KEY TERM GLOSSARY

Accrual Basis Accounting: A system of tracing income and expenses that recognizes income when it is ***earned*** (regardless of when cash is received) and recognizes expenses when they are ***incurred*** (regardless of when they are paid).

Assets: Everything that the business owns -- including such items as cash, inventory, prepaid expenses, and vehicles.

Average Tax Rate: The sum of all the tax rates that are applied to your income -- divided by the number of rates applied.

Balance Sheet: A statement of financial position that shows the assets, liabilities and net worth of the business.

Break - even: To have no profit and no loss; the point at which revenues exactly cover expenses.

Cash Basis Accounting: A system of tracking income and expenses based on when cash is actually exchanged. Income is recognized only when cash is received, and expenses are recognized only when cash is paid.

Cash Budget: A projected accounting of the cash inflows and outflows for a given period -- a projection of what the business "check book" will look like.

Cash Flow: The cash coming into a business from revenues versus the cash going out to pay expenses. Positive cash flow means more came in than went out; negative cash flow means the reverse.

Cash Position: The difference between cash inflows and outflows for any given period -- without borrowing short-term. How much cash the business has (or how much it is short) for the period.

Contribution Margin Percentage: The percent of each dollar of sales that is left after variable cost percentage has been deducted; the amount from each dollar of sales that is contributed to cover fixed costs and profits.

Contribution Margin: The amount left ***after*** variable costs are paid. The amount that is left to ***contribute*** to covering fixed costs (and profits).

Current Assets: What the business owns that is expected to be turned into cash within one year -- such as accounts receivable and inventory.

Current Liabilities: Obligations which are due to be repaid within one year.

Depreciation: The process of allocating the cost of a fixed asset (such as equipment) to the period that it benefits the business -- "writing off" its cost over its "useful" life.

Financial Gap: The difference between the funds ***needed*** to buy new assets and the funds ***available***. The amount that the company will have to ***borrow*** in order to support increased sales.

Financing Patterns: The relationship between the need for funds to support sales and the availability of those funds. The relationship between the use of profits, the use of debt, and the repayment of debt in acquiring assets to support sales.

Fixed Assets: Fixed assets are those that tend to be of a more permanent, long-term nature, such as equipment, vehicles, buildings, etc.

Fixed Costs: Expenses that do ***not*** vary with sales; those costs that are incurred whether or not any sales are made.

Fluctuating Current Assets: Current assets -- cash, accounts receivable, inventory, etc., whose levels rise and fall in direct relation to annual ***seasonal*** sales increases and decreases.

Gross Profit: Sales minus the Cost of Goods Sold, which is the cost of buying raw materials and producing finished goods.

Income Statement: The summary of the revenues; costs and expenses of a company during an accounting period.

Interest: The cost of using money; the fee which is charged for the use of the ***principal.***

Leverage: The increased rate of return that is made on net worth when by using debt to acquire assets.

Liabilities: What the business owes to creditors -- to ***non***-owners who supply funds that must be repaid. ***Debt*** is another term for ***liability***.

Liquidation Control: Ownership -- individual or collective -- of 66 2/3% or more of the shares of a corporation. These "two-thirds majority" owners can liquidate the corporation at will.

Long - Term Debt: Obligations that are scheduled to be repaid in a period greater than one year.

Long - Term Financing: Debt that is scheduled to be completely repaid at some point past one year in the future.

Marginal Tax Rate: The amount of tax paid on each **additional** dollar of income.

Merger Control: Ownership of 80% or more of the shares of a corporation. If Corporation A owns 80% or more of the shares of Corporation B, then B's dividends can be passed through to A ***without*** being taxed.

Minority Interest: Ownership of less than 50% of the shares of a corporation.

Net Profit: The amount remaining after all expenses have been met. The difference between total sales and total costs and expenses.

Net Worth: What the business owes to the owners -- the investment that the owners have in the company. Also called ***owners' equity.***

Operating Control: Ownership -- individual or collective -- of 51% or more of the shares of a corporation. These "majority" owners can hire, fire, determine dividend policy and make all operating decision for the corporation.

Percent of Sales: A method for measuring the variable assets and liabilities that a company needs to support a given level of sales. Each category of variable assets and variable liabilities for a completed year are divided by sales for that year. The resulting percentage can then be applied to ***projected*** sales for future years to determine the new investment needed for each category.

Permanent Current Assets: The base level of current assets that the company maintains at all times. The level of cash, accounts receivable, and inventory that the company requires regardless of seasonal requirements.

Principal: The face value of an obligation (such as a loan) that must be repaid at maturity, separate from **interest**.

Profit Plan: A projected or "proforma" income statement detailing revenues and expenses that are expected for some future period.

Retained Earnings: Net profits that are kept ***accumulating*** in the business (as opposed to being paid out to owners). These profits are generally ***not*** cash; instead, they have been used to purchase assets in the course of normal operations.

Retained Earnings: The net profits (positive or negative) from the income statement that are left to accumulate in the business.

Seasonal Pattern: The rises and falls in sales, profits and cash caused by seasonal demands for a product or service.

Short-Term Financing: Debt that is scheduled to be completely repaid within one year.

Sources and Uses of Funds Statement : A financial statement that details changes in financial position for a given period. It presents the sources of funds for operations (transactions that increased working capital, such as net profit) and the way funds were used (such as buying equipment or repaying debt) Also called ***Sources and Application of Funds Statement***.

Structuring Liabilities: Matching the life of the asset to the length of the financing. Short-term financing for current assets, long-term debt (or equity) for permanent current assets and fixed assets.

Sustainable Growth: The rate at which a company can grow while maintaining a targeted debt-to-worth ratio. (In other words, how fast a company can grow if it is to maintain a specified level of financial risk.)

Target Profit: The amount of profit that is planned. The profit that is added to fixed costs to determine the sales goals -- in relation to a given contribution margin.

Variable Asset: An asset that increases (or decreases) as sales rise or fall. For example, more sales would mean more accounts receivable -- even though the company was collecting them just as efficiently as before the sales increase. (In other words, the pie would be cut the same, but it would be a larger pie.)

Variable Cost Percentage: The percent of each dollar of sales that goes to cover variable costs.

Variable Costs: Expenses that vary directly with sales; those costs that are incurred ***only if*** sales are made.

Variable Liability: A liability that increases to support the variable assets, which increase as a result of a sales increase. For example, more sales would require that more inventory be kept on hand (to avoid stock-outs). This, in turn, would mean carrying more accounts payable -- if the company maintained its accounts payable turnover at the same rate as before the increase.