuing the paper stock certificates.

stock dividend

A dividend in the form of more shares of stock. A 5% stock dividend means that a stockholder holding 100 shares would receive 5 additional shares of stock. Since all shareholders receive additional shares, each shareholder's percentage of ownership is unchanged. In theory the market value per share should drop since there are now 5% more shares outstanding and the company is exactly the same as before the stock dividend.

stock option

A right to buy a specific number of shares of stock at a specific price by a specific date.

stock split

A stock split, such as a 2-for-1, means that every stockholder will have twice as many shares as was held previously. Accordingly, the market price per share after the split should be one-half of the market price existing prior to the stock split. The main reason for a stock split is to reduce the market price per share of stock.

stockholder

Also referred to as a shareholder. The owner of shares of stock in a corporation. Every corporation has common stock and those owners are known as common stockholders. Some corporations also issued preferred stock and those corporations will have both common stockholders and preferred stockholders.

stockholders' equity

Also referred to as shareholders' equity. At a corporation it is the residual or difference of assets minus liabilities.

stop payment order

A directive to a company's bank to not honor (pay) a specific check that the company had written. The company making the request will be charged a fee by the bank for this service.

stores

A part of a manufacturer's inventory that includes direct and indirect materials. Also see inventory: materials.

straight-line method of amortization

Systematically moving the same amount each accounting period from a balance sheet account to an income statement account. For example, if the amount of Discount on Bonds Payable on a 10-year bond is not significant, then each year 1/10 of the original amount of discount will be debited to Bond Interest Expense and credited to Discount on Bonds Payable each year. If the amount of discount is significant, the effective interest method of amortization should be used.

straight-line method of depreciation

The depreciation method that results in the same equal amount of depreciation expense for each full year over the life of the asset. See Explanation of Depreciation for an illustration and further discussion of depreciation.

Subchapter S corporation

A tax status allowed by the U.S. Internal Revenue Service.

subsequent event

See post balance sheet event.

subsidiary accounts

The accounts outside of the general ledger which provide the detail for the balance reported in a general ledger account. (The account in the general ledger is known as the control account.) For example, each credit customer's account balance is contained in a subsidiary account or record. The total of the subsidiary accounts or records must agree to the balance in Accounts Receivable, the general ledger control account.

subsidiary ledger

A record of the details to support a general ledger account. The general ledger account is often referred to as the control account. For example, the accounts receivable subsidiary ledger provides the details to support the balance in the general ledger control account Accounts Receivable.

sum-of-the-years' digits (SYD) method of depreciation

A form of accelerated depreciation which means that in the early years of an asset's life there is more depreciation expense than under the straight-line method. However, in the later years of the asset's life there will be less depreciation than the straight-line method.

sunk cost

A past, historical cost. They are called sunk because a past cost cannot be changed and decisions involve only the present and the future.

supplier

The provider of goods or services. Also known as the vendor.

supplier invoice

The sales invoice or bill issued by a vendor and received by the buyer. The customer will also refer to the supplier invoice as the vendor invoice.

supplies

A current asset representing the cost of supplies on hand at a point in time. The account is usually listed on the balance sheet after the Inventory account.

A related account is Supplies Expense, which appears on the income statement. The amount in the Supplies Expense account reports the amounts of supplies that were used during the time interval indicated in the heading of the income statement.

supplies expense

Under the accrual basis of accounting the account Supplies Expense reports the amount of supplies that were used during the time interval indicated in the heading of the income statement. Supplies that are on hand (unused) at the balance sheet date are reported in the current asset account Supplies or Supplies on Hand.

supplies on hand

See Supplies.

supporting services expenses

One of two broad functional categories for sorting and reporting a nonprofit organization's expenses. (The other is program expenses.) Supporting services expenses consists of 1) management and general expenses, and 2) fundraising expenses.

surrender value

See cash surrender value.

suspense account

A temporary holding place for amounts that need further analysis.

SYD depreciation method

See sum-of-the-years' digits method of depreciation.

systematic expensing

A phrase used in depreciation and amortization to indicate that the expense is being allocated on a logical basis (because a cause and effect relationship does not exist).

Accounting Terms (T)

T-account

A visual aid used by accountants to illustrate a journal entry's effect on the general ledger accounts. Debit amounts are entered on the left side of the "T" and credit amounts are entered on the right side.

take-home pay

The amount an employee "clears" on her or his payroll check. It is also the "net" amount: the gross salary or wages minus the withholdings/deductions for payroll taxes and voluntary deductions for union dues, employee share of health care costs, charitable deductions, garnishments, etc.

tangible constructed asset

Assets associated with depreciation. Examples include buildings, equipment, furniture, fixtures, trucks, automobiles, etc.

target interest rate

See hurdle rate.

tax depreciation

The depreciation used on a company's income tax return. Usually this is different from the depreciation used on the financial statements.

tax-exempt

A status granted by the U.S. Internal Revenue Service (IRS) to nonprofits applying and meeting certain conditions. This status means that the nonprofit organization is not subject to federal income taxes. It also means the donors' contributions may be income tax deductible.

taxes payable

A liability account that reports the amount of taxes that a company owes as of the balance sheet date.

telephone expense
The cost of telephone service that was *used* during the period shown on the income statement.

temporarily restricted net assets
This classification of net assets has been replaced by the FASB with the classification *net assets with donor restrictions*.

temporary accounts
Accounts that are closed at the end of each accounting year. Included are the income statement accounts (revenues, expenses, gains, losses), summary accounts (such as income summary), and a sole proprietor's drawing account.

temporary help expense
The amount of temporary staffing costs that were *used* during the time interval indicated in the heading of the income statement.

temporary investments
A current asset account which contains the amount of investments that can and will be sold in the near future.

temporary marketable securities
Generally, securities that can be sold quickly in the stock or bond market and where the investor's intention is to sell them within one year of the balance sheet date.

temporary service expense
Under the accrual basis of accounting, this account reports the cost of the temporary help services that a company used during the period indicated on its income statement.

term bonds
Bonds with one maturity date (as opposed to serial bond).

term insurance
Life insurance without a cash value.

three-way match
A technique used when processing accounts payable in order to be certain that only legitimate bills and invoices are paid. Its name is derived from the matching of 1) the vendor invoice with 2) the company's receiving report, and 3) the company's purchase order.

time-and-a-half
Also known as **time-and-one-half**. A term used in conjunction with overtime pay when an employee gets a 50% higher pay rate for hours in excess of 40 hours per week. The "half" is also known as the overtime premium. For example, an employee earning $8 per hour is required to work 41 hours this week. The employee will earn $320 for the first 40 hours ($8 times 40) plus $12 (150% of $8) for the 41st hour—for a total of $332. The total can also be computed as 41

hours times the straight-time rate of $8 = $328 plus the $4 overtime premium (the half of $8)—for a total of $332. To learn more see Explanation of Payroll Accounting.

time deposits

Savings accounts and certificates of deposits at a bank.

time period assumption

Also known as the periodicity assumption. The accounting guideline that allows the accountant to divide up the complex, ongoing activities of a business into periods of a year, quarter, month, week, etc. The precise time period covered is included in the heading of the income statement, statement of cash flows, and the statement of stockholders' equity.

time restriction

A donor-imposed restriction on net assets that requires using the assets within a specified passage of time.

time value of money

The recognition that a dollar in the present is more valuable than a dollar in the future. Present-value calculators and present-value tables assist in converting future dollars to the present value in order to make a prudent decision. To learn more, see Explanation of Evaluating Business Investments.

times interest earned

A financial ratio that compares a company's interest expense to the company's income before interest expense and income taxes. It is an indicator of the likelihood that interest payments will be made in the future. To learn more, see Explanation of Financial Ratios.

timing differences

Temporary differences between the reporting of a revenue or expense for financial statements (books) and the reporting of the item for income tax purposes. For example, it is common for companies to depreciate equipment on the financial statements over a ten-year period using the straight-line method. However, for income tax purposes the company uses the IRS's seven-year, accelerated depreciation method. Eventually, the total depreciation will be the same; however, each year for ten years there will be differences due to the timing of the depreciation.

Tony Mandella, Capital

The owner's equity account that reports the amount invested in the sole proprietorship owned by Tony Mandella plus the cumulative amount of net income minus the cumulative amount of the sole proprietor's draws since the company was started. The current year's net income and draws are usually in temporary accounts and will be transferred to the capital account at the end of the year.

trade accounts payable

See accounts payable.

trade accounts receivable

Receivables due from customers. See accounts receivable.

trade discount

A discount that often varies by customer. For example, a company may sell its products to a variety of resellers. Some of the resellers might buy $1 million of products each year, other resellers might purchase $100,000, and still others buy less than $10,000 per year. The company would probably have lower selling prices for the large-volume resellers and have higher selling prices for the low-volume resellers. One way to achieve this is to have a catalog showing just one selling price for each item, but to offer discounts that vary with the volume purchased. That discount is known as a trade discount.

trade-in of similar asset

See exchange of similar nonmonetary assets.

trademark

An intangible asset that is reported at cost (or lower) on the balance sheet. It might consist of a name or a logo. Trademarks should be registered with the U.S. Patent and Trademark Office. Also see trade names.

trade names

An intangible asset reported on the balance sheet at the company's cost (or lower). Often, successful trade names were developed by companies over many years. As a result the cost of the trade name is minimal, but the trade names are often the most valuable assets of the company. Trade names should be registered with the U.S. Patent and Trademark Office.

trade payables

Payables arising from the purchase of merchandise inventory and outside services. See accounts payable.

trade receivables

Receivables due from customers. See accounts receivable.

traditional costing

The allocation of manufacturing overhead (indirect manufacturing costs) to products on the basis of a volume metric such as direct labor hours or production machine hours. As manufacturing becomes more sophisticated the manufacturing overhead costs usually increase while the direct labor hours or production machine hours decrease. Hence, the direct labor or machine hours are unlikely to be the root cause of the manufacturing overhead.

Activity based costing (ABC) has developed as a technique to overcome the shortcomings of traditional costing.

transaction approach to determining net income

Under this method a company records detailed transactions and reports its net income by summarizing and reporting these detailed transactions. (A different approach is called the capital maintenance approach which determines the amount of net income by examining the change in owner's equity from the beginning of the accounting period to the end of the accounting period.) Accounting follows the transaction approach.

transfer price

The price at which one division or subsidiary of a company transfers products to another division or subsidiary of the company.

transferred-in cost

The cost transferred from one department to the next department in a process costing system.

transportation-in

See freight-in.

transportation-out

Also known as freight-out or as delivery expense. This is an operating expense further classified as a selling expense. It results when merchandise is sold with terms of FOB destination.

treasury bills

See U.S. Treasury bills.

treasury stock

A corporation's own stock that has been repurchased from stockholders. Also a stockholders' equity account that usually reports the cost of the stock that has been repurchased.

trend analysis

Comparable amounts from several years are expressed as a percentage of the amount during a base year. For example, sales from each year of 2014 through 2023 are presented as a percentage of the sales during 2014.

trial balance

A listing of the accounts in the general ledger along with each account's balance in the appropriate debit or credit column. The total of the amounts in the debit column should equal the total of the amounts in the credit column.

triple net lease

A lease where the lessee/tenant pays not only rent, but also the property taxes, insurance, and maintenance.

turnover

In some countries *turnover* refers to sales.

Turnover is also associated with some financial ratios such as the inventory turnover ratio, the accounts receivable turnover ratio, and asset turnover ratio.

turnover ratios

A ratio consisting of an income statement account balance divided by the average balance of a balance sheet account. For example, the inventory turnover is computed as follows: Cost of Goods Sold divided by the average Inventory balance. The Accounts Receivable turnover is Sales divided by the average Accounts Receivable balance. To learn more, see Explanation of Financial Ratios.

Accounting Terms (U)

UBIT

See unrelated business income tax.

unadjusted trial balance

An internal accounting report that is prepared prior to recording the adjusting entries. Its purpose is to verify that the total amount of debit balances in the general ledger accounts is equal to the total amount of credit balances.

unamortized bond discount

A contra liability account containing the amount of discount on bonds payable that has not yet been amortized to interest expense. To learn more, see Explanation of Bonds Payable.

unamortized bond premium

A liability account containing the amount of premium on bonds payable that has not yet been amortized to interest expense. To learn more, see Explanation of Bonds Payable.

unappropriated retained earnings

The regular retained earnings. Retained earnings that have not been restricted.

uncleared check

A check that has been issued but has not yet been paid by the bank on which it is drawn. An uncleared check is also known as an outstanding check.

uncleared cheque

See uncleared check.

uncollected funds

The amounts in a company's bank account that are not yet accessible because the checks deposited into the account have not yet cleared the bank on which they were drawn.

uncollectible accounts expense

See Bad Debts Expense.

undeposited checks

Checks received from customers and others that are not yet deposited into a bank account. Undeposited checks which are not postdated are reported as part of a company's cash.

underabsorbed

The term used by manufacturers to indicate that its manufacturing overhead applied or assigned to its output is less than the amount actually incurred.

underapplied manufacturing overhead

The situation where a company has assigned less manufacturing overhead than the amount actually incurred.

underlying principles/guidelines

The basic general rules upon which more detailed accounting standards are built. To learn more, see Explanation of Accounting Principles.

understates

Reports too little. If an error understates the inventory and the company's net income, the amount of inventory and the amount of net income being reported are less than the correct amounts.

underwriter

In securities, a party that assists a company in issuing stock or bonds.

undiscounted future cash flows

Future cash amounts that have not been discounted to their present value.

unearned premium revenue

A liability account that reports an insurance company's premiums received from its insured that have not yet been earned. For example, if the insurance company receives $600 on January 27 for an insured's insurance coverage for the period of February 1 through July 31, the $600 has not been earned as of January 31. The insurance company will report the $600 in its Cash account and should report $600 as a current liability in the account Unearned Premium Revenue. As the premium is earned, the insurance company will move the amount earned from the liability account to a revenue account on its income statement.

unearned revenue(s)

A liability account that reports amounts received in advance of providing goods or services.

When the goods or services are provided, this account balance is decreased and a revenue account is increased. To learn more, see Explanation of Adjusting Entries.

unemployment compensation tax

A tax usually paid by the employer based on the first $7,000 to $30,000+ (varies by state) of each employee's annual salaries and wages. The majority of the tax is paid to the state, since the state administers the unemployment payments to employees whose work hours have been eliminated or greatly reduced. A small portion of the tax is paid to the federal government.

unemployment tax expense: warehouse

Under the accrual method of accounting, the account Unemployment Tax Expense on Warehouse reports the unemployment tax expense the company has incurred for the employees in the warehouse during the period indicated in the heading of the income statement, whether or not the company has paid the unemployment taxes during this time period.

unemployment tax payable

This current liability account reports the amount a company owes the state and federal governments as of the balance sheet date for the employer's unemployment tax based on the governments' rates and the company employees' salaries and wages.

unfavorable variance

The amount by which actual costs exceed the standard costs or budgeted costs. Also, the amount by which actual revenues are less than the budgeted revenues.

Uniform CPA Exam

See CPA Exam.

United Way payable

This current liability account reports the amount a company owes the United Way organization as of the balance sheet date. The amount includes the withholdings from employees' pay plus the amount owed by the employer.

units of activity method of depreciation

See units of production method of depreciation.

units of production method of depreciation

The depreciation method based on the number of units produced by the asset rather than on the passage of time. This method is also referred to as the units of activity method because depreciation is based on some activity rather than years of useful life. To learn more, see Explanation of Depreciation.

unpaid principal balance

The amount of principal owed on a loan. On the typical mortgage loan, a portion of the monthly payment is applied to interest and principal. The amount of principal that remains after the principal payment is the unpaid principal balance. The following month's interest is based upon this amount.

unpresented check

See outstanding checks.

unqualified opinion

A "clean" auditor's report. That is, the auditor has concluded that the financial statements present fairly the results of the company's operations and its financial position according to generally accepted accounting principles.

unrealized holding gain

A gain from holding an asset and the gain has not yet been reported in the financial statements. As an example, assume that a company purchased land many years ago and continues to hold the land. The land was purchased at a cost of $20,000 but is now appraised at $300,000. Because of the cost principle and the revenue recognition principle, the land will be reported at its cost of $20,000. The holding gain of $280,000 is not realized or reported until the company sells the land.

unrealized holding loss

A loss from holding an asset and the loss has not yet been reported in the financial statements.

unrelated business income tax

A tax imposed on income earned by a nonprofit that is unrelated to its exempt purpose.

unrestricted net assets

Prior to 2018, this term was used by a not-for-profit organization to describe net assets without donor-imposed restrictions. Since 2018, this term has been replaced with the classification *net assets without donor restrictions*.

unsecured bond

See debenture bond.

unsecured creditor

A lender or supplier who is owed money but does *not* have a lien on any of the assets of the company that owes the money. If the company that owes the money is liquidated, the unsecured lender receives money only after the secured lenders have been paid.

unsecured loan

A loan from a bank or other lender for which the borrower is not required to pledge assets as collateral for the loan.

US GAAP

The generally accepted accounting principles practiced in the United States.

U.S. treasury bills

Federal government securities sold at a discount (because of no interest payments) with maturity dates of less than one year.

U.S. treasury bonds

Federal government securities with a fixed interest rate and maturing in more than 10 years.

U.S. treasury notes

Federal government securities with a fixed interest rate and maturing in 10 years or less.

usage variance

See direct materials usage variance. To learn more, see Explanation of Standard Costing.

useful life

This is the period of time that it will be economically feasible to use an asset. Useful life is used in computing depreciation on an asset, instead of using the physical life. For example, a computer might physically last for 100 years; however, the computer might be useful for only three years due to technology enhancements that are occurring. As a consequence, for financial statement purposes the computer will be depreciated over three years.

utilities expense

Under the accrual basis of accounting, this account reports the cost of the electricity, heat, sewer, and water *used* during the period indicated in the heading of the income statement. Because utility companies deliver the service and then later measure the amounts used and then prepare the billing, a company's Utilities Expense amount should be based on the amount of utilities *used* during the period (as opposed to the amount paid during the accounting period). The amount of Utilities Expense for the sales function is classified as a selling expense and the amount used for administration is classified as an administrative expense. Utilities used in the manufacturing process will be part of the cost of the products manufactured.

utilities payable

A current liability account that reports the amounts owed to the utility companies for electricity, gas, water, phone as of the date of the balance sheet. If a utility bill has not been received, the company will have to estimate the amount owed for the service it has used up to the balance sheet date. Instead of using a separate account for utilities payable, the amounts owed are often included in Accounts Payable.

Accounting Terms (V)

vacation pay

A common fringe benefit given to employees during a period in which they do not have to work. If an employee earns one week of paid vacation to be taken after working one full year, the employer should recognize this cost/expense and liability while the employee is earning it. One possible journal entry is to debit Vacation Pay Expense and to credit Vacation Pay Payable. Later, when the employee takes the vacation time, the employer would debit Vacation Pay Payable and credit Cash.

vacation pay expense

An income statement account showing the amount of vacation expense earned by employees (by working) during the specified accounting period.

vacation pay payable

A balance sheet liability account which reports the total amount owed to employees at the balance sheet date for future vacation days as a result of the employees' past work.

valuation account

An account used in combination with another account. For example, the account Allowance for Doubtful Accounts is used with Accounts Receivable in order to present the net amount of the accounts receivable. The account Accumulated Depreciation is used with property, plant and equipment to indicate how much of an asset's cost has been allocated to Depreciation Expense. Here the account Accumulated Depreciation is used to report the assets' book value (not the assets' market value).

value billing

Billing a client based on the value of the information or service provided rather than billing based on time spent.

variable cost

A cost or expense where the total changes in proportion to changes in volume or activity. For example, if a company pays a sales commission on all of its sales, commission expense is a variable expense because commissions increase in total as sales increase and decrease in total as sales decrease. The cost of flour is a variable cost for the baker of artisan breads.

variable cost rate

The amount by which total costs will change when an activity is increased by one unit. In the equation of the line, $y = a + bx$, the variable cost rate is represented by "b" and the units of activity are indicated by "x".

variable cost ratio

Variable costs and expenses divided by net sales. To learn more, see Explanation of Break-even Point.

variable costing

See direct costing.

variable expenses

Expenses that vary with some activity. For example, sales commissions expense and cost of goods sold will be greater when sales are greater; electricity expense will decrease when machine hours are reduced.

variable manufacturing overhead applied

The variable manufacturing costs other than direct materials and direct labor that have been assigned to the products manufactured via a predetermined rate. Ideally, by the end of the accounting year the amount applied will equal the amount actually incurred.

variable manufacturing overhead cost

The indirect manufacturing costs that will change in proportion to the change in an activity such as machine hours. For example, a portion of a manufacturer's electricity cost will vary with the change in the number of machine hours worked.

variable manufacturing overhead efficiency variance

A variance arising in a standard costing system that indicates the difference between the standard amount of variable manufacturing overhead for the good units produced (standard hours times standard rate) and the variable manufacturing overhead based on actual activity (actual direct labor hours or actual machine hours times standard rate). To learn more, see Explanation of Standard Costing.

variable manufacturing overhead incurred

The actual cost incurred for manufacturing costs other than direct materials and direct labor which increase as production volume increases. Examples include manufacturing supplies and electricity to operate the production equipment.

variable manufacturing overhead spending variance

A variance arising in a standard costing system that indicates the difference between the actual variable manufacturing costs incurred and the expected variable manufacturing overhead costs based on some activity such as actual direct labor hours or actual machine hours. To learn more, see Explanation of Standard Costing.

variable overhead efficiency variance

See variable manufacturing overhead efficiency variance.

variable overhead spending variance

See variable manufacturing overhead spending variance.

variance

A term used with standard costs to report a difference between actual costs and standard costs. To learn more, see Explanation of Standard Costing.

variance analysis

To learn more, see Explanation of Standard Costing.

variance reports

Accounting reports that identify the differences between standard costs and actual costs, between budget amounts and actual amounts, etc.

vehicles

A long-term asset account that reports a company's cost of automobiles, trucks, etc. The account is reported under the balance sheet classification property, plant, and equipment. Vehicles are depreciated over their useful lives.

vendor

The supplier of goods or services.

vendor invoice

The name used by a buyer of goods or services for the sales invoice or bill received from the supplier of the goods or services.

vendors

Suppliers. Companies that provide goods or services.

vertical analysis

A type of financial analysis involving income statements and balance sheets. All income statement amounts are divided by the amount of net sales so that the income statement figures will become percentages of net sales. All balance sheet amounts are divided by total assets so that the balance sheet figures will become percentages of total assets.

volume

Sometimes referred to in the context of cost or expense behavior such as "variable expenses increase as volume increases." In this context volume might be an activity such as the number of machine hours, the number of units produced, the number of pounds processed, the number of units sold, or the dollars of goods sold.

volume-based allocation

An allocation of indirect costs based on the units of production, the number of machine hours, the number of labor hours, etc.

volume variance

See fixed manufacturing overhead volume variance.

Accounting Terms (W)

wages

The compensation earned by employees who are paid on an hourly basis. It is common for production workers to earn wages, since they are usually paid via an hourly rate.

wages expense

The compensation *earned* by hourly-paid employees during the interval of time indicated in the heading of the income statement. Under the accrual basis of accounting, the date that wages are paid does not determine when the wages are reported as an expense.

wages expense: delivery department

Under the accrual method of accounting, this account reports the amount of wages that the delivery employees have *earned* during the accounting period indicated in the heading of the income statement. Because wages are usually associated with hourly-paid employees, the expense will likely appear on the income prior to the date that the wages are paid. To learn more, see Explanation of Payroll Accounting.

wages expense: warehouse department

Under the accrual method of accounting, this account reports the amount of wages that the warehouse employees have *earned* during the accounting period indicated in the heading of the income statement. Because wages are usually associated with hourly-paid employees, the expense will likely appear on the income statement prior to the date that the wages are paid. To learn more, see Explanation of Payroll Accounting.

wages payable

A current liability account that reports the amounts owed to employees for hours worked but not yet paid as of the date of the balance sheet.

warranties

A promise to repair, replace, refund, etc. a product during a specified period. The company making the promise has a contingent liability and a warranty expense that should be recorded at the time the product is sold.

warranty expense

The expense associated with a commitment to repair or replace a product for a specified period of time. The expense should be reported on the income statement at the time that the sale of the product is reported in order to comply with the matching principle. A related account, Warranty Payable or Warranty Liability is also established at the time of the sale.

warranty liability

A liability account that reports the estimated amount that a company will have to spend to repair or replace a product during its warranty period. The liability amount is recorded at the time of the sale. (It is also the time when the expense is reported.) The liability will be reduced by the actual expenditures to repair or replace the product. Warranty Payable or Warranty Liability is considered to be a contingent liability that is both probable and capable of being estimated.

warranty payable
See warranty liability.

weighted-average accumulated expenditures on self-constructed assets
One of the amounts used in determining the amount of interest to be capitalized when a company self-constructs certain long-term assets.

weighted-average cost flow assumption
Used in the periodic inventory method to compute the value of inventory and the cost of goods sold. This average cost is based on the total cost of goods available for sale for the entire year (after all purchases for the year have occurred). The average cost per unit is then applied to the units in inventory and to the units that have been sold.

weighted-average cost of capital
A weighted-average of the cost of a company's debt, common stock, and preferred stock.

weighted-average number of shares of stock outstanding
Used to calculate the earnings per share of common stock: Earnings available for common stock divided by the weighted-average number of shares of common stock outstanding. The weighted-average number of shares is needed when shares of stock have been issued or repurchased within the period of the earnings.

white-collar worker
A term often used when referring to office workers, managers, professionals, and executives. These employees' pay is often stated as a salary for a month (and not as an hourly pay rate).

whole life insurance
Life insurance with a cash value (as opposed to term insurance, which does not have a cash value).

window dressing
Actions taken or not taken prior to issuing financial statements in order to improve the amounts appearing in the financial statements.

WIP
See inventory: work-in-process (WIP)

withdrawals by owner
Also referred to as draws. These are a reduction of owner's equity, but are not a business expense and they do *not* appear on the sole proprietorship's income statement.

withholdings
The term associated with payroll deductions from an employees' gross wages or gross salary.

work-in-process inventory
See inventory: work-in-process (WIP).

work-in-progress
Work-in-progress is the long-term asset account that is used to report the amounts spent on the construction of buildings and equipment until the asset is completed and put into service.

worker compensation insurance
Insurance often required by states and paid for by the employer to compensate workers who were injured on the job. The amount of the insurance premiums vary by type of work performed. For example, rates are higher for operators of machinery and are lower for office employees. To learn more, see Explanation of Payroll Accounting.

worker compensation insurance expense
Under the accrual method of accounting, this account reports the amount of worker compensation insurance expense that pertains to the period indicated in the heading of the income statement, whether or not the company has paid the insurance premiums within this time period.

The worker compensation insurance expense associated with the selling and administrative functions of the business will appear as on operating expense on the company's income statement. Worker compensation insurance cost associated with employees in the manufacturing function of the business will be an integral part of the cost of the products manufactured. If all of the products are sold, the worker compensation insurance cost will be included in the cost of the goods that were sold. If some of the products manufactured are in inventory, then some of the worker compensation insurance costs will be included in the costs of the products that are held in inventory.

worker compensation insurance payable
This current liability account reports the amount a company owes as of the balance sheet date for its worker compensation insurance policy premiums. The amounts owed are usually based on the policy's rates for the various work classifications of the company's employees.

working capital
Current assets minus current liabilities.

working capital ratio
See current ratio.

write-down
The reduction of an asset's carrying amount. For example, we often reduce or write down inventory from its cost to its net realizable value when the net realizable value is lower.

write-off

The reduction or removal of an asset amount. For example, an account receivable will be removed or written off if the customer is not able to pay the amount owed to the company.

write-up

The increase in a carrying amount. Also see write-up work.

write-up work

The preparation of financial statements from a client's information and without any review or audit of the amounts.

Accounting Terms (X)

x

The symbol for the number of units of product, number of machine hours, or other indicator of activity or volume as shown in the equation of the cost line y = a + bx.

x-axis

A graph's horizontal base which indicates the total number of units or other units of volume or activity for the amounts indicated by the y-axis.

Accounting Terms (Y)

y

The symbol that represents the total cost in the equation of the cost line y = a + bx.

y-axis

A graph's vertical scale that usually indicates the total dollars for the volume or units indicated by the x-axis.

year-to-date net income

A company's net income from the start of the current accounting year until a specified date. For example, the year-to-date net income at May 31, 2024 for a calendar year company is the net income from January 1, 2024 until May 31, 2024. For a company with a fiscal year beginning on July 1, 2023 the year-to-date net income at May 31, 2024 is the net income for the 11-month period from July 1, 2023 through May 31, 2024.

yield

Market interest rate, current return, effective interest rate. Also see yield to maturity.

yield to maturity

The total annual return on a bond investment if held to maturity. For example, if a bond is purchased at less than its maturity value, the yield to maturity includes the annual interest plus the gain as the bond increases from the investment amount to the maturity value.

If the bond is purchased at more than its maturity value, the yield to maturity includes the annual interest minus the loss as the bond decreases from the investment amount to the maturity value.

Accounting Terms (Z)

zero-based budgeting

Rather than the previous year's budget being the starting point for the next budget, a zero-based budget assumes no activities: everything in the budget must be justified.

zero coupon bonds

A bond without a stated interest rate. Because no interest is paid, the bond will sell for a discount from its maturity value. Rather than receiving interest, an investor's compensation will be the difference between the discounted price at which the bond was purchased and the price the investor receives when selling the bond. If the investor holds the bond to maturity, the investor will earn the difference between its discounted cost and its maturity value. A U.S. Series EE savings bond is a form of a zero-coupon bond.