Personal Law Dictionary

AAA See American Accounting Association.

abandonment To give up, voluntarily, an ownership or leased interest in a property. When a lease is involved, the property reverts to the owner; when an owner is involved, the property usually reverts to the state.

abatement The cancellation of a levy imposed by the government. Levies are commonly for taxes or for special assessments that an individual (or organization) has not paid.

ABC See activity-based costing.

ABC method An inventory scheme in which items are categorized by their order of importance or their financial value—“A” being the highest value.

abnormal spoilage Spoilage beyond that expected (or normal) in any manufacturing process. Abnormal spoilage is always treated as a loss.

absorb Transferring one account to another so that the first account ceases to exist. For example, a “work in progress” is transferred to a “finished goods” account when that work is completed.

absorption costing A type of costing in which all manufacturing expenses are treated as cost of goods (or product cost), and nonmanufacturing expenses (e.g., marketing costs) are treated as cost of sales (or period cost). In other words, the cost of sales is not included in the inventory value of the product and cannot be reported as part of that value.

abusive tax shelter A limited partnership that the Internal Revenue Service determines is claiming illegal tax deductions. A common scenario is a partnership overvaluing property, thus allowing itself greater tax write-offs for depreciation. When the IRS disallows such write-offs, it usually claims back-taxes and imposes interest and penalties on the partnership.

Academy of Accounting Historians A professional association dedicated to the study of the history of accounting. The association produces the Accounting Historian’s Journal.

accelerated cost recovery system (ACRS) A method of depreciation against taxes created by the Economic Recovery Act of 1981. The type of property determines its class, and each class is assigned a depreciation rate. For example, for 3-, 5-, 7- and 10-year classes, the depreciation is 200 percent against the declining balance. The purpose of the ACRS is to encourage capital investment by businesses.

accelerated depreciation For fixed assets, a method of depreciation that recognizes higher rates of depreciation in the early years and lower amounts in the later years—the kind of depreciation one would use for a piece of office equipment (e.g., a copier) that would run more efficiently in its early life, would require more maintenance later on. Accelerated depreciation (which involves tax benefits) is thus a way of creating similar charges to income during the life of the asset.

acceleration clause A provision in a mortgage in the event of a default in

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which the remaining principal and interest are immediately due and payable.

acceptance This term has three meanings: (1) when one party to a business arrangement accepts the offer of another, thereby creating a verbal contract leading to a written contract; (2) a draft drawn by a business that a bank guarantees; and (3) a drawee's promise to pay such a draft, which the beneficiary accepts.

access time The time a computer requires to process and provide data from the time that data was originally requested.

accommodation endorsement Agreeing to be responsible for someone else's debt if that person defaults. The person applying for credit may not otherwise be able to obtain credit without such an endorsement (e.g., a parent agrees to be responsible in this way for a child's first car loan).

account The relationship between a creditor and debtor (one is said to have an account with the other) and the record of each financial category within an individual business, separately reported in that company's financial records (e.g., an account for a particular asset, customer or a vendor, cash on hand).

account form A kind of balance sheet, one in which assets are positioned to the left, liabilities and equity to the right. The more common form, the report form, puts assets above liabilities and equity.

accountability The responsibility of ensuring that the financial records of a business or organization are in order and accurate. The chief financial officer of a company is is accountable to that company's board of directors. A company's auditors are responsible to those using that company's financial statements (including the Internal Revenue Service and to government entities in general) that the statements are true and in no way fraudulent.

accountancy Generally a term in British usage, meaning what Americans mean by accounting (i.e., the theories and practice of the profession).

accountant Someone who performs accounting services (i.e., a person who creates financial plans, monitors those plans, and prepares financial statements and tax returns). In firms of accountants, or in the largest corporations, accountants customarily specialize in a particular branch of the discipline (e.g., taxes or cost accounting). Accountants may also act as advisers to management. See also certified public accountant.

accountant-in-charge During an audit, that person who is ultimately responsible for the final report and to whom the assistants report. The accountant-in-charge will also report to the management of the company being audited, is ultimately responsible to his own firm for the audit, and is the "point person" to whom the IRS (and any other government agencies) refers if they have any queries.

Accountants for the Public Interest (API) A professional organization that analyzes public policies in terms of their financial implications and provides technical services to not-for-profit organizations.

accountants' index Published quarterly by the American Institute of Certified Public Accountants, this bibliography lists books and articles of interest to the accounting profession.

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Accountants International Study Group (AISG) A professional organization comprised of representatives from the American Institute of Certified Public Accountants, the Canadian Institute of Chartered Accountants and the Institute of Chartered Accountants of England and Wales. It is devoted to examining questions of common interest to accountants in the three different countries.

accountant's liability A general term referring to the potential legal liability of an accounting professional (liability to those retaining the accountant as well as those who are relying on the financial statements that the accountant prepares—e.g., investors or the government). Although at its most serious the accountant could be guilty of fraud, in general the liability is the result of the accountant's not having implemented the rules of generally accepted auditing standards (GAAS).

accountant's responsibility Ethical obligations to those who have retained the accountant (i.e., those depending on the accuracy of the accountant's work).

accounting A term used to refer to (1) the process of recording, analyzing, and explaining financial information or (2) the discipline itself.

accounting change Any variation in the way that accounts are prepared. There could be various reasons for the change (e.g., new IRS regulations or the adoption of new methods in, say, allowing for doubtful, probably noncollectable, accounts receivable). Whenever such a change occurs, accountants are expected to footnote any financial statement, offering a full explanation of the reason for the change.

accounting control Any discipline to ensure accuracy imposed on a company's financial record keeping (e.g., having one person make entries for purchases and another person check those entries).

accounting convention A practice universally accepted by the accounting profession, such as those practices that are incorporated in GAAP (generally accepted accounting principles) or in GAAS (generally accepted auditing standards). These conventions change from time to time (e.g., in response to new tax rulings).

accounting cushion Overstating a potential expense (e.g., for bad debts) because an accountant believes extraordinary circumstances are involved. The effect of cushions is to decrease profit. Accountants must be careful about this kind of overstating because, if it proves wrong, it can create an unrealistic level of profit the next year when it is "backed out."

accounting cycle The progress of a particular transaction from its occurrence to its recording in the financial records to its appearance in a financial statement. For example, a sale occurs, is registered as an account receivable, and then appears on a profit and loss statement as a sale.

accounting entity Any economic unit that separately maintains records of its financial transactions. An accounting entity can be a small company, separate companies within a large conglomerate, or divisions within a large company.

accounting equation Any procedure in which double-entry bookkeeping is involved (i.e., in which a debit offsets a credit or vice versa).

accounting error A genuine mistake rather than fraud, it is often caused

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by carelessness, bad internal controls, or not following generally accepted **accounting principles. accounting event** Any recorded financial transaction.

Accounting Hall of Fame Founded at Ohio State University in 1950, this organization recognizes outstanding contributions to the accounting profession.

accounting manual Any guidebook created by a company or organization to set out its accounting standards and practices as a guide to its employees.

account missstatement A pronouncement, in formal financial statements, that is in violation of generally accepted accounting principles (GAAP). It must be acknowledged, corrected, and footnoted in subsequent financial statements.

accounting period The time covered by any financial statement. Common periods are annually, based on calendar or fiscal year; quarterly, required by the government of publicly owned companies; and monthly, usually for the internal use of the company or organization.

accounting policies Those policies employed by a particular company. They must be consistent with common practice, but otherwise there is often some leeway. An example would be the way in which a company values its inventory: one company might include cost of labor as well as cost of materials; another might include cost of materials but not labor, preferring to "expense" it as overhead. Whenever there is variation from the norm, accountants must explain accounting policies on formal financial statements.

accounting practice The ways in which accountants perform their duties on a day-to-day basis. These practices can vary depending on the needs of a company for which an accountant works or for clients for which the accountant serves as a professional advisor/auditor.

accounting principles The rules of the profession (i.e., the ways in which

certain accounting problems are handled. Generally, these rules are those of generally accepted accounting principles (GAAP), which are based mainly on the pronouncements of the American Institute for Certified Public Accountants.

accounting procedure Any method used in the recording of financial transactions or in the preparation of financial statements.

accounting records Any instrument that monitors the financial workings of a company or organization (e.g., a cash receipts journal, invoices, or checks).

accounting series releases (ASRS) Documents issued by the U.S. Securities and Exchange Commission (SEC), which serve as official requirements and mandates for the accounting profession.

accounting software Any program that allows accountants to maintain company financial records on a computer.

accounting standard Conduct mandated by either the law or by a professional body, such as the American Institute of Certified Public Accountants.

accounting system That which is followed by a particular company or organization to record, store, and communicate its finances. Any such

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system must of course conform to industry standards, to professional rules of conduct, and to government regulations.

accounting trends and techniques An annual publication of the American Institute of Certified Public Accountants, which includes a survey of the financial reporting techniques in the annual reports of 600 U.S. companies. The goal is to advise accountants of any innovations or new techniques in financial reporting.

accounting valuation In accounting, the value assigned to a company's assets. This is a highly important task in accounting for it effectively values the company as a whole after its liabilities have been deducted from the total.

accounts payable Undertakings to pay for goods and services rendered to a company by outside suppliers/vendors. Accounts payable are a crucial part of a company's short-term debt and are recorded as a liability on the balance sheet.

accounts receivable Amounts a company is owed from customers who have purchased its goods or services. Accounts receivable are recorded as an asset in the company's balance sheet.

accounts receivable discounted An account receivable (i.e., a debt) that is sold to another company at a discount because it has proven difficult to collect: the company making the sale accepts, say, 75 percent of the value of the debt; the company paying that 75 percent (usually a collection agency) then attempts to collect and receives the difference between the full amount and the discounted amount for its services.

accounts receivable turnover The speed at which a company collects its receivables. It a common business experience that the longer receivables are outstanding, the harder they become to collect.

accretion Growth in the value of assets.

accrual accounting The opposite of cash basis accounting. Accrual accounting recognizes revenue when earned (when the company renders a bill) and expenses when incurred (when the company is invoiced). In other words, transactions are treated as if cash has been received or paid out.

accrued assets See accrued revenues.

accrued expenses/liabilities Those expenses incurred during an accounting period but not paid at the end of that period.

accrued liabilities See accrued expenses.

accrued revenues/accrued assets Income earned during an accounting period (i.e., the company has billed for goods or services) but not received during that period.

accumulated benefit obligation The current value of benefits owed to an employee but not yet given to that employee (e.g., the present value of that employee's pension).

accumulated depreciation The total amount (to date) claimed on a particular fixed asset (e.g., the entire depreciation claimed on a particular

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piece of machinery from its purchase until the present time).

accumulated income The profit that has been held (i.e., not paid out in dividends) by a corporation.

accuracy Also known as accurate presentation. The soundness/correctness of an accounting process or item (e.g., an invoice or a financial statement).

accurate presentation See accuracy.

acid test ratio Slang: a test of liquidity. Dividing liabilities by liquid assets (cash and accounts receivable, not inventory). The goal is to determine whether assets are equal to or greater than liabilities.

acquisition cost The real price of goods or services. That is, the base costs as well as incidental costs (e.g., transportation of a manufactured item from manufacturer to user).

ACRS See accelerated cost recovery system.

activity analysis An evaluation designed to determine the most cost-effective way of creating a particular product or providing a particular service.

activity-based costing (ABC) An attempt to identify the various tasks performed in a company as a way of assigning overhead costs to goods or services.

activity center The cost of two or more business activities that it makes sense to put together. For example, a company might decide to regard as one cost the inputting of order information and the printing out/dispatch of the resulting invoices, even though these tasks might be performed by two different people.

activity cost driver That which causes costs to increase beyond the basic cost of a particular product or service. For example, the same customer orders 10 of the same product, one at a time, during the course of a month rather than ordering all 10 at once. Ten different orders must be processed and fulfilled, adding to the cost of the "activity" of producing that product.

activity cost pool Bringing together all the costs—fixed and variable—associated with a particular activity within a company.

activity driver analysis The systematic determination of the costs involved in a particular business activity.

actual cost The real cost involved in buying and selling a product. For a buyer, actual cost will involve the list price after discounts as well as transport, storage, and possibly administration. For a seller, the actual cost involves materials, labor, and overhead.

actuarial activity The analysis of statistics. The term is usually used with regard to the insurance industry in which many financial analysts are engaged in the study of probabilities (e.g., the median age to which people are currently living).

actuarial basis The means used to determine how much must be periodically contributed to a pension fund to ensure that these contributions

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(and the interest on those contributions) equals the amount the employer is obliged to pay out of that fund when an employee retires.

actuarial gains or losses The difference between estimates of what contributions to a pension fund should be and the actual amount included in that fund. For example, if the pension fund earns more than was expected, there has been an actuarial gain.

actuary An accounting professional, skilled at computation, who analyzes insurance probability projections.

additional paid-in capital Money beyond the stated value (the par value) of shares that shareholders pay for those shares. Shares with a stated value of $20 may be currently selling for $25. The extra $5 is additional paid-in capital.

adequate disclosure A comprehensive explanation included within financial statements to the extent that readers of those statements will feel that they fully understand what has been presented.

adjustable rate loan A loan with an interest rate based on an outside factor. For example, the interest on business loans is often based on U.S. prime rate. A bank may give its best customers a prime-rate loan; other customers may pay more than prime. As the prime rate changes, the interest on these loans will change.

adjusted basis The value used as a base against which depreciation is calculated. Normally, the adjusted basis is the original cost.

adjusted gross income (AGI) A formulation of the Internal Revenue Service: the difference between the gross income (total pay) of the taxpayer and allowable adjustments to that income (e.g., the “adjustment” the government allows for contributions to an IRA or for medical expenses).

adjusting journal entry Correcting any accounting mistakes at the end of an accounting period or the adjustment of amounts that involved estimates in the first place.

administrative budget The kind of comprehensive financial plan by which the management of a company attempts to monitor its activities and progress.

ad valorem tax A levy on property. The most common of such taxes is that which is imposed by states and local municipalities on real estate.

advance Funds given to an employee before payday—usually because of a special or emergency situation—or funds paid to a vendor before that vendor has supplied a product or done any work (e.g., the deposit given to construction company before that company begins a project: this advance is customarily subtracted from the final bill). Any company receiving such an advance must treat it as a liability until the work has been completed.

adverse opinion An auditor’s claim that a company’s accounts do not fairly present its financial position or that they are not produced in accordance with generally accepted accounting principles. An adverse opinion is not common: it must be included (with reasons) in any audit opinion and is usually the result of an auditor’s being unable to convince a client to revise the company’s financial statements.

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affiliated company One with which there is a close relationship, though neither company holds a majority interest in the other. The term is also used to describe two companies that are subsidiaries of a third, controlling company.

AGI See adjusted gross income.

aging of accounts The classification of accounts according to the length of time that has elapsed since the invoice date or the due date. An aging schedule customarily breaks down invoices into 1-30 days, 31-60 days, 61-90 days, and over 90 days. In general, the longer an account is outstanding, the more difficult it is to collect.

AICPA See American Institute of Certified Public Accountants.

AISG See Accountants International Study Group.

alimony payments Support payments from one former spouse to another—generally husband to wife. The person making the payments may deduct them as part of the calculation of adjusted gross income (AGI). The person receiving the payments must, for tax purposes, treat them as income.

allocate Charging the expenses of achieving revenue to a number of different departments or spreading a cost over two or more accounting periods (e.g., a lawyer is engaged and paid a three-year retainer of $30,000: $10,000 of that amount would be charged in each annual accounting for the next three years).

allowance This term has three meanings: (1) reducing the value of an asset; (2) reduction in the amount owed to a vendor because of delays or because of damaged goods; and (3) the acceptable amount of spoilage in the manufacture of some product.

allowance for bad debts/allowance method A provision in accounts for the possibility of failure to collect some of a company's accounts receivable. In a well-done company balance sheet, gross receivables are reduced to reflect what the accountant believes is the likely net amount to be collected.

all-purpose financial statement A financial statement that will be regarded as thorough and as meeting the needs of all potential users—from employees to creditors to stockholders.

American Accounting Association (AAA) A professional organization, the membership of which is largely teachers of accounting. It is devoted to the theoretical foundation of accounting and publishes a quarterly journal, The Accounting Review.

American Institute of Certified Public Accountants (AICPA) The professional organization for certified public accountants. The AICPA provides technical guidance and advice to its membership and to government agencies such as the Securities and Exchange Commission. It also issues the authoritative Statements on Auditing Standards (SAS).

amortize/amortization The reduction of the value of an asset over a period of time (e.g., the reduction in the value of a piece of equipment).

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analytical procedures Evaluations of financial information performed by a qualified auditor. These evaluations range from the simple (comparison of last year's earnings with this year's) to the complex (predicting future growth or contraction).

analyze To evaluate any accounting-related item.

annual budget One prepared for either a calendar or fiscal year.

annualize To predict expenditure on a particular business cost for a year based on the experience of a few months. For example, an accountant might assume that if the cost of telephone services has been running at $200 a month, then the annualized cost (for a fiscal or calendar year) is going to be $2,400. This technique is commonly used in creating an annual budget or forecast.

annual report The financial document prepared by companies to summarize the previous year. It usually consists of the company's financial statements for the year, annotated with explanations; the report of the company's auditors; and a letter from the president or CEO of the company. The annual report is intended for the use of the company's shareholders, banks, employees, creditors, or any entity that has dealings with the company.

annuity Any kind of periodic payment of more or less the same amount (e.g., a company's receipt of dividends on its holdings of preferred stock).

antedate A service that is in effect from a particular date that precedes the date on which the contract is executed (e.g., the services of some professional who begins work for a company before the formal contract is signed, though the contract acknowledges actual commencement of work).

antitrust laws Three sets of U.S. government laws designed to encourage competition by ensuring that one company (or group of companies) do not unfairly control the market for particular goods or services.

API See Accountants for the Public Interest.

application program A computer program, designed for accountants, that specifically deals with a particular accountancy problem or accountancy problems in a particular industry.

applied cost A cost that is assigned to a particular product or service that is not "inherent" or obvious in the initial determination of cost. The most common applied cost is that of a company's overhead.

appraisal/appraisal value The estimated value of a particular asset, used for the purposes of determining how it should be stated in a company's accounts or the price at which it should be sold.

appreciation An increase in the value of an asset (e.g., the increase in value of property or shares).

appropriation The allocation of retained earnings (i.e., earnings not paid out as dividends) for a particular purpose (e.g., to buy new equipment or to establish a contingency fund).

arbitrage Buying an asset in one market and selling it in another in order to

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realize a profit.

arm's-length transaction A transaction between unrelated parties (e.g., an online transaction in which one party bids for the goods another has for sale).

arrears Past due payments on an account.

articles of incorporation Those documents prepared for individuals who wish to found a corporation in a U.S. state. They must file these documents with the relevant government official, usually the secretary of state. A copy of these documents is returned to the individuals. Along with the state-issued certificate of incorporation, these papers become the new corporation's license to begin operations.

articles of partnership Similar to articles of incorporation in that they are filed with the state authority, the acceptance of which allows the partnership to begin operations—appropriate to partners but not shareholders. Typically, these articles include commentary on the capital contributions, the purpose of the partnership, and the duties of partners, which in a corporation is generally covered by its bylaws, a separate document setting out the internal workings of the corporation.

ASRS See accounting series releases.

assessment An official (government) valuation of property for the purpose of levying a tax on it.

asset Any resource that is expected to provide a future economic benefit to a business. Assets are usually described according to their monetary value. In accounting, an asset is referred to as having "tangible" or "intangible" value. A tangible asset is one the value of which can be easily determined (e.g., a company car). The value of an intangible asset is much more difficult to quantify (e.g., goodwill or a trademark).

assignment of accounts receivable Using accounts receivable as collateral on a promissory note. If the assignor defaults, the assignee may collect the accounts receivable; they then belong to the assignee.

at par At face value. A share that has a face value of $50 and is being traded at $50 is said to be trading at par. If the share is trading above $50, it is trading at a premium; if less than $50, it is trading at a discount.

attest/attest function Statement by an auditor that financial statements fairly and accurately represent the trading results and financial condition of a company.

attorney's letter A letter sent by an auditor to a lawyer to verify that what a client has told the auditor about pending (or the absence of) legal action against the company so that the auditor may include notes on the company's legal position in the audit report.

audit An audit refers to four kinds of company procedure: (1) compliance audit—a determination of whether a company is operating according to national rules and regulations, as well as the regulations of the jurisdiction in which it operates; (2) management audit—an evaluation of the effectiveness of a company's executives; (3) internal audit—an investigation by a senior member of staff (not necessarily the company's chief financial officer or

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accountant) to determine that a company's procedures (including both financial controls and the day-to-day activities of the company) are operating consistently with company goals; and (4) financial audit, that which most people understand by the term audit—the formal examination of a client's financial records by a licensed certified public accountant to decide whether they are accurate and whether they conform to generally accepted auditing procedures (GAAP), leading to an audit opinion.

audit committee A committee set up by a company, and composed of outside directors, to oversee audit operations and to appraise the performance of the company's certified public accountants.

audit evidence That information that an auditor uses to arrive at the conclusions on which the audit opinion or audit report is based. The auditor is also determining the "quality" of the information (i.e., how sound the financial procedures of a client may or may not be).

audit liability The legal responsibility of auditors to make sure that the accounts they audit and the resulting financial statements are correct, that their audit opinion is sound. There is precedent for suing auditors for their mistakes.

audit opinion The report made by the certified public accountant after that accountant has conducted an investigation of a company's records at the end of its financial year. The purpose of the opinion is to verify that the company's records are true, that it has been operating in accordance with generally accepted auditing procedures (GAAP). The CPA may conclude that the company is not in compliance and is then obliged to say so in the audit opinion.

audit planning The setting out—by an auditor—of the steps an audit will involve.

audit program The procedures to be followed in an audit, generally prepared by the head CPA, to guide the assistants who will be helping the CPA. Usually, completion of each step is noted on a written program, and the person responsible for having completed the step signs his or her name.

audit report/auditor's report One of two kinds of report: a "short form," which includes the CPA's statement about whether a company has fairly expressed its financial condition in its financial statements; or a "long form," usually rendered for a large or complicated business in which the CPA also discusses scope of the audit, offers extensive commentary on the financial position of the company, makes suggestions about the future, and comments on the effectiveness of the company's accounting procedures.

audit risk The possibility that an auditor may fail to note some kind of irregularity or mistake in a company's financial statements.

audit test The attempt by an independent auditor (a CPA) to verify the information given to that auditor by a client. Common audit tests are asking a number of the client's accounts receivable or accounts payable to confirm that the balances recorded by the client are accurate.

audit trail The process by which an auditor traces the progress of a particular financial transaction (e.g., a sale, which could involve an order from a customer, the fulfillment of that order, the creation of an invoice,

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the collection of that invoice, the conversion of that entire transaction to a "completed sale," and its appearance in a company's financial statements). A company's accountant may periodically conduct such investigations to ensure that a company's financial procedures are in order. Likewise, a CPA, auditing a company's annual financial statements, customarily also conducts sample audit trails to ensure that none of the company's transactions are overlooked.

auditing evidence Evidence of particular transaction reconstructed by a CPA if something in a client's financial statements looks questionable. For example, if a CPA notes that at the end of the financial year some 50 percent of a company's receivables remain uncollected, and the figure at the end of the previous financial year was 25 percent, the CPA might choose to examine procedures for recording receipts.

auditing procedure/process An auditor's technique in assessing the validity of a company's financial statements. Depending on what the client requires, the audit may involve a simple survey of the financial statements (usually appropriate for small companies) or it may involve a complete audit, in which the CPA and assistants verify each of the company's financial transactions. The extent to which a CPA is able to certify accounts depends on the type of audit undertaken.

auditing standards Standards that a CPA employs in verifying a client's records. In the United States, the most common of these standards are those announced by the American Institute of Certified Public Accountants (AICPA), which publishes generally accepted auditing standards (GASS).

auditor A professional accountant with qualifications to perform an audit.

authorized capital stock The maximum number of shares that a corporation is allowed to issue according to its articles of incorporation. Issued shares—those sold to shareholders—are usually less than authorized shares.

average age of inventory The length of time it customarily takes any item in a company's inventory to sell.

average life The life expectancy of an asset.

avoidable cost A business cost that would not be incurred if a company stopped producing a particular product or service or engaging in a certain activity. Most costs (except for certain overheads) are avoidable: accountants constantly examine such costs to discover which could be cancelled without affecting the overall profitability of the company.

back order An order that cannot be filled at present because the item is not in stock. The order is kept on file and as soon as the product is available, it is shipped to the customer. An excessive number of back orders on file in a company usually indicates poor inventory control.

backup A duplicate copy of original financial data. In recent years, the term has come to refer to "backing up" any data stored on a computer—by, for example, "backing up" data on a disk that can be removed from the computer each night and separately stored.

backup withholding Funds withheld from any nonwage fee paid to a recipient when that person's Social Security number is not known. The law

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states that the entity paying the fee (which could be interest or dividends as well as a straight fee for services) must deduct 20 percent of the sum paid and remit it to the Internal Revenue Service. This is not an extra tax on the individual. The 20 percent is credited against the taxes of the person being paid when that person is properly identified and submits a tax return.

bad debt One that cannot be collected despite the best efforts of a company to do so.

bad debt expense An estimate in any financial statement of how much of recorded accounts receivable is unlikely to be collected.

bad debt recovery The circumstance that a sum written off as noncollectible is then in fact paid. The accounting method is to “reverse” the original write-off. If bad debt recovery happens frequently, it may be an indication that the accounting staff in a company writes off debt too quickly.

balance The amount owed on a loan; the positive amount in a bank account; or the difference between debits and credits in an account.

balanced budget One in which total expenditures are at least no more than total revenues. If expenses are less than income, the budget is said to have a surplus. If expenses are greater than income, the budget is said to have a deficit.

balance of payments A country’s trading record with the rest of the world, usually calculated as the difference between the monetary value of a country’s imports as opposed to the monetary value of its exports.

balance of retained earnings The amount in any given year that a company does not pay out to its shareholders. The calculation is comprised of three components: the balance at the beginning of the year, any adjustments during the course of the year, and the new year-end balance.

balance sheet A statement that shows a company’s financial position at the end of a particular period. The year’s financial statements always include a balance sheet, but many companies also produce one at the end of each month to accompany their profit and loss statement. A balance sheet offers three component’s of a company’s financial position: its assets, its liabilities, and what it owes to shareholders (i.e., the equity shareholders have contributed to the company by buying its shares plus any unpaid earnings on those shares). The balance is achieved in this way: assets equal liabilities plus shareholder’s equity. Balance sheets are used extensively in business for the reason that they provide an overall view of the condition of a company and help executives, directors, and their professional advisors easily see the resources of a company as well as what it owes. Balance sheets are regarded as the single most pertinent document illustrating a company’s financial condition.

balloon A term commonly used in real estate to describe a kind of mortgage or equity loan. In effect, a balloon is the payment on any loan substantially greater than previous payments—one that pays off the loan.

bank balance The final amount shown at any time in a bank account. To reconcile the account with an individual’s or company’s records, one must consider deposits not yet credited to the account, checks that have not yet been presented for payment, and any bank charges or fees not yet added.

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bank statement A statement prepared by a bank, usually monthly, to show transactions in an account. Customarily, bank statements show the following: the opening balance for the month; the deposits made; the checks cleared; any charges to the account (services charges and fees for stopped checks); and the ending balance.

banker's acceptance A draft, guaranteed by a bank, drawn by a business for future payment for goods or services. Such instruments are often used in foreign trade, where there is a time length between dispatch of goods and receipt of goods, and therefore of payment for those goods. Because it is guaranteed by a bank, a banker's acceptance reassures the seller that the bill will be paid.

bankruptcy A situation in which debts of a business are substantially greater than the value of its assets and the business files for court protection. The court supervises the liquidation of assets and the payment to creditors, prorated, of what this liquidation yields. Another kind of bankruptcy, Chapter 11, often called a reorganization bankruptcy, allows the company protection from its creditors even while it makes arrangements to pay them what they are owed over an extended period of time.

bankruptcy prediction The pronouncement of an auditor about whether a particular business is a going concern or whether, in the view of the auditor, the company has long-term problems. If the prediction of the auditor is that the company is likely to run into trouble, that a bankruptcy could be a possibility, then the auditor is obliged to say so in the annual audit report.

bargain purchase A purchase in which goods are acquired for under their market value (e.g., the acquisition of the equipment of a company that is going out of business.

barter The exchange of goods and services between companies when no cash changes hands for tax reporting purposes. However, the companies must report the full market value of such transactions.

base stock The minimum amount of inventory necessary for a company to function effectively.

basis The starting point for calculating a loss or gain. Also, the value against which depreciation is claimed.

basis of accounting The method that a company employs to record revenues and expenses—accrual accounting or cash basis accounting.

basket purchase See lump-sum purchase.

Bayesian probability The revision of previous estimates based on new information or new experience. For example, an estimate of orders to be received in the next six-month period is based by a company on its experience of the previous six months—but an economic downturn severely curtails orders, and the company must revise its forecast.

bear Stock market slang for one who believes that prices in the securities or commodities markets will decline. The opposite of a bull, who believes that prices will rise.

beginning inventory The balance at the beginning of any accounting period (e.g., the beginning of a company's fiscal year). Inventory is of three kinds: raw materials, work in progress, and finished goods.

behavioral accounting Also called human resource accounting. An approach that places a value on a company's personnel and includes that valuation in its balance sheet. This kind of accounting is most likely to be appropriate in a company that employs highly qualified professionals in which the assets of the company can truly be said to be depleted if certain members of staff leave (e.g., an advertising agency or a legal partnership).

bellwether security One that over time has proved that its movement up or down in value is indicative of the way that the market in general is moving.

benchmarking Comparing the procedures of a company to those of companies that are highly efficient and profitable in an effort to improve productivity or competitiveness.

benefit approach to pensions The amount of pension benefits, in return for services rendered, available at the present time: the current value of these benefits.

Beta Alpha Psi Founded in 1919, the national accounting fraternity, with chapters at some 130 universities.

betterment A capital expenditure for the replacement of a component of plant or equipment that will result in improved performance, thus resulting in an increased value for that particular asset.

bill of exchange See draft.

bill of lading A written document issued by the carrier that accompanies a shipment of goods and specifies the terms and conditions of transport. Usually issued for long-distance or overseas transport.

bill of sale A written document that transfers goods or title to an asset from a seller to a buyer according to specified terms and conditions.

billings on long-term contracts Periodic invoicing by a company for work that the company is doing for a client over a long period of time (e.g., a contractor's billing a developer for completed stages in a three-year-long housing project).

blanket insurance A policy that covers several items of property for the amount of their fair market value.

blue chip stock One that has a long record of growth or dividend payments. Such stocks are usually regarded as the best long-term investments, appropriate for those who wish to invest but do not wish to speculate in the stock market.

board of directors A group of people chosen by the shareholders of either a public or private corporation to run the business according to the company's charter and bylaws. It is common for a board to consist of a company's high-ranking executives (e.g., its president or CEO) as well as outside directors who it is hoped will bring a more generalist perspective to the group. Among other things, a board of directors has ultimate responsibility for a company's financial practices.

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boilerplate That part of any contract that is more or less common to all contracts.

bond Any written undertaking by a company, government agency, or other organization to pay the holder of the instrument a fixed amount on maturity. Interest payments are involved, and are usually paid semiannually. Bonds are either "secured" or "unsecured." Secured bonds (e.g., a mortgage bond) have a claim on real estate or other securities; unsecured bonds have no specific claim on any assets (they are often referred to as "junk" bonds).

bond discount An amount under face value at which this instrument can be issued. This discount can happen if the interest rate is below that prevailing in the marketplace, if the bond does not mature for a number of years, or if the company issuing it is perceived to be in financial trouble.

bond premium The amount above face value at which this instrument can be issued. This premium can happen if its interest rate is above that prevailing in the marketplace or if the company issuing it is perceived to be in a very strong position in its particular industry.

bond ratings Usually prepared by such agencies as Moody's or Standard and Poor's, an analysis of whether a bond is likely to go into default—a measurement of risk, in other words.

bonus method A practice in partnership formations: a partner who has contributed something other than capital (goodwill or expertise, for example) is credited with having contributed additional capital.

book(s) The financial records of a company, specifically its journals or ledgers.

book balance The final amount showing in any account at the end of an accounting period.

book inventory The value of inventory as shown in company records. It is not necessarily "true" inventory, which because of spoilage/damage can be determined only by a physical inventory.

book value The net value (net = original cost less depreciation) shown for an asset on a company's balance sheet.

bookkeeper/bookkeeping The person(s) within a company who is in charge of various accountancy support functions. Duties could include making entries in various company ledgers, doing the payroll, and reconciling bank statements. A bookkeeper is usually not a trained accountant but often someone who has gained expertise through on-the-job training.

bottleneck Any accounting activity that isn't working efficiently, usually because the work involved is greater than the personnel available to do that work. For example, a company suddenly receives a great number of orders, far beyond the capacity of its one order clerk to process in a timely way.

bottom line A company's net income after taxes or the end result (i.e., the final consequence of an activity).

branch accounting The practice of maintaining different accounts for each branch of one business entity. The purpose is to provide management the means of determining how well each branch is doing. Customarily, these different accounts are combined at the end of the financial year.

break-even analysis A determination of when a company's revenues equal its costs in producing the goods or services that create those revenues. Any revenues beyond the break-even point are profits. If costs are greater than revenues, however, the company is operating at a loss.

break-even point/break-even sales Revenues precisely equal the costs that produced those revenues. See break-even analysis.

bridge loan A short-term loan, often carrying a higher rate of interest, that is made in anticipation of a long-term loan. The most common example is money advanced by a lender so that an individual may purchase a home before that person has sold his or her current home; the bridge loan is paid back when the current home is sold, and the lender (the same lender or another one) provides a long-term mortgage on the new home.

brokerage fee An amount, usually a commission—though it can be a straight set fee—paid to a broker for buying or selling securities.

budget/budgeting A forecast, framed as a financial plan, of how a company will perform over some future accounting period, usually the following financial year. The forecast involves predicted income and expenses, acquisition of assets, and final profit or loss.

budget committee A company group, usually comprised of that company's senior executives and chief financial officer, that reviews, vets, and potentially revises a company's budget for the year.

budget control The attempt to control a company's activities to make those activities conform to that company's annual budget.

budget manual Any codification by a company of the ways in which it customarily prepares its annual budget; a guide to any financial professional who is preparing that company's budget for the first time.

budget report A report (usually monthly) that analyzes the difference between budgeted revenues and expenses and actual figures. These reports are used by companies to monitor their month-by-month progress against the budget.

budget slack/budgeting slack Underestimating revenues and overestimating expenses as a way of protecting the financial analyst who prepares a budget. As it produces something other than a true forecast, this practice is discouraged and not widely practiced.

budget variance The difference between projected revenues and expenses and actual revenues and expenses as shown by the monthly budget report.

budgetary participation Involvement by management in the budget process. Many companies involve not just their accountants but also their senior managers in the budget process as a kind of fairness: managers will be judged on how well they meet budgets. Many companies believe, therefore, that managers should participate in devising those budgets in the first place.

bull Stock market slang for an individual (or institution) that believes a particular company share or the market in general will experience a price rise.

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The opposite of a bear, who believes that a share or the market will decline.

business cycle A theoretical construct that economies periodically expand or contract; such cycles affect an individual company's growth and income.

business expenses Those expenses that may be legitimately deducted from a company's gross profit in the computation of how much that company owes for state or federal taxes. Put another way, expenses that are necessary to create company revenues. Examples would include a provision for bad debts, the purchase of new equipment, or payroll.

cafeteria plan Slang for a benefit plan that permits employees to make their own choices among various company benefits on offer.

call The option to buy (e.g., shares in a company at a specified price within a specified period). Also refers to bonds or preferred stocks that may be redeemed before their maturity.

call premium The amount an issuer must pay the holder of bonds or preferred stocks, beyond face value, to call in those instruments before their maturity. Instruments that involve a call provision almost always involve such a premium.

call price That which must be paid to call in a financial instrument bearing a call provision. It is equal to the face value of the instrument plus the call premium.

callable security A security that involves a call provision. Customarily, the issuer exercises that provision if the instrument carries a higher rate of interest than that which is current in the marketplace, as a means of reissuing at a lower rate of interest.

Canadian Institute of Chartered Accountants Founded in 1902, the primary professional organization for Canadian "chartered" accountants (the same as CPAs in the United States).

canceled check A check paid by a company's bank and then returned to the company: it constitutes the company's evidence that a particular debt has been paid.

capacity costs Costs related to providing facilities that allow a company to produce its goods or services, such as rents, property taxes, and insurance premiums. Capacity costs are always fixed costs.

capital In accounting, capital has four meanings: (1) long-term assets that are not themselves sold in the normal course of business, such as a factory building or equipment; (2) a company's resources (i.e., the difference between its current assets and current liabilities); (3) any goods purchased for use in the production of goods or services (e.g., computers); and (4) the interest of an owner in a business, the difference between assets and liabilities that constitutes the value of the business—also called equity or net worth. (In a corporation, stockholders' equity is the capital.)

capital account In a privately held business, the owner's net worth—the difference between the business's assets and liabilities. In a partnership, such an account exists for each owner. In a corporation, the term refers to stockholders' equity.

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capital addition Anything that adds to the value and life of a company's assets. In taxation, the cost of any improvements.

capital asset An asset added to a business to assist in the running of that business, rather than something that has been purchased for resale (e.g., land or goodwill or trademarks). In taxation, any property held by a taxpayer other than cash, inventory for sale, or accounts receivable.

capital budget/capital budgeting A long-term plan for investment in capital assets involving three phases: identification of need, selection, and administration.

capital decay The process by which an asset loses its value over time (e.g., a factory building becomes outmoded for its purpose or computers become technologically obsolete).

capital expenditure Any purchase of a long-term asset or means to improve a current capital asset.

capital gain Any profit involved in selling a capital asset. Both individuals and corporations are taxed on capital gains, though some gains (e.g., an individual selling a personal residence) are exempt to certain limits.

capitalize To charge an expenditure to the appropriate asset account because it will provide a benefit to the company for more than one year.

capital loss A loss on the sale of a capital asset. Such losses are deductible by individuals and businesses to offset capital gains. A corporation may deduct capital losses only to the extent that it has capital gains.

capital market Any trading center (e.g., the New York Stock Exchange) for long-term debt and company shares.

capital recovering allowance A concept in taxation, that a company may recover the cost of capital via such means as depreciation.

capital stock Another term for equity shares in a corporation—those authorized by its articles of incorporation and sold to investors. There are two basic kinds of capital stock: preferred stock and common stock.

capital structure Those assets of a business that provide its financing (apart from outside bank financing): the company's common and preferred stock and its retained earnings.

carrying costs Any expenses that a business incurs for holding inventory. These expenses could include interest on money borrowed to create inventory, storage charges for holding inventory, or insurance against damage of inventory.

cash Money that a company has deposited in a bank as well as any instrument that a bank will accept as cash (e.g., checks or money orders). Notes receivable or accounts receivable are not regarded as cash and may not be entered as such on financial statements.

cash basis accounting Recognizing income and expenses when cash is received or disbursed as opposed to when goods are sold or debt incurred

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(i.e., the opposite of accrual basis accounting). The method is generally only possible for a small service business that does not maintain any kind of inventory.

cash disbursement/cash payments journal A financial records book used to record all payments made in cash for accounts payable and operating expenses. It usually provides substantial detail, including date of transaction, check number, explanation, and the balance.

cash discount See sales discount.

cash dividend That which is periodically paid to shareholders, typically expressed as dollars and cents per individual share (though with preferred stock, it is usually expressed as a percentage of par value).

cash equivalent The amount that can be realized in the marketplace by selling particular goods or services.

cash flow Cash receipts less cash disbursements for a particular period of time. If, in a given month, a company pays out $30,000 and collects $40,000, its cash flow for the month is said to be $10,000.

cash flow forecasting A kind of financial forecast in which an accountant attempts to predict (for any given period) how much cash will come into the business (customers paying bills, investment income) against how much will have to be paid out (operating expenses, accounts payable).

cash flow statement A document that explains the sources from which cash has come into the business and the ways in which it has been disbursed.

cash-generating efficiency The ability of a company to generate cash from its operations.

cashier’s check A check drawn by a bank on its own funds: it is used as an equivalent of cash.

cash receipts journal A record of all company transactions that have involved the receipt of cash (e.g., collection of a company’s accounts receivable). Typical entries would note date of receipt, amount, and explanation.

cash shortage/overage A problem for businesses that deal almost exclusively in physical cash (e.g., a small retail establishment). The cash on hand is less or more than what is recorded on the cash register.

cash surrender value A portion of the premiums paid on an insurance policy if the beneficiary of that policy cancels it. In companies, the cash surrender value is regarded on the balance sheet as an investment.

CD See certificate of deposit.

ceiling The net realizable value of an asset.

cell The intersection between a row and a column in an electronic spreadsheet. The cells can be made to relate to each other in particular detail to make them calculate and create financial data.

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certificate of deposit (CD) An investment instrument available at banks and other financial institutions that offers a certain rate of interest if the instrument is kept in place for a certain period of time. If the depositor withdraws funds before the CD matures, there is a significant penalty involved.

certified check A check that a bank guarantees to pay.

certified financial planner (CFP) Someone who has passed the examinations of the College for Financial Planning and is competent to analyze the financial condition of clients and to prepare financial plans for these clients.

certified financial statements Statements accompanying a certified public accountant's audit report.

certified management accountant (CMA) One who has been trained in management skills as well as accounting: that person has passed a series of examinations certifying that competence.

certified public accountant (CPA) An accountant who has passed the Uniform SPA Examination administered by the American Institute of Certified Public Accountants (AICPA) and is therefore licensed by the state in which the accountant practices to use that title. A CPA is authorized to write an audit opinion or audit report on a company's financial statements and can act as a final auditing authority.

CFO See chief financial officer.

CFP See certified financial planner.

change in reporting entity Notification to government taxing agencies that two of more formerly independent companies are now combined into one and will jointly prepare financial statements and tax returns in the future. It is common for companies in this situation to restate their financial results for the previous five years as if they were combined during that period.

Chapter 7 A type of bankruptcy in which, after a company has liquidated many of its assets to pay off most creditors, the court appoints a trustee to make management changes in the company, arrange for further financing, and run the business with a view to avoiding further loss. The underling assumption of a Chapter 7 bankruptcy is that, with a fresh start, the company can prove itself to be a viable business.

Chapter 11 A kind of bankruptcy that is effectively a reorganization of the business. Managers remain in control of their business while the court provides them protection from their creditors. The company and its creditors work together to restructure its debt (i.e., reschedule payments to its creditors). The assumption of a Chapter 11 bankruptcy is that, allowed to restructure its debt, the company will survive.

charge To debit an account.

charitable contributions deduction That which is allowed by the government as a credit against taxes.

chart of accounts A guide—by name and number—of the respective

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accounts listed in a company's ledger: it serves as a kind of index to the ledger, helping anyone examining the ledger easily find accounts.

chartered accountant The British, and British Commonwealth, equivalent of a U.S. certified public accountant.

check A draft drawn upon a bank, payable to the person named in the draft. When used as a verb: to determine an item's accuracy.

chief financial officer (CFO) The executive within a company who directs the financial affairs of that business. Usually the CFO is also a member of the company's board of directors.

circulating capital That which is nonstable because it is continuously used up and must be replenished to ensure a company's continued operations (e.g., materials, labor, and overhead).

classification as going concern See going concern.

classification of assets The process of grouping a company's resources under appropriate headings (e.g., current assets or investments).

classification of liabilities The process of grouping a company's debts by the date on which they are due.

Clayton Antitrust Act of 1914 A federal statute that outlaws practices in restraint of trade and competition (e.g., price discrimination and exclusive dealerships).

closed corporation See private corporation/privately held company.

closed-end mutual fund One in which the shares are limited to a certain number and are traded like the common stock of a corporation. After the shares are initially issued, the only way that an investor can buy or sell shares is in the open market (i.e., purchase from a seller shares that have already been issued). See open-ended mutual fund.

closely held corporation A company that has only a few shareholders. It is different from a privately held corporation in that it does trade shares (i.e., although it is a "public" company, very few shares are actually traded).

closing entry The journal at the end of a financial period—usually the financial year—that transfers the net difference between revenues and expenses to owners' equity. Both revenues and expenses accounts are then at zero, the point at which entries for the new year begin.

CM See contribution margin.

CMA See certified management account.

code of professional ethics Rules of conduct issued by the American Institute of Certified Public Accountants (AICPA), setting out standards for CPAs to follow. The best known of these rules is that CPAs may not divulge client information to any third party other than the government.

COGS See cost of goods sold.

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COLA See cost-of-living adjustment.

collateralize To pledge company assets to secure a debt. Common forms of collateral include company fixed assets, inventory, and accounts receivable.

collection period The number of days it customarily takes a company to collect its accounts receivable. A long collection period (more than 30-60 days) can prove a burden to a company because it disallows the company from discharging its own accounts payable in a timely manner.

combined financial statement A financial statement in which income statements and balance sheets of related business entities (e.g., subsidiaries of the same holding company) are combined so that they may considered as one reporting entity. Intercompany transactions are eliminated in a combined financial statement.

commercial paper A short-term (no more than 270 days) unsecured loan to a financially strong company.

commodities futures Contracts in which sellers promise to deliver a given commodity by a certain date at a predetermined price. That price is determined on the floor of a commodity exchange. These contracts, which may run for as much as a year, may be bought and sold at any time. Financial officers in companies often purchase currency futures when they must pay for some future expense in a foreign currency and want to “lock in” that currency against current rates against the dollar.

common cost One that is shared by different departments or across different products or jobs (e.g., fixed overhead costs).

common stock A share in a public or privately held company. Common stockholders have dividend and voting rights. In a bankruptcy, common stockholders are paid after bondholders and preferred stockholders. The advantage of common stock is that it involves the possibility of substantial appreciation.

communication in accounting The concept, universally acknowledged, that it is difficult for an auditor to explain how well a company is doing based solely on its financial statements, that auditors must strive in audit opinions and audit reports to convey information that financial statements, however complex, cannot provide in themselves.

comparative statement A statement that includes balance sheets and income statements for numerous years—one in which the specific components of those statements are arranged side by side so that the reader may compare the changes in individual categories from year to year.

compound interest The rate incurred when interest in subsequent periods is earned not just on the original principal but also on the accumulated interest of prior periods. In other words, the kind of loan in which interest is also being paid on interest.

comptroller general The head of the U.S. General Accounting Office (GAO), the independent auditor of the federal government.

condensed financial statement An income statement, balance sheet, or changes in financial position statement in which less essential detail has been combined into general categories. A document that provides a quick perspective on a particular business.

Conference Board, The A group of high-level businesspeople who study economic trends and issues in management. Its goal is to improve the business climate and the practice of business activities.

confirmation An auditor's request to a third party to verify the existence of a financial item relating to the auditor's client (e.g., a request to a bank to verify balances in accounts or a request to a vendor to verify an account payable).

conglomerate merger A merger in which disparate companies merge, the benefit in theory being that of diversification of risk because the conglomerate operates across various kinds of businesses.

conservatism A philosophy of accounting that holds that it is better to understate assets and overstate liabilities. The underlying notion is that it is "safer" to be pessimistic than to be optimistic management, and investors, are therefore less likely to make mistakes.

consigning A way of selling certain kinds of goods. The consignor delivers goods to the consignee; the consignee does not pay for them, and they are not considered to be part of the consignee's inventory; the goods still belong to the consignor. The consignee acts as the consignor's agent in selling the goods to third parties. When goods are sold, the consignee forwards the proceeds to the consignor, less a commission for the consignee.

consistency The sameness of accounting procedures within a company from one accounting period to another.

consolidated balance sheet One that shows the financial position of a group of related companies as if they were just a single economic unit.

consolidated financial statements Those that bring together assets, liabilities, and operating accounts of a parent company and its various subsidiaries.

constraining/limiting factor Some phenomenon that curtails the production or sale of a particular product or service (e.g., a labor shortage or an general economic downturn).

Consumer Price Index A measurement of the price of consumer goods, issued each month by the U.S. Bureau of Labor Statistics. The measurement is of current prices against those of the base period.

consumption tax A tax levied on the consumption of an item (e.g., a sales tax).

contingent asset One that depends on some future circumstance that may or may not occur. For example, a company holds a patent on a particular product, which, after it has left production, may or may not be successful.

contingent liability A liability that may occur in the future as a result of some past event (e.g., a company is involved in a lawsuit that it could lose: it could be forced to pay damages).

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contingent reserve A fund that includes a portion of a company's retained earnings as a safeguard against any future losses or unexpected expenses.

continuing account Those components of a balance sheet (e.g., fixed assets) that are carried over from one accounting period to the next.

continuity See going concern.

continuous audit The practice of testing accounting procedures and book entries to correct mistakes as a way of making the CPA's work easier at year's end.

contra account One that corrects the value of an asset (e.g., an account that records the depreciation of an asset).

contributed capital See paid-in capital.

contributed capital in excess of par See additional paid-in capital.

contribution margin (CM) Also called marginal income. The difference between sales revenue and the variable costs of a product or service (e.g., labor and materials). The amount, in other words, that can be applied to fixed costs (rent, utilities), which in turn may generate profits. Calculating contribution margins can be useful in various ways: it helps to establish how well a department or division of a company is doing; it demonstrates how much prices can be lowered in an economic downtown; and it helps accountants to focus on which company costs are fixed, which are variable.

controllable costs Variable costs, such as materials and labor.

controlled company One in which the majority of voting stock is held by one person or one organization so that effectively there is no outside input.

controller The head accounting executive in a business, though such a post may not exist in a company that also has appointed a chief financial officer. The alternate British spelling, comptroller, is sometimes used in the United States, particularly in the federal government.

convention An accounting practice that is universally accepted (e.g., the general structure of a balance sheet).

conversion A term with three meanings: (1) the move from one currency to another (e.g., paying a debt in the United Kingdom by converting dollars to pounds; (2) substituting one valuation for another (e.g., restating the value of an asset after allowing for depreciation); and (3) exchanging one security for another (e.g., converting convertible bonds into common shares).

convertible debt securities Those securities that may be exchanged for a given number of common stocks at a set price. This conversion is allowed by the terms of the conditions of the security, and it is customarily the choice of the security-holder (i.e., it is an option always available to the security holder).

cook the books A slang term meaning to falsify financial records to make a company's financial condition look better than it is. Such a practice is unethical and illegal.

copyright Protection given by federal (and international) law to the

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authors of creative works. The copyright may be held by a company that has produced a particular work, and in that instance it may be sold. Its asset value is the price of acquisition or creation.

corporate failure The cessation of trading of a business, which is usually preceded by a period of financial distress, during which a business cannot meet its financial obligations.

corporate joint venture Any cooperation between two or more otherwise unrelated companies to achieve a particular goal (e.g., a cooperative pact between two manufacturers to build an airline: one of them provides the frame, the other provides the motor).

corporation A business entity, with legal status, in which ownership is vested in those who purchase its stock and in so doing contribute capital to fund the business; a corporation is, however, regarded (in terms of taxation or responsibility for liabilities) as a legal entity separate from its shareholder-owners. A corporation is formed when its founders file articles of incorporation with the relevant state authority, usually the secretary of state. Shareholders may sell their shares to other investors.

correcting entry See adjusting journal entry.

cost The price paid to acquire the essentials of any business, that which is needed to produce the company's goods or services. Materials, labor, and premises are common costs in virtually any business.

cost accounting The practice of identifying all expenditures in the production of particular goods or services as a means of determining a unit cost. The goal is to determine accurately the price that ought to be charged for a company's products/services.

cost allocation Also called cost apportionment, cost assignment, cost distribution, and cost reapportionment. The task of establishing exact costs of the components of a company's goods or services. For example, in trying to establish the real costs of a manufactured product, a cost accountant must determine not just the costs of materials and labor but those of administration, customer service, fixed overhead, and marketing.

cost apportionment See cost allocation.

cost assignment See cost allocation.

cost behavior analysis Separating all costs into either variable or fixed costs.

cost center Any unit in a business or organization in which the managers are responsible for only their own costs. For example, a sales department may be a cost center, responsible for only its own costs, not those of other departments that produce or market goods and services. Cost centers are useful to management in that budgeted costs for the unit can be compared to actual costs, to determine whether the budgeted costs are in fact wrong or if the center is operating inefficiently.

cost distribution See cost allocation.

cost driver Any element that is a constant in creating cost (e.g., salaries of

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staff involved in producing particular goods/services).

cost-effective That choice of expenditure that is most likely to bring the greatest benefits.

cost estimation Also called cost prediction. Predicting future costs on the basis of past costs but factoring in any new variables.

cost management The attempt to monitor and adhere to budgeted costs.

cost of capital The rate of return on a company's investment that is necessary to maintain its share price—the costs of its debt and its equity against its income.

cost of goods sold (COGS) Also called cost of sales. The actual cost to the company of its good or services, not the price at which it is sold; the difference is its gross profit.

cost-of-living adjustment (COLA) A change upward in an employee's pay because inflation has changed the cost of basic consumer commodities. It is comparatively rare for COLA to appear in a white-collar employment contract, but it is not uncommon in union-driven labor/management contracts.

cost of prediction error The cost involved in a company's failure to predict accurately a component of its budget (e.g., its sales in the current financial year).

cost of sales See cost of goods sold.

cost-plus pricing A common and relatively foolproof way of establishing the price for goods and services. A product or service is priced at its cost (materials, labor, and overhead) plus a profit markup. Say that a product costs $100; the company strives for a 30 percent profit margin; therefore, the price is $130. The term also refers to the kind of contract to supply products/services, the development cost of which is unknown: cost is therefore left open—to a certain limit; whatever the cost, a fixed fee (i.e., the profit) will be added to it.

cost prediction See cost estimation.

cost-price relationship The concept that a price must be competitive yet sufficient to cover all of a company's costs. The most difficult aspect of this relationship is that, while it is usually comparatively easy to determine direct costs, it is often difficult to isolate such less specific costs, per unit, as marketing, sales, or distribution.

cost reapportionment See cost allocation.

cost reduction program Any attempt to cut costs as a way to improve a company's profitability. Companies must be careful in instituting such a policy, to make sure that it is cutting wasteful costs, not costs that are essential. For example, a company may decide to cancel any business lunches; it may turn out that its salespeople are concluding important business deals at such lunches, far greater in value to the company than the cost of the meals.

cost sheet A document prepared for each job as a means of accumulating

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(not missing) any costs associated with a job. It is a means, therefore, of determining what a company's pricing ought to be.

cost variance The difference between what a job is estimated to cost and what it actually costs. It is one of management's primary jobs to ensure that such variances are minimal.

coupon rate The interest on a debt security. That interest is against the face value amount of the security.

CPA See certified public accountant.

creative accounting An ironic term referring to management's attempt to "misstate" certain elements of financial statements to make net income look better than it is.

credit An entry on the right side of any account: revenues as opposed to payments. Also, that which one gives a buyer or borrower in return for the buyer's or borrower's promise to pay later.

credit against tax See tax credit.

credit analysis The process by a lender (usually a bank) of determining whether an applicant (an individual or a business) is a good risk and how much credit can be extended to that applicant without the loan's being risky.

credit balance A term with two meanings: (1) the amount to the good in an account; and (2) an overpaid customer account: the selling company owes the buying company that amount until the buying company makes another purchase, at which point the amount of the purchase is reduced by the amount of the credit balance.

credit line An amount of money made available to a borrower by a financial institution. Although there is often a requirement about what balances must always exist in a borrower's account, credit lines do not involve either collateral or a contract.

creditor An individual or a business that has extended credit to a buyer and is owed for money for those goods or services.

creditors' equity The total amount of a company's liabilities. In the event of a liquidation of the business, creditors are paid before stockholders.

cumulative preferred stock A kind of stock the dividends of which, if not paid when scheduled, accumulate. All such accumulations must be paid before common stockholders can receive any dividends.

current asset An asset that, with rare exceptions, has a life of one year or less.

current cost The price it would cost to replace a company asset.

current liability A debt that a company must pay within one year.

customer response time Also called delivery cycle time. The period from an order's being placed to that order's being delivered to the customer.

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cutoff date In an audit, a nominal date toward the end of an accounting period after which no transactions can be recorded; as well, all transactions that happened before the date must be recorded. Sometimes, a cutoff date can involve stoppage of work in a particular company department (e.g., to ascertain actual inventory on the cutoff date, management of a company may disallow any further shipping of goods for several days until a physical inventory can be conducted).

data privacy Any security measures employed by an accountant/auditor to make sure that confidential records cannot be accessed except by authorized personnel. Most financial data is now computer stored, and the most common security measure is to allow access only to those who have been given a password.

data processing Transformation of raw data into information through recording, classifying, sorting, and reporting. Most such processing is now handled by computers, except in very small firms.

days to sell inventory The amount of time that inventory is held before it is sold. Generally, the longer inventory is held, the greater the chance that it cannot be sold at full price.

debenture A long-term debt that is not secured by a lien on specific property. Because it is unsecured debt, it is generally issued by large and financially sound companies about which there is unlikely to be any doubt, in the minds of investors, about the possibility of repayment.

debit An entry on the left side of an account: expenses as opposed to revenues.

debit memorandum A document sent from a seller to a buyer, notifying the buyer, usually because of an error in invoicing, that the seller is debiting (increasing) the amount of the buyer's accounts payable.

debt and equity securities A dual method of financing a business through debt (bonds) or equity (shareholders' contributions to capital in buying the company's stock).

debt-equity ratio An analysis of a company's financial statements to ascertain the kind of protection available to its creditors (e.g., whether or not the company is overextended in its borrowings against the value of its equity).

debt financing Raising money either by borrowing it from a bank or other financial institution or by selling bonds or notes payable.

debtor Any individual or company that has a legal obligation to pay money to another individual or company.

debt restructuring A change in a company's debt structure, which reflects concessions granted by its creditors, usually involving giving the company more time to pay its debts. Debt restructuring is usually an indication that a company is in financial difficulties. It may be agreed by the creditors privately or it may be imposed on them by the court (e.g., in a Chapter 11 bankruptcy).

debt to net worth ratio See debt-equity ratio.

decision making Choosing between business alternatives as a means to

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achieve a particular objective.

declaration date The day on which a dividend is agreed by a company's board of directors and subsequently announced.

deductions Those expenses that a company is legally allowed to deduct from its income in preparing its financial statements and its tax returns.

default Failure of a debtor to meet principal or interest payments on a debt by a due date. When this happens, the lender may make claims against a company's assets to recover the money loaned.

deferred cost An expenditure that has a future benefit beyond one year.

deferred credit Revenues received by a business that are not yet reported as income. For example, an advance or retainer for a company's services that have not yet been performed, and therefore for which the revenue has not yet been earned.

deferred maintenance Upkeep that has been postponed, which may in turn result in a decline in a company's production or a diminishment in the value (the earnings potential) of an asset.

deficiency Additional taxes that the Internal Revenue Service decides a company owes beyond that which it has reported it owes. If the company disagrees, it may state its case with the IRS. If that fails, the company may appeal to the tax court.

deficit A debit balance in a company's retained earnings account because of accumulated losses.

defined benefit pension plan A plan that sets out the pension benefits that employees will receive when they retire.

deflation A general decrease in prices.

degree of relative liquidity (DRL) The percentage of a firm's expenditures that can be funded with cash generated by simply its normal operations.

delivery cycle time See customer response time.

demand deposits An account from which funds may be drawn at will and from which funds may be transferred by another party by means of a check (e.g., a common bank account).

deposits in transit Cash receipts that arrived at a company's bank too late to appear on the company's current bank statement.

depreciable asset/depreciation One that loses its value over time. For tax purposes, companies are allowed to charge depreciation against the values of their fixed assets.

depreciable life Economic life of a fixed asset. All of a company's fixed assets (except land) may be depreciated.

derivatives Financial instruments that are based on some underlying asset, such as stocks, bonds, commodities, or currencies.

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detailed audit One in which virtually all of a company's transactions and record keeping are thoroughly examined. This kind of audit is much more comprehensive than what is normally done at most companies. It can be provoked by suspicions of illegal activities or as one of the ways of preparing for a major change (e.g., the sale or merger of the company).

development stage enterprise A company that is devoting virtually all of its efforts to establishing itself, one for which there has not yet been any significant revenue.

dilution The weakening of an item in a financial statement. The term commonly refers to the phenomenon of a company's issuing more common stock, thus reducing the equity interest of each common stock that then exists.

direct costs Those that can be easily identified at source (e.g., the direct labor costs or the direct material costs of a particular product).

direct costing The practice of creating inventory value solely on the basis of the costs of labor and materials directly associated with the creation of that inventory..

direct labor Work specifically involved with creating a particular product or service.

direct material That which becomes a crucial part of a finished product.

direct write-off method Writing off a debt when it becomes obvious that a particular account receivable is not collectible. This method is usually unacceptable for internal accounting purposes for the reason that it fails to account in advance for potential bad debts (thus creating a more positive expectation of the company's receivables than is warranted), but it is the only method allowed by the government for tax purposes.

director A member of the board of directors of a corporation. The board, selected by shareholders, is the chief governing body of the corporation, though generally it is not involved with the day-to-day running of the company, which is the responsibility of its senior executives (though, generally, the head executive—the CEO—is a member of the board). The board's responsibilities include selecting a company's corporate officers; declaring dividends; deciding on major expansion or contraction of the company's activities; and advising officers on long-term strategy.

disbursement Payment by cash or by check.

disclaimer Statement by an auditor that a company's accounts provide insufficient evidence that they are correct, or that the auditor has been allowed insufficient time by the client to examine accounts in a way that the auditor believes is mandatory. In other words, the auditor says that it is impossible to provide an audit opinion.

disclosure Explanation provided by a company's officers about the financial position and results for the year, offered either as footnotes or as a separate page(s) of notes in a financial report. Auditors also provide disclosures based on their audit of the company's accounts.

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discontinued operation The abandonment of a particular aspect of a company's business either because that segment has been sold or because it has been purposely shut down for being no longer profitable.

discount A percentage off a list price, which can be offered by a seller to a buyer as an inducement to buy. A discount, a percentage amount, is also sometimes offered for prompt payment of an already rendered bill (e.g., a 5 percent discount, 5 percent off the price) if the customer pays the invoice within 10 days.

discount rate The interest charged by the U.S. Federal Reserve Bank to its various member banks for loans. This rate is less than prime rate. It affects all other U.S. interest rates from prime rate to the rate of interest on mortgages.

discretionary cost Also called managed cost. Any cost that is easily increased or decreased—one that is not a fixed cost (e.g., marketing costs).

disinvestment The decision to terminate an operation—usually because management has decided that the likely revenues from a project will be less than the costs of continuing or maintaining that project.

disposable income Also called take-home pay. The amount of money an individual has left after taxes and other government deductions (e.g., Social Security contributions) have been removed from that person's gross pay.

distress price A discounted price that a company will accept as a way to help avoid severe financial difficulties.

distribution cost Any of the costs involved in fulfilling an order, including warehousing, shipping, and customer service.

distribution to owners Payment of a company's earnings to its shareholders via a dividend.

dividend Periodic distribution of earnings to shareholders. Dividends are declared per individual share.

dividend exclusion The amount a company may exclude from taxes of any dividends it receives from holding the stock of other corporations.

domestic corporation A company that is incorporated in the United States rather than a foreign country.

donated capital An asset offered to a company by a state or local government to encourage that company to relocate to that state or municipality, or to remain there.

double-entry bookkeeping The kind of financial record-keeping that involves two entries for each transaction—a debit and a credit.

draft Also called a bill of exchange. Financial instrument common in international trade in which the seller (the exporter) requests the buyer (the importer) to pay an agreed amount of money at a specified time.

DRL See degree of relative liquidity.

due date A promised delivery date for goods or services.

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earned income Income which is due a person for that person's personal services, including wages, salaries, tips or bonuses, and any fees earned from self-employment. It does not include lodging or food provided by an employer or pension payments.

e-mail See electronic mail.

earned income credit A tax abatement available to low-income taxpayers.

earnings The income of a business in a specific accounting period—revenues less all costs and expenses.

earnings forecast Projection of how much shareholders will earn in the current year (i.e., how much will be earned per share). Such forecasts are usually devised by management and a company's accountants, though sometimes by independent analysts.

earnings per share (EPS) The amount stockholders of a company will earn per share in the current year. This measure is widely used by financial analysts and investors to judge the profitability of companies and to speculate about how they will do in the future. EPS determinations are a less than exact science for the reason that a company can have an extraordinary year (either to the bad or the good) that isn't likely to be repeated.

EC See electronic commerce.

economic life An estimate of how long a fixed asset will continue to provide benefits to a company (e.g., a piece of equipment might be estimated to have an economic life of five years, after which it will have to be replaced). Depreciation is most frequently based on such estimates.

effective tax rate Amount of tax divided by the amount of taxable income. If the tax is $25,000 on income of $100,000, then the effective tax rate is 25 percent.

effectiveness Whether an economic outcome measures up to a company's forecast.

efficiency The accuracy of the cost of each unit produced. For example, the "cost" of preparing a report for a client, based on previous experience, is estimated to be 10 hours, against a quoted fee based on that expectation. If estimated time was accurate, the cost is said to be efficient; if the job takes 13 hours, the cost is said to be inefficient.

EFTS See electronic fund transfer system.

electronic commerce (EC) The buying or selling of goods on the Internet. EC is increasingly a feature of U.S. business life.

electronic fund transfer system (EFTS) System for electronically transferring funds between buyers and sellers. EFTS is also used by many companies to transmit the payroll of their employees directly to employees' individual accounts.

electronic mail (e-mail) A document transmitted electronically from the sender's computer to the receiver's computer via an agency (e.g., America

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Online) that acts as an information center, receiving and forwarding e-mail. The widespread use of e-mail has sped up the process of business-to-business communication considerably.

elements of balance sheet Those components that traditionally appear on a balance sheet: assets, liabilities, and the equity account. The detail for these components appears in the company's chart of accounts.

embezzlement The theft of company funds, usually by someone with direct access to those funds.

employee stock ownership plan (ESOP) A plan that encourages employees to invest in their company's stock. Depending on the extent of their stock ownership, employees may also participate in the management of the company.

encumbrance Debt that has been secured by a lien on a company's assets.

ending inventory Goods on hand that have not been sold as of the end of an accounting period.

endorsement Signature on the back of a check by the payee (recipient) of that check: most banks will not cash a check without such an endorsement. They can be one of three kinds: (1) a straight endorsement, which would allow anyone who came into possession of the check to cash it; (2) a restrictive endorsement, which limits it to the purpose noted—"for deposit to my account," for example; or (3) an endorsement that makes the check payable to another person: this requires naming the new payee above the signature of the original payee.

engagement letter That which a client gives to a certified public accountant (or an outside auditing firm), hiring that CPA to audit the company's books: it generally sets out the terms and responsibilities of the job, cites the fee, and provides a provision for reimbursement of expenses.

entertainment expense deduction A tax deduction allowed companies if these expenses are directly related to the active pursuit of the company's interests and are reasonable and necessary (e.g., a company salesperson taking a potential client to lunch to discuss the company's services). A company may, however, deduct for taxes only 50 percent of such costs.

entity A self-contained economic unit that is capable of financial measurement and is eligible to pay taxes (e.g., a sole proprietorship, partnership, or corporation).

entrepreneur An individual with the initiative and drive to start a business and assume its risks. Customarily, the entrepreneur founds/creates the business and then hires people to work for him or her.

entry Any transaction in an account book.

EPS See earnings per share.

equity Also called net worth. In accounting, equity equals assets minus liabilities. In a sole proprietorship, equity belongs to the owner; in a corporation, it belongs to the stockholders.

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equity financing Obtaining financing by issuing preferred or common stock—or both.

ESOP See employee stock ownership plan.

estimated tax Corporations must remit to the Internal Revenue Service in quarterly payments 90 percent of what they judge their tax to be for the year.

ex-dividend A stock that is selling without having recently paid a dividend.

examination Another term for an audit of a company's financial records.

Excel A popular spreadsheet software created by Microsoft.

excess capacity Machinery and equipment or labor that is not being fully utilized because there are insufficient orders for the products it produces.

exchange A public market for the buying and selling of securities or commodities (e.g., the New York Stock Exchange or the Chicago Board of Trade).

exchange rate The price at which one currency may be traded for another (e.g., on any given day it may require $1.85 to buy one euro; a week later, that exchange rate may be $1.84 to the euro).

excise tax A tax levied on specific products, usually for a particular purpose or goal. For example, such a tax on cigarettes might be used to fund public health care; a tax on gasoline might be used to fund the repair of roads.

exempt income Income not subject to tax (e.g., the interest on various kinds of municipal bonds).

exemption organization An organization that does not have to pay federal taxes (e.g., not-for-profit religious, educational, and charitable organizations).

expected annual activity The projected level of production of goods or services for the coming year. Because such activity depends on consumer demand, it is often difficult to predict.

expenditure Paying with cash, or incurring a liability to pay at some time in the future, for goods, services, or assets.

expenses The "outgoings" of any business, subtracted from revenues to arrive at the company's net income.

extension of time for filing An allowance by the government to file a tax return beyond the normal due date. Typically, the Internal Revenue Service will grant an individual a three-month extension, a company a six-month extension.

external audit/auditor An audit conducted by an outside, independent auditor, not a company employee. The term does not imply that such an audit is conducted away from company premises. Although the auditor may do some of the work at the accounting firm of which the auditor is a member, most of the work must, of necessity, be done on company premises.

external document An item crucial to company record-keeping that

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is produced not by the company but by outside organizations (e.g., the company's checks cancelled by its bank or invoices produced by its suppliers).

extraordinary item Something in a company's accounts that is highly unusual or that occurs infrequently (e.g., a loss as a result of a fire).

face value The nominal amount of a debt or the worth of a security as stated on that security.

factoring Selling one's receivables at a discount to an organization that specializes in collecting debt. The "factor" attempts to collect at full value, and the difference between that value and the discount is the factor's commission on the transaction.

factory ledger A record kept by a factory in which direct costs are recorded (e.g., the cost of materials actually used in the manufacture of a product).

Fair Labor Standards Act (FLSA) of 1938 A federal law that applies to all employees of companies that engage in interstate commerce, including minimum wage laws. Except for very small retail establishments, most companies are involved in trading in more than one state and therefore are subject to minimum wage and other regulations of the act.

FASB See Financial Accounting Standards Board.

Federal Insurance Contribution Act (FICA) The law that covers Social Security contributions and benefits. The taxes withheld from an employee's wages are called FICA taxes, which are based on the current FICA tax rate and on the employee's salary. The employer must match the amount of the employee's contribution. A self-employed person is also responsible for FICA taxes, but pays the entire contribution (i.e., a self-employed person's FICA taxes are roughly double those of a person employed by a company or organization).

Federal Reserve Board/System Created by Congress in 1913, the system is comprised of 12 Federal Reserve District Banks. Its primary function is to determine and administer U.S. monetary policy, which it does by controlling the supply of money and by setting the base interest rate (the rate at which it will loan to commercial banks).

Federal Trade Commission (FTC) The federal agency (established in 1914) responsible for prosecuting unfair competition and preventing monopolies in U.S. business.

Federal Unemployment Tax Act (FUTA) The law that requires employers to pay an unemployment tax based on the size of the company's workforce, which in turn funds unemployment insurance. State and federal governments are involved in the administration of this tax, and some states also tax employees.

fees Charges for services rendered. The term is generally used to describe the remuneration of such professionals as lawyers or auditors, who generally work on a per-job basis rather than for a salary or hourly wages.

FICA See Federal Insurance Contribution Act.

fiduciary Any individual (or organization) who holds or administers property owned by someone else (e.g., an executor of an estate or the trustee of a

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trust fund).

filing status One of four categories in which an individual taxpayer is classified: (1) married, filing a joint return; (2) married, filing separately; (3) head of household; and (4) single. The tax rate applied is determined by an individual's filing status.

financial accounting Information presented in accordance with generally accepted accounting principles (GAAP).

Financial Accounting Standards Board (FASB) The organization with the authority to enforce generally accepted accounting principles (GAAP). That is, although FASB is not a government body, certified public accountants are required to follow its dictates in their auditing and reporting practices.

financial decisions A decision generally considered one of four main types: (1) deciding the appropriate amount of funds to employ in a business; (2) selecting the most appropriate projects; (3) raising funds on the best terms available; and (4) managing revenue sources.

financial future A contract to buy or sell a financial instrument at a specific price at some specified date.

financial planner A professional who specializes in offering personal financial advice to individuals. A financial planner may be a lawyer or a CPA but can also possess licensure, such as certified financial planner.

financial projection A forecast of what a company's budget for the near future and the consequent financing needs.

financial statements A report setting out the financial information about a company. It is itself comprised of three required documents: a profit/loss statement (income statement), a balance sheet, and a statement detailing changes in the company's financial position.

finished goods inventory The amount of product a company has on hand (i.e., has not yet sold to customers).

fiscal year The 12 consecutive months for which companies traditionally (and by law) account for their business operations. Typically, the fiscal year is the calendar year, but some organizations (notably government units) use a different year. The term is also used in taxation to mean any 12-month period other than the calendar year.

fixed asset An asset that produces income, has physical reality, and has a life of longer than one year.

fixed cost A cost that remains constant over a given period (e.g., the rate of taxes).

fixed overhead Anything in overheads that remains a constant, no matter what the level of activity in a business (e.g., rent).

fixed price One set by a contract, which must be adhered to regardless of the actual cost of the goods or services. The term is also used to mean the level at which investment bankers agree to sell a new security.

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fixture An asset that is physically attached to property and that usually cannot be removed without causing damage and therefore loss of value (e.g., built-in shelving).

flat tax At present, a theoretical concept: a rate that would be the same for all income levels, one that would simultaneously eliminate all deductions. If the flat tax was 10 percent of income, a taxpayer earning $50,000 a year would pay $5,000; a taxpayer earning $100,000 a year would pay $10,000. Neither taxpayer would be allowed any deductions.

flextime A scheduling concept: employees are allowed to work hours of their own choosing within limits: rather than a traditional 9 to 5 for office workers, for example, employees could choose to work 7 to 3 or 10 to 6.

float The amount of money in a company's bank account represented by checks that have been issued but not yet been cashed.

floating exchange rate Since 1971, exchange rates between the dollar and foreign currencies have been dictated by the marketplace (i.e., they are allowed to float and are not fixed by their respective governments).

flotation cost Cost, paid to an investment banker in charge of the transaction, of issuing new securities in the public marketplace.

flowchart A chart representing in some schematic way the process of a particular business activity (e.g., the path an order takes through a company from the time it is placed until it is delivered).

FLSA See Fair Labor Standards Act.

FOB See free on board.

footnote The explanatory notes to a financial statement, regarded as a crucial and integral part of that statement. Subjects that footnotes generally cover include accounting policies, pending litigation, and tax matters.

forecast A projection of the likely future performance of any component of a business—sales, costs, earnings—leading to conclusions about the future financial performance of the company as a whole.

foreign corporation A corporation formed under the laws of a country other than the United States.

foreign currency accounting Accounting that includes provisions for the difference between currency exchange rates, when a company has made a purchase from or a sale to a company abroad, between the time that something was purchased and the time at which it was paid for. This gain or loss must be reported in a company's accounts. On income statements it is recorded as "Profit or Loss on Foreign Exchange."

foreign tax credit Any credit allowed against U.S. taxes for taxes that a company has paid in a foreign country.

forgery Acting falsely (e.g., signing someone else's name on a petty cash voucher, and taking funds as if that person had done so).

form of balance sheet The two ways in which a balance sheet is presented: (1) account form—assets are presented on the left, liabilities and owners' equity is on the right; or (2) report form—assets are presented above, followed by liabilities and owners' equity below.

form 10-K The form that publicly traded companies must submit each year to the Securities and Exchange Commission (SEC). Financial statements, supporting documents, important disclosures, and general information about the business are included in this submission.

401(k) plan An investment plan that allows employees to defer part of their gross salary and invest that money in stocks, bonds, or money market funds. The employer commonly provides a choice of investments, and many employers match (partially or wholly) their employees' contributions. The contributions and any of the earnings on plan's investments are tax free until the employee withdraws them, commonly when that employee retires (when the rate of taxation will be lower than it would have been when the employee was working) or when the employee leaves the company—in which case the 401(k) plan can be transferred to a new employer.

franchise The right given by one company to another to use the first company's name to operate the second company's business. The franchisee is commonly expected to have certain cash reserves and to use the franchisor's products. Many U.S. fast-food restaurants are franchises.

fraud Deliberate act by an individual (or organization) to cheat another (e.g., falsifying financial records to cover up an embezzlement of funds).

free on board (FOB) Delivery will be made without charge to the place named.

fringe benefit One provided to an employee by an employer at no cost to the employee; the benefit is in addition to the employee's basic salary (e.g., a health care plan for which the employer pays).

front-end loading The practice of brokerages and mutual funds of taking their fee (for handling the transaction) from a client's first installment payment toward the purchase of shares.

FTC See Federal Trade Commission.

full-cost profit margin The difference between revenues and the entire cost of the product that is being sold, factoring in direct costs as well as those of marketing and distribution.

full disclosure The act of presenting all material facts in the footnotes to financial statements so that any potential readers will, in theory, have no questions about the statements.

full faith and credit A phrase used on government securities to convey that the entire weight (and revenue powers) of the federal government backs up the security (e.g., example a U.S. Savings Bond).

fully vested The acknowledgement that an employee will be entirely entitled to the benefits of a pension plan when that employee retires (i.e., the employee has now qualified for the full extent of this benefit).

function cost Classifying the nature of the expenditure of a particular cost

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(e.g., the marketing cost).

fund Monies or assets that are set aside for a particular purpose—the petty cash fund, for example. When used as a verb: to provide monies, to finance.

funded pension plan A trustee-managed pension plan to which an employer makes contributions and receives payments from upon retirement.

furniture and fixtures A depreciable asset, such as office or store equipment.

FUTA See Federal Unemployment Tax Act.

future value Amount by which an investment will grow if it continues to earn the same amount of interest compounded annually.

GAAP See generally accepted accounting principles.

GAAS See generally accepted auditing standards.

GAO See General Accounting Office.

GATT See General Agreement on Tariffs and Trade.

gain Excess achieved on the sale of an asset over and above the book value that a company has recorded for that asset.

GDP See gross domestic product.

General Accounting Office (GAO) A federal agency that acts as an auditor of the different units of the federal government.

General Agreement on Tariffs and Trade (GATT) A treaty in effect among various western countries: its purpose is to foster international trade relations by encouraging bilateral agreements that reduce tariffs and other trade restrictions. In other words, it is a treaty/agency devoted to free trade among nations.

general and administrative expenses Expenses resulting from management activities within a company (e.g., the salaries of company officers and the fees of lawyers and auditors).

general contingency reserve Retained earnings that are allocated to nonspecific future expenditure for potential as opposed to probable expenditure.

general ledger The central record of a business's individual accounts (i.e., all the accounts that provide the components of that business's financial statements: assets, liabilities, stockholders' equity, expenses, and revenues). A company's general ledger was in the past an actual set of books. Currently, it is more likely to be maintained on a computer.

generally accepted accounting principles (GAAP) The standards and practices that accountants follow in creating financial statements. These standards are to an extent based on convention, but they are codified by publications of the American Institute of Certified Public Accountants. In any audit report, the certified public accountant must assure readers that GAAP have been followed by the client and by the auditor's own staff.

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generally accepted auditing standards (GAAS) Guidelines that are published by the American Institute of Certified Public Accountants (AICPA) that auditors follow in preparing (and certifying) financial statements for clients. Any certified public accountant who does not follow these guidelines is in violation of AICPA rules and can be held legally liable by clients.

general partner A participant in a partnership who is jointly liable for the debts incurred by the partnership.

general price index (GPI) Change in the prices of U.S. goods and services; a gauge that measures the purchasing power of the dollar.

gift tax A tax levied on the transfer from one person to another of money or property (the tax is levied on the donor).

going concern An accounting/auditing assumption that a business will continue in existence because, having been subjected to testing by an auditor during an annual audit/review, its finances seem sound.

going-concern value That value which a company possesses for a potential purchaser over and above the book value of its assets (the difference between the two sums is referred to as goodwill).

going public See initial public offering.

golden parachute A lucrative contract offered to a senior executive as an inducement: the executive gains compensation (a large bonus, stock options) if his or her job is lost as a result of a merger or acquisition. Sometimes these contracts involve so much money as to be a disincentive to would-be purchasers, which can be one of their purposes in the first place.

goods Raw materials or finished products. Sometimes the term is used to refer to all assets, including cash and fixed assets.

good and services The sources of revenue for a business.

goods-in-process inventory See work-in-process.

goodwill The difference between what a purchaser is willing to pay for a company and the market value of that company's assets. The term usually refers to a company's value (above ordinary asset value) for such intangibles as a company's reputation, the regard with which it is held in the marketplace, its competitive edge, and the likelihood that it will have good future earnings. Goodwill is regarded as an intangible asset that must be amortized over a period of years after the purchase.

greenmail A company targeted for a takeover buys back its share at a premium from the would-be purchaser. In return, the purchaser agrees to call off the takeover.

gross domestic product (GDP) The dollar value of all the goods and services produced in a particular period during a specific period of time, usually the prior year, by all U.S. enterprises. This figure also includes government spending.

gross income See gross profit.

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gross margin See gross profit.

gross profit Sales minus the direct cost of those sales before any other expenses are subtracted. When expenses are subsequently subtracted, the result is called net profit or net income.

gross sales Total sales before discounts or any reductions for returns.

growth stocks Those of young companies with no real earnings record but with the potential for rapid expansion and increasingly good sales. The term is often used currently to refer to high-tech or biotech companies, most of which are believed to be rapid-growth industries.

hacker A computer whiz who attempts to break into and damage a computer system. A hacker's motivation is endlessly debated, but most people would agree that part of that motivation is the self-esteem engendered by being clever enough to accomplish such a feat against formidable odds.

half-year convention A tax rule: a newly acquired asset is in service for at least one-half of the tax year no matter when it was placed in service.

hard copy Output from a computer that is printed on paper and can be filed in a conventional way. Many companies that use computers for accounting functions still routinely produce and file a hard copy backup.

hardware A computer term: the electronic devices that comprise a computer. See software.

head of household One of the four categories of U.S. taxpayer: an unmarried person who maintains a home for a dependent relative (or relatives) and contributes at least 50 percent to the cost of maintaining that establishment.

hidden reserve An understatement of owners' equity or net worth.

historic cost The price of an asset plus the additional expenses of bringing it into use. Examples of these additional expenses would be transport costs or costs of installation.

holders of record Owners of a company's stock, as registered in the company's stock register.

holding company A corporation that holds more than 50 percent of the stock of other companies, thus effectively controlling them.

holding gain/loss An increase or decrease in the value of an asset or a liability during a particular accounting period.

home office deduction A deduction allowed a taxpayer for maintaining an office in what is otherwise the taxpayer's home. The requirement is that stated portion of the home is regularly used for office purposes.

human resources accounting A type of accounting that places a value on the company's employees and includes that value in its balance sheet. Regarding people as assets is fairly uncommon in most companies; the practice usually occurs only in firms of professionals (e.g., lawyers,

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accountants, consultants, and advertising account executives).

IBRD See International Bank for Reconstruction and Development.

ideal capacity The best output possible if a company is operating at maximum efficiency with no problems.

idle capacity Unused potential to create goods or services, usually the result of a deficiency of materials or manpower.

idle time The cost of direct labor when employees are unable to do their jobs because of equipment failure or shortage of materials or a natural disaster.

illegal act An audited entity's breaking of the law.

illiquid A company that lacks immediate cash or working capital.

IMF See International Monetary Fund.

impairment of asset value The decline in the worth of an asset because it is less useful than it was in producing income.

impairment of capital An excess of liabilities over assets because of losses.

impound To take possession of money or property as a result of a legal action (i.e., a court has made an decision, allowing such possession).

imprest fund See petty cash fund.

improvement An expenditure that extends the life of an asset or in some way improves it. Such an improvement is regarded as a capital investment and can be capitalized. An example would be upgrading a group of computers by installing an in-house server. (Simple repairs, however, are not regarded as improvements and cannot be capitalized.)

incentive stock option (ISO) A benefit offered to employees that allows them the opportunity to buy shares of company stock at a particular price during a specified period of time. The great advantage of this kind of option is that it is not taxable when granted or when the option is exercised, but only if the stock is subsequently sold and if, when sold, it involves a capital gain. There is a limit on stock options of $100,000 per employee in any one year.

income Money earned during an accounting period, resulting in an increase of total assets. An excess of revenues over expenses within a given period.

income deduction The nonoperating expenses of a business; they are listed in the final section of an income statement just before net income. They are not subject to the company's day-to-day control and include such items as interest and taxes.

income statement See profit and loss statement.

income tax The government levy on the annual earnings of an individual or a business entity. The maximum corporate tax is 35 percent.

incorporation Legal existence of a corporate entity (i.e., recognized by

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the state and allowed to operate according to the corporation's articles of incorporation). All incorporated entities share certain characteristics: limited liability of shareholders; paid-in-capital; independence of operation from stockholders; and a name protected from use by other business entities.

indenture A legal document that states the terms and conditions under which a bond has been issued and the rights of the bondholders (i.e., the guarantees of the issuing corporation).

independent accountant A certified public accountant who has no financial interest in, or other connection with, clients who have retained that CPA to audit their financial statements.

independent auditing The concept that an auditor objectively evaluates a company's financial records and prepares financial statements and audit opinions without any subjective bias.

indirect cost Any expense that it is difficult to assign to a particular activity within a company.

indirect labor That which is not directly involved in the creation of a company's goods or services but is crucial to the company's continued functioning—the work of cleaning staff, for example.

indirect liability See contingent liability.

indirect tax One that is collected by a company but not actually paid by that company (e.g., a sales tax added on to the price of goods and collected by the company from consumers, which in turn the company then remits to a taxing authority). The company has not actually paid the tax itself.

individual retirement account (IRA) A personal retirement account funded by an individual with tax-deductible deposits. IRAs are the federal government's way of encouraging people to save for a supplement to their Social Security retirement benefits.

inflation A general rise in the level of prices. When inflation is rampant, people tend to prefer investment choices such as property as opposed to stocks or bonds.

information cues Those kinds of information regarded by auditors as most reliable as a basis for forming their judgments about a company's financial condition (e.g., cues from third parties are regarded as more reliable than cues from a company's own management team).

information return Any kind of return filed with the Internal Revenue Service that does not require the payment of taxes (e.g., a W-2 form for an employee).

initial public offering (IPO) Also called going public. The means by which shares of common stock are first offered for sale in public markets (via the exchanges or via over-the-counter methods).

input cost Any direct cost involved in the creation of a product or a service (e.g., the employee labor involved in producing the product or service).

inside director A member of a company's board of directors who also

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works for the company, as opposed to an outside director, who is not an employee of the company.

insider information Facts achieved by a corporate director, officer of the company, or shareholder, who, given the opportunities of his or her position, obtains knowledge that may be used primarily for personal gain or that of someone else with whom this person is closely associated. For example, this person knows that the company earnings for the year will be bad, and, in advance of the publication of those results, sells stocks at a price higher than they will command after the results are published.

insolvency Inability of a company to pay its bills and meet its other financial obligations as they become due. This condition usually leads to bankruptcy.

installment sale A sale in which the buyer is allowed to pay the seller with staged payments over time. A contract is usually involved.

institutional investor Any entity that trades large volumes of securities (e.g., a pension fund or a mutual fund). A very high percentage of the trading of U.S. exchanges each day involves buying and selling by institutional investors.

insurance A contract, called a policy, that one party, for an agreed periodic sum, called a premium, will pay the other party a sum of money if some contingency transpires (e.g., the loss of property of the insured party).

intangible assets Assets that have no physical substance yet are of value to a company (e.g., goodwill) or one that represents a right (e.g., a patent or a franchise).

interest The amount charged by a lender to a borrower for the use of the lender's funds. Also, the equity ownership in a business by either an individual or another company.

interest deduction The cost paid by a business for the use of funds, which amount may in turn be deducted from taxes.

interest on investment The expected return on any debt instrument.

interest rate The percentage per annum charged by lenders to borrowers, which may be fixed or variable (i.e., may change as various interest rates change). Lenders usually give their best customers prime rate; other customers pay prime plus a percentage above prime.

interim audit A periodic audit performed by a company's accountants as opposed to the end-of-year audit performed by an outside certified public accountant. The purpose of an interim audit is to determine whether a company's various financial systems are effective or to prepare in advance some of work necessary for the end-of-the-year audit.

interim financial statement A statement prepared by a company's accountants, usually monthly or quarterly, to give management an idea of how well the company is performing in terms of its forecasts.

internal audit An audit performed by a company's own accountants, usually as a guide to management.

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internal controls Those checks and balances that a company imposes on itself to ensure that its financial record-keeping is adequate and correct.

internal document Record of a financial transaction created by a company (e.g., its invoices to buyers). The outside auditor relies more on external documents because they come from independent sources.

internal rate of return (IRR) A complicated calculation in accounting, the purpose of which is to determine whether an investment will earn more than the cost of the capital needed to fund it.

Internal Revenue Code The federal tax law of the United States, which includes the rules and regulations that must be followed by taxpayers, both individuals and businesses.

Internal Revenue Service (IRS) That branch of the federal government in charge of collecting most kinds of national personal and corporate income taxes. Through the U.S. Tax Court, the IRS can also prosecute a taxpayer. If the IRS suspects wrongdoing on the part of a taxpayer, it may also audit that taxpayer. IRS audits of business tend to be time-consuming and extensive, often involving more than one year's returns.

International Bank for Reconstruction and Development (IBRD) Also called the World Bank. The agency that assists countries in need, usually developing countries, to strengthen their economies. It makes loans to the governments of those countries for different purposes, but most IBRD loans are for infrastructure work.

International Monetary Fund Established at the end of World War II, this agency monitors the international financial system, intervening when necessary (e.g., it lends to countries that are having temporary deficits and are unable to meet their international obligations).

Internet A worldwide system of linked computer networks that allows businesses to use such facilities as electronic mail.

inventoriable cost See product cost.

inventory A company's goods on hand (or in transit or on consignment) at any particular time. A physical count of inventory usually occurs at year's end to resolve any discrepancy between what a company shows on its books and what is available for sale (i.e., is not damaged or miscounted).

inventory reserve A portion of retaining earnings set aside as a buffer against any future decrease in the value of inventory because of price declines in the marketplace.

inventory valuation Any calculation of how much various items of inventory are worth, including materials, work-in-progress, and finished goods.

investment The purchase of the securities of another company. Also, the act of spending money to acquire any capital asset that creates revenue.

investment banker The intermediary who buys new securities from a company and then sells them to investors. The investment banker buys the securities from the company for less than the sales price and is then compensated by the difference between the two prices.

invoice A bill prepared by a seller of goods or services and given to the buyer, as the buyer's notification that payment should be made.

involuntary bankruptcy Bankruptcy provoked by a petition of a company's creditors, not by the company itself.

involuntary conversion The loss of an asset in a unique or unexpected way—a loss because of violent weather, for example.

IPO See initial public offering.

IRA See individual retirement account.

IRR See internal rate of return.

IRS See Internal Revenue Service.

ISO See incentive stock option.

issued capital stock Shares that have been issued, and recorded as issued, by a company.

itemized deduction A deduction that can be subtracted by a taxpayer from gross income (e.g., the interest on a mortgage).

JIT See just in time.

joint and several liability A phrase in certain contracts meaning that all the signatories to that contract can be half responsible for its obligations either as individuals or as a group.

joint return The annual tax statement filed by a married couple as if they were a single economic entity; that is, their total income is regarded as earned by both equally, even if one of them has in reality earned nothing. The tax rate is more advantageous than if each had filed separately.

joint tenancy Also called joint tenancy with right of survivorship. Two or more persons who own real or personal property equally. Upon the death of one of the joint tenants, the property passes to the survivor(s); it does not become part of the deceased's estate.

joint tenancy with right of survivorship See joint tenancy.

joint venture Two or more companies that join together for the purpose of completing a particular project.

journal Book (or computer record) where business transactions are first recorded, chronologically, before being posted to individual accounts in a general ledger.

Journal of Accountancy The leading professional journal in the United States for accountants, published by the American Institute of Certified Public Accountants (AICPA).

judgment A court order to pay money. Also, an auditor's opinion of a company's financial records.

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junior accountant In an accounting firm, someone who is not yet allowed to work on his or her own and is subject to the supervision of a senior member of the firm.

junk bonds See bonds.

just in time Inventory that is manufactured (or acquired) only as it is needed for use or to be sold.

Keogh plan A retirement plan for self-employed individuals who may defer taxes (up to a certain limit) until they withdraw funds (their contributions and the earnings on those contributions) during their retirement. The current annual maximum contribution is $40,000.

labor-intensive A company in which labor costs are greater than capital costs.

land Real property that is owned for its immediate productive use or as an investment. Land is not subject to depreciation because it is not an asset that is “used up.”

L/C See letter of credit.

lead time The time involved between placing an order and having it delivered.

learning curve A chart/graph that shows an individual’s progress at mastering a particular business skill. The term is also used in a more casual sense, meaning the length of time it takes someone to learn how to do something.

lease A legal agreement: an owner (the lessor) allows a renter (lessee) to occupy the owner’s property for a specified period of time in return for paying a monthly fee and for observing certain terms and conditions.

ledger A written or electronic file in which all of the accounts of a business are kept. The transactions are listed chronologically in a journal and posted to the individual accounts of the ledger. The ledger in turn provides the basis for the income statement and the balance sheet.

legal capital Stockholders’ equity, the par value of shares times the number of shares a company has issued. Legal capital can be increased, but it cannot be reduced (e.g., by paying out a dividend).

legal liability The responsibility of an accountant to his or her clients and anyone else relying on the results of the accountant’s work (accountants can be sued for fraudulent or careless work). Also, the obligation to pay a certain amount of money to a company in return for having received goods or services from that company.

lessee An individual or company paying a rental fee to a landlord in return for the right to occupy real property.

lessor Owner of real property who gives someone else the right to occupy that property in return for a rental fee.

letter of credit A document issued by a buyer’s bank that guarantees

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payment to the seller (up to a stated limit) for merchandise when that merchandise is delivered. In other words, the buyer's credit is replaced by that of a bank, which is a comfort to the seller who may or may not be familiar with the buyer but will be familiar with the reputation and stability of the bank. Letters of credit are often used when the buyer is in one country and the seller is in another.

letter of recommendation A letter from an auditor to the auditor's client, usually presented at the same time as the conclusion of the audit: it contains the auditor's observations on the client's accounting procedures and includes suggestions for improvements.

letter of representation A mandatory document, presented by a client to that client's auditors, stating that the financial statements, as prepared or sanctioned by management, and given to the auditors as a first but crucial step in the audit, are a true reflection of the company's financial position.

leveraged buyout The acquisition of one company by another in which the assets of the target company are used as collateral for loans to the acquiring company, enabling it to accomplish the takeover. These loans are paid back by the earnings of the acquired company. The term is also used of a company using its own assets as security for loans to accomplish a takeover.

levy Collection, usually by the government, of a specified amount (e.g., a tax levy).

liability The obligation to pay funds for goods or services received. The person or company having a liability is called a debtor. Liabilities can be of three kinds: an actual liability is one that exists—goods/services have been received, and an invoice has been rendered; an estimated liability is one that is certain to exist but the precise amount is unknown (e.g., taxes on a business for the year); and a contingent liability is one that may or may not occur (e.g., a shipment is for the moment lost; it might not be found and would have to be replaced).

lien The right of some person or organization to hold someone else's property as security that a debt will be paid. Liens are imposed by the government (e.g., a tax lien imposed by the Internal Revenue Service). Liens can also be private: the most common example is a mortgage, in which the

lender has a lien on the property (can collect by selling the property if there is a default) until such time as the borrower has paid off all the principal and interest on the property.

life cycle The progress of a company (or its products) through the phases of development, growth, maturity, and decline.

life-cycle costing The estimate of a product's revenues during its expect life cycle against its expenses.

limited audit An audit that covers selected accounts and transactions.

limited liability Liability that does not extend beyond the owners' investment in a business; that is, the owners can lose that investment, but they are not held responsible for the debts of the business. Corporations and limited partnerships are limited liability business structures; sole proprietorships and usual partnerships are not.

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limited liability company (LLC) A business structure in which personal liability is limited, as it is in a corporation. It otherwise operates as a partnership: the partners—called “members” in an LLC—are allocated the profits (or losses) of the company, depending on their ownership stake, and they, not the LLC, are responsible for taxes on profits or may use losses to offset any other income.

line of credit A bank’s agreed obligation to make loans to a company up to a specified maximum for a specified period of time, usually one year. A line of credit is typically operated in conjunction with a company’s bank account (i.e., if a company needs additional funds, these funds are deposited in the company’s current bank account).

liquid Having cash or assets that can easily be converted to cash (e.g., publicly traded shares) adequate to cover one’s immediate or short-term obligations.

liquid asset Cash or a security that can be readily converted to cash.

liquidation Closing a business by selling its assets, paying off its liabilities, and distributing any remaining proceeds to its owners.

liquidation accounting A form of financial reporting that abandons some of the usual procedures of financial statements in favor of a system that records balance sheet items at their sell-out value.

liquidation value The amount that assets are likely to bring in a sale when a company is going out of business. It is almost always the case that this amount is less than could be achieved from a more orderly sale over a greater period of time.

liquidity A term to express whether a business has the funds or assets that can be easily converted to funds to cover its obligations when they are due.

listed securities Stocks and bonds that are traded on one of the main public securities exchanges, as opposed to unlisted securities that are those traded in the over-the-counter market.

LLC See limited liability company.

loan An agreement between a lender and a borrower by which the lender will loan the borrower cash in return for interest and an agreement to pay back the cash by a certain date.

lockbox A U.S. Post Office box used to collect remittances from customers. The recipient’s bank collects from the lockbox at least once a day and immediately deposits the proceeds in the recipient’s bank account. The advantage for companies is that their funds are more quickly available than they would be if remittances were mailed to their offices. The disadvantage is that the service is usually expensive.

log A record of the usage of a piece of business equipment.

long-term asset/long-lived asset An asset that is expected to be of value for a number of years (e.g., an office or factory building).

long-term debt Money that will be owed for longer than one year.

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long-term liability A liability that will be payable for longer than one year (e.g., a five-year lease of equipment).

loss A situation, in any accounting period, when there are more costs and expenses than there are revenues.

loss carryforward The practice, allowed by U.S. tax laws, of using a loss from one year to offset profits in following years; a loss may be “carried forward” for 20 years.

mainframe A large computer that can support more than 100 users at one time.

maintenance Keeping equipment in good repair to ensure it continues to perform. Maintenance is regarded as an expense, not a capital improvement.

managed cost See discretionary cost.

management advisory services (MAS) Consulting offered to clients by many firms of certified public accountants to improve the efficiency of management in such areas as financial planning. Usually, the CPA’s MAS department is separate from the tax or audit divisions within the firm.

management review An evaluation by a company’s external auditor of that company’s management and how well it is performing to achieve earnings and growth.

manager A senior member of a company’s staff who is in charge of some department or division of the company and whose duties are to plan and control the operations of that department/division. The term is also used of the lead auditor in any external audit.

manufacturing costs Expenses associated with the creation of a product. There are three components: materials, labor, and factory overhead.

margin A technique used by some investors: the investor purchases stocks or commodities from a broker with a down payment but not the full amount due. The broker retains the instruments as collateral and charges the investor interest on the money owed. Buying on margin is a speculative investment strategy: if the price of the instrument rises, the investor can sell, pay off the broker, and pocket the profit. If the value of the instrument declines, the investor has lost money, as the investor is committed to paying the broker the original sale price.

margin of safety The difference between actual sales and the sales required to “break even” (i.e., pay for the cost of those sales). It is therefore the amount by which sales may drop before a company experiences a loss.

marginal income See contribution margin.

markdown Any reduction in the original sale price of an item. There can be many reasons for a markdown, including excessive inventory, less aggressive pricing elsewhere in the marketplace, damaged costs, or a company’s need for immediate increased cash flow.

market value/market price A price at which sellers agree to sell and potential buyers agree to buy.

marketable securities Equity or debt instruments that are easily tradable and that can be readily converted to cash if necessary.

markup The amount added to the basic cost of an item to achieve a selling price. The term is also used to convey a particular practice in the wholesale/ retail world. The manufacturer sells a product to a merchant at a particular price—the wholesale price; the merchant “marks it up” to the retail price and sometimes sacrifices that markup during a sale in order to maximize cash flow.

MAS See management advisory services.

master budget A projection in the form of financial statements, referred to as pro forma statements because they are a “guesstimate” of how well a company will do in the next financial period—usually the next year.

materiality An omission or mistake in financial statements that is significant in its consequences.

maximum tax The highest rate that could be assessed on an individual or on a company.

meal expense deduction The amount allowed by the Internal Revenue Service for meals that have a business purpose. No deduction is allowed unless business has actually been discussed during the course of the meal, and many people are still unaware that the deduction may be only 50 percent of the cost of the meal.

menu When used in regard to computers, a term meaning the list of tasks that a particular program can perform or the list of services available from an online service.

merchandise inventory Any goods that are acquired for resale. A merchant acquires goods from a manufacturer for resale to the public.

merger Combining two or more companies, with one company (typically) retaining its previous identity. A larger company will often buy a smaller company (or companies) by making a direct offer to the smaller company’s management or by purchasing a controlling interest in the shares of the smaller company.

minimum cash balance The amount of cash a company needs to avoid a cash shortage, usually calculated by estimating likely sales against potential expenses.

monetary item Any asset or liability, the value of which is fixed in dollars at the time of a purchase was made or a liability was incurred.

money market The market for short-term (less than one year) debt instruments.

money order A check issued by a bank (or other financial institution), made payable to a particular person or company, after the person requesting the check (an individual or company) has given the bank matching funds in return. Sellers who are unfamiliar with the buyer often ask for a money order

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because it is payment guaranteed by a financial institution.

mortgage A lien securing a loan that has as its collateral real property: the lien stays in place until the loan, and the interest on that loan, has been completely repaid.

multitasking Managing two or more tasks at the same time.

mutual fund A spread of securities managed by an investment company that issues shares in this portfolio to individual investors. The investment company may or may not charge on commission on the sale of shares (one that charges a commission is referred to as a “load” fund; one that does not is a “no-load” fund), but it will always charge a management fee to investors who retain share ownership in the fund. Investors are attracted to mutual funds because such a fund guarantees a diversification of risk and professional management.

NAA See National Association of Accountants.

NASD/NASDAQ See National Association of Securities Dealers.

National Association of Accountants (NAA) Professional association comprised mainly of accountants who are not certified public accountants.

National Association of Securities Dealers (NASDA) The organization of brokers who handle over-the-counter securities (i.e., those not handled by the traditional stock exchanges). The association is self-regulating, and it operates a computerized system that provides running quotes on the price of OTC securities. The system is known as NASDAQ (National Association of Securities Dealers Automated Quotations).

negative assurance The guarantees that certified public accountants give to various users of company financial statements that everything they have reviewed is correct. The assurance is negative because the CPA is effectively saying that nothing adverse has come to the CPA’s attention, or that of the CPA’s staff, during the course of an audit.

negative confirmation A request from a certified public accountant to a company debtor or creditor asking for confirmation that the company’s records are correct: the confirmation is negative because the debtor/creditor need respond only if there is a disagreement with the company’s records.

negligence Failure on the part of an auditor to audit a company’s records according to usual standards of precision and diligence.

net income Also called net profit. Revenue less all costs and expenses.

net loss Amount by which revenues for any given accounting period are less than costs and expenses.

net operating loss (NOL) Amount by which operating expenses of a business are greater than its operating revenue over a particular period of time.

net proceeds Amount received from the sale of goods/services, less the costs of making that sale. The term is also used to describe the amount received from the sale of securities, less the cost of bringing that sale to the

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market.

net profit See net income.

net realizable value The proceeds of the sale of an item in inventory, less the costs of making that sale. Also, accounts receivable, less the cost of collection and an allowance for doubtful accounts.

net sales Gross sales less an allowance for returns.

net working capital A company's current assets less its current liabilities.

net worth See equity.

New York Stock Exchange (NYSE) The leading U.S. exchange for the buying and selling of securities, located in New York City.

next-in, first out (NIFO) A method of valuing inventory that uses the cost of replacement rather than the original (historic) cost. This method is not a common one.

NIFO See next-in, first out.

NOL See net operating loss.

nominal interest rate The amount published on the face of a debt instrument or loan—that which will be charged to the borrower.

nonprofit organization Such organizations as charities, religious institutions, and educational entities that operate on the basis that profit, if any, will not be shared with investors. Most such organizations are exempt from federal income taxes.

nonpublic company The stocks of the company are not traded on either the country's stock exchanges or in the over-the-counter market.

nontaxable investment income The interest on a tax-free municipal bond, which does not have to be included in taxable income on a tax return.

normal spoilage That which is to be expected, and is anticipated, in the manufacture of any product.

note payable A document that includes a promise to pay money at a future date. The payment always consists of principal and usually interest as well.

not-sufficient-funds check (NSF check) Check not covered by funds in the account on which it is drawn. Payment is denied to the payee, and the check is generally returned from the payee to the individual or company payer. Generally, because NSF checks are a serious occurrence, banks will not resort to this action with client companies without a conference with the company involved.

NSF check See not-sufficient funds check.

NYSE See New York Stock Exchange.

objectives of financial reporting/statements To provide information that will be useful in making financial decisions. Financial statements should

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provide reliable information on a company's financial position, its operating results, and the changes in its financial status, all of which should help its management to make informed decisions about the future.

objectivity Freedom from any kind of bias in making accounting decisions.

obsolescence An irreversible decline in the value of an asset, resulting from market changes or changes in technology

Occupational Safety and Health Act (OSHA) Administered by the U.S. Department of Labor, OSHA is a federal law that mandates the standards that employers must maintain with regard to their health and safety of their employees.

off-balance sheet asset An asset that is expected to have some future benefit for the company, though the date on which that benefit will occur is imprecise (e.g., a carryforward tax loss that one day the company expects to be able to use). Such assets are not recorded on a company's balance sheet.

off-balance sheet liability A liability that may transpire at some point in the future and, given the imprecision of the occurrence, is not included in the company's balance sheet (e.g., the company is threatened with litigation that may or may not happen, or, if it does, may not result in a judgment against the company).

Office of Management and Budget (OMB) The advisory body, with management and accounting responsibilities, within the Executive Office of the President of the United States.

OMB See Office of Management and Budget.

on account A sale or a purchase on credit. Also a partial payment on a long-term obligation.

online searching Using a computer to search for information on the Internet.

open account An account that is in force (i.e., the account is a reflection of current or expected trading).

open-book management A method that attempts to involve all employees in improving the financial performance of a company. Employees are given access to the company's financial information and budgeting and are allowed to comment on its operating procedures.

opening entry A term that refers to the first entry in the commencing financial records of a new enterprise, to the establishment of a new account within an existing enterprise, or the first balance at the opening of a new accounting period.

operating cycle The time period, on average, between buying inventory and receiving cash proceeds from its eventual sale.

operating expenses Those that are associated not with the production but with the selling and administrative activities of a company. They are a period cost (i.e., they refer to a time period rather than to the creation of the product).

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operating income Revenue less cost of goods, less any expenses related to the normal operations of the company. Operating income does not include investment income or interest income or expense.

operating loss A monetary loss that occurs when revenues are less than the combined cost of goods sold and operating expenses.

operations The activities involved with the production of a company's goods or services.

opinion An auditor's evaluation of a company's internal financial controls to determine what aspect of those controls must be "tested" in any audit.

option Generally, the right to sell or buy something at a particular price within a particular period of time. One of the most common is the employee stock option, in which employers may buy company stock at a below-market price.

order entry The first step in recording a order received or placed.

ordering costs All the costs associated with creating a purchase order.

ordinary income Earnings attributable to the usual operations of a company.

organization chart A chart that shows a company's reporting structure.

organizational costs Those costs incurred in setting up a business (e.g., lawyers' fees, registration fees, and deposit on premises).

OSHA See Occupational Safety and Health Act.

OTC See over-the-counter market.

outlay Any expenditure.

out-of-pocket cost Cash outlays for any accounting period (e.g., the cost of advertising).

outside director A member of the board of directors who is not an employee of the company.

outsourcing Acquisition of products or services from outside sources as opposed to producing them within the company making the acquisition. One common kind of outsourcing is having a company's payroll prepared by an outside organization expert at the task.

outstanding capital stock Shares that are owned by shareholders.

outstanding check A check that has been issued but has not been presented to the bank (by the payee) or has been presented and has not yet cleared.

over-the-counter market (OTC) The market for the buying and selling of shares that are not listed on the country's major stock exchanges. Typically, buying and selling is via computer. Dealers are called "market makers."

overdraft A company draws money against a previously established line

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of credit and is charged interest on the daily balance of its drawings. The borrower pays interest on the money actually drawn, not on the full overdraft amount.

paid-in capital Stockholders' equity, plus any premium (price above par) they may have paid for the stocks they hold.

paid-in surplus Paid-in capital that is in excess of the par value of the stocks themselves.

paper profit Profit that is not yet realized, the result of holding an item (an asset or a share) that has increased in value from its original cost rather than selling it to realize the gain.

par value The value assigned to a share of stock by a new company; this amount is printed on the stock certificate.

parent company The owner of a subsidiary company or companies. The parent company may be a holding company—that is, one that does not trade itself but administers the activities of its subsidiaries.

participative budgeting Allowing key employees in various of a company's departments to provide contributions to the budget process.

partnership A kind of business organization in which two or more persons contribute capital and their services to the organization. It is easy to form, but the disadvantage to some people is that partners are personally liable for the debts of their operation, unlike corporations, in which owners' risk is only that they may lose their equity (i.e., the money they have paid for their shares).

password A series of characters (letters or numbers or both) that permits access to a company's computer system. The object of a password is to prevent unauthorized persons from seeing a company's confidential data, particularly that having to do with its finances.

patent An exclusive right, mandated by the federal government, to allow a particular company the right to use, manufacture, or sell a product/process for a period of 20 years. Usually, the individual or company holding the patent has invented the product/process.

payable An amount owed by one party to another party—a debt, a liability on a company's balance sheet.

payment in kind Exchanging goods or services rather than paying for them in cash: in other words, one person (or company) performs a service for another person (or company) and they return the favor with goods/services of equal value.

payroll costs Those costs incurred for employees' services, including employees' compensation, FICA costs, and benefit plans.

payroll taxes Those taxes applied to employees' salaries (or the net income of self-employed individuals). Social security taxes are also imposed on employees, with employers responsible for a matching amount. Employers also pay unemployment taxes based on the number of their employees.

PE See public accountant.

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P/E ratio See price-earnings ratio.

penny stock A slang expression for a very inexpensive stock. It is inexpensive because it is usually highly speculative, issued by a company with almost no trading record or a longer-lived company with a bad trading record.

pension fund A retirement fund set up and administered by a trustee for the benefit of a company's employees. Employees contribute to the fund, and very often employers contribute or, in some instances, are the sole contributors. The pension fund and its earnings are retained by the trustee until individual employees retire.

pension plan A retirement plan administered by the employer in which the employer provides employees a guaranteed retirement income. The employer may deduct these expenses from taxes.

per diem On a daily basis. An accountant may charge on this basis, and some companies fund their employees on a per diem basis for food and lodging when they are traveling on business for the company.

performance audit An appraisal of how well a particular activity or department within a company is contributing to the company's long-term strategic goals.

period cost/period expense An expense that is not directly connected to the production of a product and therefore cannot be added to cost of inventory. It is instead charged against sales revenue in the period in which it is incurred (e.g., marketing or sales efforts are period costs).

periodic audit Audit of an intermediate period of less than a year—not a company's final financial results, in other words.

permanent file A file consisting of working papers, documents, and schedules created in the course of an audit that can be used and referred to in future audits.

perpetual inventory system A system in which inventory—materials, work in process, cost of goods sold—is monitored on a daily basic. Physical inventory is still taken annually, but companies who maintain a perpetual inventory system believe that the advantage is that they are always aware of their cost of goods and can make price adjustments accordingly.

personal exemption The amount that an individual taxpayer can exclude from taxable income.

petty cash fund A fund maintained to meet small expenditures. The cash is periodically reimbursed, based on the total amount of the vouchers, which together with the remaining cash should add up to the fixed amount of the fund.

physical inventory An actual count of inventory in which number of units times unit costs should yield the value recorded on the company's books. If the two numbers do not reconcile, the book value is adjusted to match the physical inventory value.

plant and equipment/property, plant and equipment The fixed assets used in business operations, including land and buildings.

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pledged asset One that is used as a collateral for a debt.

point of sale (POS) Generally accepted accounting principles (GAAP) require accountants to record revenue in the accounting period in which it is determined to have occurred. For services, that point comes when the services have been performed. For products, it takes place when goods have been delivered.

portfolio Maintaining a variety of securities so that risk is reduced. There are personal portfolios—the mix of securities that a private individual maintains. There are also professional portfolios (e.g., the holdings of a mutual fund).

POS See point of sale.

post To transfer entries from a journal to individual ledger accounts.

postretirement benefits Those benefits, in addition to a pension, that a company may provide to its retirees in good standing. The most usual of such benefits are continued medical insurance or life insurance.

practical capacity The highest level at which a factory can operate efficiently.

precious metals Valuable commodities, such as silver or gold, that are traded as if they were securities. Their prices usually increase in bad economic times and decline in good times—the opposite of stocks. Consequently, investors often move to precious metals when economic times are bad. Tax must be paid on gains made on trading precious metals.

preemptive right The right of a current shareholder in a company to maintain the same percentage of ownership by buying stocks to the extent of that percentage before they are sold to the public in a new stock offering. The purpose is to allow current shareholders to maintain the same level of control—and the same investment stake—as they did before the new offering.

preferred creditor A creditor who has rights beyond those of ordinary creditors in any bankruptcy proceeding because the preferred creditor has secured assets (i.e., collateral).

preferred stock A class that has preference over common stock in the distribution of earnings and in the event of a company liquidation. There is usually a fixed dividend on preferred stock, which makes them preferred over common stock, which, though likely to pay a greater dividend if a company is doing well, pay nothing if the company is doing poorly.

preliminary audit Accounting work done before the actual audit to quicken the process of the audit and the publication of the audit report. For example, the staff in an accounting department might start to analyze accounts receivable balances to clear up any discrepancies before the actual audit begins.

premium A term used in several contexts: (1) amount received above the par value of a security; (2) periodic payments on an insurance policy; (3) the excess not typically paid on a usual expense (e.g., a bonus for an employee); and (4) in a promotional campaign, something given away to call attention to a particular product or service.

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premium on capital stock Any amount over the par value that a company receives in a sale of stock (i.e., the stock sold for more than its stated par value).

prepaid expense An expense that covers something that extends beyond the current accounting period. For example, a company generally pays its rent a month in advance.

price-earnings ratio (P/E ratio) A mathematical calculation: the market price of a share divided by the current earnings per share. Generally used as an indicator of how well a particular business is doing, though fast-growing companies (which are usually young companies) often have very good P/E ratios that they do not sustain in the long term.

prime rate The best interest rate available, that which banks (or other financial institutions) charge their long-term and most solid customers. Other interest rates are often stated as prime rate plus.

principal This term has various meanings, including (1) the owner of a private business firm; (2) the head of firm of certified public accountants; and (3) the amount borrowed (before interest) on any kind of loan.

prior period adjustments Those adjustments that must be made to correct errors in previously issued financial statements. Such adjustments are charged to retained earnings.

private accountant An individual employed by only one organization as opposed to one who works for a firm that serves many different clients.

private corporation/privately held company A company that is owned by only a few individuals; its shares are not publicly traded on any of the country’s stock exchanges.

private placement A sale of stocks in which the issuing company sells directly to an investor without offering them at the same time to the general public via a stock exchange. Usually, this placement is a substantial one: the investor is buying a large number of shares.

privatization The transition in an enterprise when it moves from being state owned to being privately owned (i.e., owned by private investors).

privileged communication Confidentiality, such as that which exists between an individual and his or her lawyer (i.e., lawyers are not legally required to disclose the content of communications with clients). In general, this kind of legal protection does not exist between clients and accountants.

pro forma Any financial document that is considered speculative. Customarily, any pro forma statements prepared by a trained accountant are soundly based on past performance.

pro rata To allocate an expense to a variety of different company cost centers, depending on their responsibility for that cost (e.g., allocating overheads to different divisions/activities of the company).

proceeds Any funds received from the sale of assets or the sale of securities.

product cost The value of inventory, comprised of three components: direct materials, direct labor, and attributable overhead.

product unit cost The cost of a single product, including direct materials, direct labor, and attributable overhead divided by the number of products created in the process.

productivity How well and how cost-effectively a company produces its goods and services.

professional ethics For accountants, those standards of conduct established by such organizations as the American Institute of Certified Public Accountants.

profit and loss statement Also called an income statement. A common form in accounting in which the components that result in net income are calculated. It is always a part of a company's annual report.

profit center A unit of a business that is analyzed for its effectiveness by being measured by the criterion of whether it is profitable.

profit margin The ratio, stated as a percentage, of a company's net income to sales. In other words, if a company's share, after costs/expenses, on a sale of a $100 is $20, then the company is said to have a 20 percent profit margin.

profit-sharing A plan that allows employees to share in some part of a company's annual net income, usually involving criterion such as an employee's years of service to the company.

profit variance The difference between a company's forecast of profit and the actual profit it achieves.

profitability The ability of any company to generate revenues in excess of its costs and expenses (i.e., its net income is positive, not negative).

progress billing Any billing that assesses only a portion of a final, total billing. Such billing is common to long-term projects in which the buyer agrees to periodic payments to reimburse the seller.

progressive tax Any tax that assesses a higher rate as income increases, thus a taxpayer earning $100,000 a year pays a higher rate (on at least part of that income) than a taxpayer earning $25,000 a year. The personal income tax in the United States is a progressive tax.

promissory note A written and signed document in which a borrower undertakes to pay when asked, or at some future stated time, a specific amount of money.

promotional expenses Expenses related to a type of marketing in which tangible goods are given away to potential customers (e.g., a manufacturer of laundry detergent gives away small samples of the product). Such expenses are deductible from a company's taxes as a bona fide advertising/marketing expense.

property, plant, equipment The traditional fixed assets of any business.

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prospectus This term has two meanings: (1) an informational document issued by a company when it is planning a new issue of its stock: it offers potential investors the “story” of the company, a list of its officers, its financial statements, and its plans for the future; and (2) an informational document issued by a company’s director when they plan to sell the company—used for the benefit of potential buyers; it lists much the same information.

provision An expense that must be recognized in a company’s accounts, even though the precise amount of the liability is not exactly known (e.g., a company’s provision for noncollectible accounts receivable).

proxy Any situation in which a person transfers voting rights, via power of attorney, to another individual. The most common of these situations is that in which an individual gives rights to another person to vote the first person’s stockholding when that first person cannot attend a stockholders’ meeting.

prudent investment An investment that is generally recognized as involving little risk (e.g., a U.S. Treasury bond).

public offering The act of offering stocks in a company to the general public via a stock exchange and after registering with the U.S. Securities and Exchange Commission. An intermediary, an investment banker, is usually involved, handling the transaction on behalf of the company.

publicly held company A company that is owned by a great number of investors, the shares of which are traded on one of the country’s stock exchanges.

pull-through production A system in which an order from a customer actually provides the reason for a product to be manufactured. In other words, the company does not maintain inventory but produces its products only on demand.

purchase discount A cash or trade discount. A cash discount is offered in return for a customer’s paying a bill promptly; a trade discount usually is a reward for a high-quantity purchase.

purchase order The form used by a company to acquire goods or services—a formal document (as opposed to a verbal order) sent to a vendor.

qualification Statement in an audit report that the auditor regards something in a company’s financial statements as unverifiable.

quality control In accounting, all the procedures and safeguards an auditor employs to make sure that financial statements are accurate, that they correctly reflect the financial status of the company under review.

quality of earnings The idea that financial statements provide a true and accurate picture of a company’s net income.

quarterly reports Those reports that are issued by companies between their more formal annual reports. Usually, such reports are prepared by a company’s in-house accounting staff rather than outside auditors. They are a useful way of monitoring whether a company is meeting its budget forecasts.

quick asset An asset that could be converted to cash in a relatively short period of time (e.g., a company’s accounts receivable).

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Quickbooks A leading accounting software for small businesses.

rate of exchange See exchange rate.

rate of return on investment The amount, after taxes, expressed as a percentage, that an investment yields on an annual basis.

raw materials inventory The ending balance of goods on hand in any accounting period—goods that can be used in the creation of finished products.

real account A balance sheet item that is carried forward into the following year.

real estate/real property Any property, such as land or buildings, employed by the company in creating income.

real estate investment trust (REIT) A company that manages a real estate portfolio for its investors. REITs qualify for special tax treatment if they have 100 investors and distribute at least 95 percent of their income to these investors, who in turn are responsible for taxes.

real-time system A computer facility that allows instant access to all of the information that it holds.

realization Crediting revenue at the time of a sale of goods or provision of a service.

reasonable test The act of testing whether a particular expenditure in a company's accounts corresponds to its own expenditures in this category in prior years or to industry norms.

rebate A term with three meanings: (1) a refund; (2) a payment, usually in cash, on a portion of a purchase price—an inducement to a potential customer to buy; or (3) repayment of interest to a borrower because that borrower has paid off a loan before its maturity.

recapitalization The process of revising the ratio of a company's capital structure between equity and debt financing.

receipts Cash or other assets received for a company's goods or services.

receivables See accounts receivable.

receiving report A document, prepared by a company for its own internal use, describing all purchased goods delivered to its premises.

recession A decline in the country's gross national product for two successive quarters.

recognition Recording a transaction in a company's financial records.

reconciliation Adjusting the difference between two sets of records (e.g., reconciling the differences between a company's record of its disbursements and revenues during a particular month against that company's bank statement). There is usually a discrepancy because of time sequences: the company records transactions as they happen, but the bank may not yet be aware of all of these transactions (the company has issued a check but it has not yet cleared the bank).

redemption The right of a company to “call in” its preferred stock by paying the holders of that stock its par value plus some kind of additional financial incentive.

refund See rebate.

registered security One for which the owner is recorded in the formal records of the company.

registration statement Extensive statement that a company issuing new securities to the public statement must submit to the U.S. Securities and Exchange Commission. It contains complete facts, historical and financial, about the issuing company.

regressive tax A tax rate that declines as income rises—the opposite of progressive tax. The term is also used of a fixed tax rate that would tend to benefit the wealthy rather than the poor (e.g., a tax on food would be regressive because lower-income individuals spend a larger percentage of their income on food than do the wealthier). Sometimes used in a slang sense, to suggest expenditures that are more likely to affect the poor (e.g., a state lottery, which historically tends to consume the essential income of those who can least afford to lose it).

Regulation S-X A directive of the U.S. Securities and Exchange Commission, it specifies the format of financial reports. It also mandates that companies intending to offer stocks and other securities to the public must provide the sort of disclosure sufficient to allow investors to make informed decisions.

rehabilitation tax credit A tax incentive for those who use or rehabilitate historical structures.

REIT See real estate investment trust.

reliability In accounting, an auditor’s conviction that the financial controls of a company are working properly, that the company’s financial records provide an accurate picture of that company.

rent expense Cost to lease real property.

reorder point Level of inventory on hand at which it is reasonable to reorder (or produce) more stock.

reorganization That which is allowed certain companies that would otherwise be bankrupt—called a Chapter 11 bankruptcy. The company is allowed to negotiate with its creditors to create long-term payments plans; simultaneously, it reorganizes with a view to operating more efficiently in future.

replacement cost The current cost to replace an existing asset with one of the same earnings potential.

report dorm The format of an income statement or balance sheet that reads from top to bottom (assets, followed by liabilities, followed by stockholders’ equity) rather than side by side (assets on left-side, liabilities/stockholders’

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equity on right side).

reporting Furnishing others, usually executives, with financial information on some sort of regular basis (e.g., monthly) that will allow them to make informed decisions.

reporting currency The currency in which a company prepares its financial statements (e.g., U.S. dollars in the United States, euros in France or Germany).

representation letter A written undertaking by the management of a company, to the company's auditors, that management believes its financial statements to be fair and accurate. Also, accepting the responsibility for that accuracy.

research and development costs (R&D) Those costs incurred to gain new knowledge and skills, ultimately to produce new goods or services for a company. The Internal Revenue Service allows companies to deduct 20 percent of their R&D cost increase over an average of such expenditures over the past three years.

reserve That part of a company's earnings that it decides not to pay as dividends but to hold for a designated purpose (e.g., to increase the size of its premises or to provide a "hedge" against what is seen as a likely economic downturn and a potentially high rate of bad accounts receivable).

residual value The estimated current value of an asset, particularly at the end of its life, after all depreciation has been taken against taxes.

resource costs The cost of economic components needed to perform a company's business (e.g., materials, salaries, and office supplies).

restatement Redoing any financial statements to incorporate revisions discovered to be necessary after a first publication of that statement.

retained earnings The accumulated earnings of a company since it started business, less the dividends it has paid out.

retirement Removing a fixed asset from active service (e.g., a piece of equipment that no longer properly functions) or an individual's permanent withdrawal from full-time employment.

retirement of debt Cancellation of a debt obligation because it has been paid.

return on assets A company's net income divided by its total assets.

revenue An increase in the assets of a company (or a decrease in liabilities) that is the result of its operations. This increase may be the result of sales of goods or services or earnings from interest, dividends, and royalties.

revenue bonds Debt (and its interest) that is repaid from the proceeds of a particular project created in the first place by the money that was raised by the bond issue (e.g., a new civic auditorium). Such bonds are generally issued by municipalities.

revenue recognition The way in which income is recorded in an accounting period. The most common practice is to record revenue at the time of the

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actual sale of goods and services.

revenue ruling A statement issued by the Internal Revenue Service clarifying U.S. tax laws.

review An end-of-year accountancy procedure that in its thoroughness falls far short of an audit in that testing is customarily minimal. A review is often elected by small companies that have a comparatively small number of transactions during the course of the year.

revolving fund A fund that is cyclical—it is replenished with money, that money is spent, it is replenished again (e.g., a petty cash fund).

right Any legal entitlement, including an entitlement within a corporate structure (e.g., certain investors right to purchase additional shares before a new stock offering is presented to the general public).

right of return The purchaser may return goods for full credit.

rights offering An offering in which existing stockholders may buy new common shares in a company before they are offered to the general public.

risk The possibility, even probability, that a company will encounter some financial problem, which in turn makes investing in that company a speculative choice.

rollover The movement of funds from one investment instrument to another (e.g., a bond matures, and the bond holder decides to use the proceeds to invest in other bonds).

round lot A unit of trading as specified by a stock exchange. The New York Stock Exchange requires a round lot of 100 shares of stock.

royalties Payment to an owner for the use of property. The term is most commonly used of materials in copyright (e.g., a book the publisher pays the author a royalty, usually a stated percentage of earnings, for the right to publish and sell the author's work).

safeguarding of assets Any means of protecting a company's assets through internal controls established by the company.

safety margin The excess of sales beyond a break-even point. If the break-even point on the sale of a particular product is sales of $100,000, and the current sales are $125,000, then $25,000 is said to be the safety margin. In other words, the company's sales could decrease by anywhere up to $25,000 a month before it was making a loss.

sale Revenue achieved because a customer has purchased a company's goods or services. The term is also used to designate the phenomena whereby a retailer reduces prices to dispose of inventory or raise cash quickly.

sale and leaseback A transaction in which the buyer leases back to the seller the property he has just purchased from the seller. It is a way for the seller to continue to use property and realize cash at the same time—in effect, a form of loan.

sales budget/sales forecast The calculation, per product or services, of

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what a company's revenues will be in the immediate future. It is the most important component of any business plan/budget, because sales are the basis for all other elements of any financial forecasting.

sales discount A tangible allowance given by the seller to the buyer for paying an invoice more quickly than the normal 30 or 60 days—an incentive, expressed as a percentage of the total invoice, to pay early.

sales journal One in which sales are entered and analyzed.

sales tax A local tax (state or municipal) that is added to the price of goods or services that the buyer must pay. The seller does not retain the tax but passes it on to the relevant government agency.

salvage value That price that an asset is likely to command when it is no longer of use to a business. It is generally likely to be a minimal amount.

sampling Using one or more examples of the same financial "type" to determine the characteristics of the whole.

schedule An auditor's working papers, created during an audit; also, the auditor's supporting worksheets, showing how various final numbers were calculated.

scope The subject of a paragraph in an audit report: the auditor sets out the procedures used in the audit, and comments on the financial statements examined.

scrap value See salvage value.

seasonality The phenomenon of a business being affected by the time of year (e.g., a restaurant that does very well just before Christmas but has its worst business of the year in the weeks after New Year).

SEC See Securities and Exchange Commission.

secured liability One backed by assets pledged as collateral, which assets can be sold if there is a default.

Securities and Exchange Commission The U.S. government agency that regulates that regulates the trading of stocks by, and financial reporting of, U.S. corporations.

security The collateral that underwrites a loan (e.g., a mortgage on which the lender has a lien on the property purchased by the borrower) or any financial instrument that declares ownership (e.g., stock in a corporation or an option to buy that stock).

seed money Funds offered to an entrepreneur—often by friends or family, sometimes by venture capitalists—to start a company. Often the willingness of such people to offer seed money in turn influences banks and other financial institutions to offer more formal financing.

self-employment income The taxable income of a person who is self-employed: it comprises all the business income (and losses) of that individual. Such an individual does not pay higher income taxes than a person who is employed by a business or organization, but the self-employed individual

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does pay a higher Social Security tax than someone who is not self-employed. Because the self-employed individual is paying the entire tax, there is no employer to pay half that tax.

self-liquidating loan A loan that pays for a nontypical high expense—the need for increased inventory during a busy season, for example—and is then paid off as revenues are realized.

selling and administrative expense budget An analysis of those costs that are not directly involved in the production of goods or services (i.e., operating expenses) needed to support the functioning of a business.

selling expense The expenses of marketing and selling goods or services.

selling group/selling syndicate A group of brokers who have come together to sell a new issue of company stocks.

selling short The practice of selling securities that don't actually belong to the seller. The seller has made a "down payment" to a broker on those securities, in this way "owns" them, then sells them hoping that their price will decline by the time the seller must pay the broker in full—in this way realizing a profit on the transaction.

senior accountant An accountant who works for a firm of certified public accountants who is not yet at the manager level but who supervises an audit for a client. The senior accountant's work is subject to the scrutiny of a manager.

senior security A security that in normal practice or in any liquidation or bankruptcy proceedings has precedence over other kinds securities (e.g., preferred stock has seniority (must be paid first) over common stock).

separate return A tax return filed individually by married couples. Generally, there are more tax advantages to be gained by filing a joint return.

service department A department in a factory that performs essential services but is not involved in production (e.g., the cleaning and maintenance department).

service life The estimated time that an asset will be useful to a business.

services The business of a company that does not create or sell a tangible product but instead provides professional advice and skills (e.g., a firm of lawyers).

set of accounts The group of ledger records that a business maintains.

setup costs The expenses a business incurs to prepare to create a particular product or to offer a particular service.

share One unit of ownership in a corporation, limited partnership, or mutual fund.

shareholder See stockholder.

Sherman Antitrust Act of 1890 A law prohibiting monopolies among U.S. corporations.

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short-form report An audit report that generally includes two paragraphs, one describing the scope of the audit, the other setting out the auditor's opinion.

short-term debt A debt that must be paid within one year.

short-term debt ratio The calculation of debt payable within one year as compared to the company's total debt. A high ratio may indicate that the company may have difficulty in meeting its financial obligations.

short-term investment Any investment that an investor expects to hold for less than one year (e.g., stocks than an investor expects to hold for a short term because the price of those stocks is expected to rise, netting the investor a profit as soon as the stocks are sold).

shrinkage The excess of inventory recorded on a company's books over actual inventory. The reasons for the discrepancy usually have to do with damage to inventory that is not recorded until there is a physical count.

simple interest A calculation based only on the original principal, not on principal and accumulated interest.

single-entry bookkeeping A simple system, often maintained by small businesses, in which transactions of a certain kind are recorded in a simple record (e.g., expenditures recorded only on the stubs of a company's checkbook or income recorded only in a bank deposit book). Provided the transactions are fairly limited in number, financial statements can be prepared from such records.

social audit A informal, internal audit having to do with the community efforts of any business.

Social Security tax A federal levy on employers and employees to fund the U.S. Social Security program, which provides retirement benefits to employees and their survivors. Employers and employees pay equal shares.

software Any set of instructions for a computer.

sole proprietor An unincorporated business with just one owner, usually a small business. The disadvantage of such a business entity is that the sole proprietor is directly responsible for all the debts of the business.

solvent A business is considered solvent if it is able to satisfy its financial obligations when they are due.

source document A original record on which entries in a company's financial records are based (e.g., an invoice or a check stub).

special journal A company record of a particular kind of transaction (e.g., a journal that records just the company's sales).

special situation An event, usually nonrecurring, that requires some kind of variant in a company's usual record-keeping.

speculation Making an investment in a high-risk instrument (e.g., the stocks of a company that if it succeeds is likely to do very well but is more likely to fail because of entrenched competition).

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spin-off A kind of reorganization in which a company transfers some of its activity to a new, specialized corporation: the original company owns the new corporation.

spoilage Those products, in any run, that are damaged or not up to usual standard.

spreadsheet Numbers arranged in fixed rows and columns, universally used for financial calculations. Computers now greatly reduce the work of compiling spreadsheets via software packages.

standard A performance objective, usually based on experience (e.g., it generally takes lawyer “A” 15 hours to prepare a residential lease). Standards are used to estimate costs, fees, and prices

standard cost The cost of goods or services that is determined by experience, which ought to be attainable unless there are unforeseen circumstances.

standard deduction Deductions allowed by the Internal Revenue Service to an individual taxpayer who chooses not to itemize deductions. This deduction is automatic: that is, it is incorporated into tax tables that employers use to calculate an employee’s income tax contributions. It is only when allowable itemized deductions are greater than the standard deduction that the taxpayer is allowed an extra deduction.

standard opinion Evaluation given by a certified public accountant that a company’s financial statements are presented in accordance with generally accepted accounting principals (GAAP). The CPA is, in other words, satisfied that the financial statements are accurate.

statement The presentation of the financial condition/performance of an entity. It usually involves three components: income statement, balance sheet, and changes in financial position.

statement of account The rendering of the current state of transactions between a debtor and credit. It may record only the balance due or it may include a financial history (i.e., previous balances or payments received) as well.

statement of cash flows A document that shows a company’s cash disbursements and cash receipts for a particular period of time. Such a document is required in a company’s annual report.

statement of retained earnings A document that accompanies the balance sheet: it shows the opening balance of retained earnings, changes that occurred during the course of the year, and a new, end-of-year balance.

state unemployment compensation A subsidy to individuals unemployed because they have lost their jobs (generally, it is not available to people who have quit their jobs), financed by a state payroll tax on employers. There is some difference in the way it is administered from state to state.

statutory audits Audits formulated to meet the requirements of a particular government agency (i.e., the scope of the audit is set by the agency). Such firms as banks and brokerages are subject to statutory audits.

stock A term with two very different meanings: (1) a company’s inventory;

and (2) partial ownership of a corporation as evidenced by a share document, of which there are two kinds: common stock and preferred stock.

stock bonus plan An incentive plan for employees in which the reward is not cash but shares of the employer's stock.

stock certificate A document that is evidence of an investor's partial ownership of a corporation. The certificate commonly shows the number of shares the investor owns, par value, class of stock, and voting rights. Stock certificates can be traded.

stock compensation See stock bonus plan.

stock dividend Distribution of additional shares of company's stock to its stockholders, on a pro-rata basis, that is reflecting the percentage of stock they already hold.

stock register A record of the details of a company's shares—who owns them, how many, par value, and date they were issued.

stock right The right of existing shareholders to buy shares in a new stock offering before it is offered to the general public—the purpose of which is to allow shareholders to maintain their ownership interest in the company, if they wish to do so. For example, if an investor owns 1 percent of a company, that investor can buy 1 percent of the new offering, thus continuing to keep the same ownership interest.

stock split A corporation's act of issuing a substantial number of new shares, thus reducing the par value of its exiting stock. The usual reason for such an action is that the company wishes to reduce the price of its shares in the marketplace, to make them more attractive to a greater number of buyers.

stock subscription An agreement in which an investor agrees to buy a certain number of shares at a particular price at some time in the future. Usually, a down payment is involved, and the shares are paid for in installments.

stockholder Any individual or entity that owns shares in a corporation. Return on the investment is in the form of dividends or in an increase in the value of the stock—because it is trading at a higher price than that for which it was purchased.

stockholders' equity The ownership interest in a company of its stockholders—the value of their contributions to the company as well as their interest in its earnings.

stockholders of record The investors holding stock on the date of record who are therefore entitled to a declared dividend.

stop-loss order A directive from an investor to that investor's broker to sell a particular stock if it exceeds or falls below a certain price.

stop payment A directive to a bank by someone who has issued a check not to cash that check when it is presented for payment.

stores Retail establishments, but the term is also used to refer to raw materials and supplies.

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straight-line depreciation A method that provides for equal charges for each accounting period; it is the easiest and most common way of calculating depreciation expense. Subtract salvage value from cost of asset, then divide that sum by the life of the asset. Say that you acquire a piece of machinery for $100,000, and imagine that you could sell it at the end of its useful life for $20,000; your balance is $80,000. You imagine that useful life to be 10 years. Annual depreciation expense is therefore $8,000.

strategic alliance Agreement between two or more companies to work together on a project to achieve a common benefit. For example, a designer of women's clothing creates a strategic alliance with a chain of department stores to give that chain exclusive right to sell those clothes, an agreement that both sides believe will lead to greater profits for each.

strategic planning Devising the means to achieve a company's strategic objectives. It usually involves two steps: deciding what products to produce or sell, or what services to offer and determining how best to market these goods/services to potential customers.

subchapter S corporation A corporation in which the income of the corporation is regarded as the income not of the entity itself but, proportionately, of its stockholders.

subordinated debt Securities that have a right to a firm's assets only after the claims of holders of senior securities have been paid.

subscription An agreement to buy a security.

subsequent event Some important financial occurrence that happened after the financial statements were prepared but before the audit report is presented. This event must be disclosed in a footnote.

subsidiary company A company in which controlling interest is held by another company, called the parent company.

substantive auditing test A test that affirms the accuracy of account balances.

sunk costs Those costs that management decides to write off because an investment now seems likely to yield poor results that do not justify further investment in money, materials, and/or labor.

surplus The amount of retained earnings after dividends have been paid.

surviving company In any business combination of two or more companies, the one that acquires the assets of the other and continues the operations of both companies or the merged companies.

system weakness Inadequate controls in a company's accounting methods and practices.

take-home pay See disposable income.

takeover The acquisition of one company by another, which may be forced (the acquiring company acquires a majority of the shares of the acquired company) or friendly (one company, in negotiations, agrees to be sold to the

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other).

tangible asset An asset that has physical substance and a useful life of greater than one year.

target income Income that a business is trying to achieve in any given accounting period.

target price The expected market price of a product, that which a company hopes to get for a product it manufactures or distributes, based on current market conditions.

tariff A tax on imports or exports, usually calculated as a percentage of the price.

tax A charge imposed by the government (federal or state) on personal income and the income of companies, as well as on estates and gifts. The payment of such tax is legally enforceable.

tax avoidance Payment of the least amount of tax consistent with the law by using such means as trusts, buying securities on which interest is exempt (e.g., municipal bonds), or selling at a loss. Tax avoidance is not illegal.

tax court The U.S. court in which the judges handle disputes between taxpayers and the Internal Revenue Service.

tax deed The title that passes to the purchaser of property sold to pay a tax debt.

tax effect Impact on taxes of an individual's or a company's income and expenses.

tax evasion Not paying taxes that are legally due the federal or state government. Tax evasion is different from tax avoidance in that it always involves practices that are illegal (e.g., understating income, claiming deductions that are mythological, or overstating losses). Taxpayers are penalized for tax evasion and may even face criminal prosecution.

tax-exempt bond A security (issued by a state, county, or municipal authority), the interest of which is not subject to either federal or state taxes.

tax haven A foreign country that levies low taxes on individual or company earnings.

tax lien A tax authority's claim on a taxpayer's property for delinquent taxes. When taxes are paid, the lien is removed.

tax planning The analysis of ways to avoid taxation (e.g., figuring out the most advantageous way to withdraw funds from a retirement account).

tax rate The amount of tax in effect for individuals (based on status and amount of income) and for companies, stated as a percentage.

tax return The form used to report taxes due to a federal, state, or local government. The most common tax return is the Form 1040, for federal taxes, filed by individual taxpayers by April 15 following the tax/calendar year.

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tax year That year which a tax return covers—generally the same as the calendar year, though companies (unlike individuals) may elect a different fiscal year, provided their doing so is approved by the tax authority (partnerships are generally required to use the same tax year as their partners).

taxable income For corporations, gross income less bona fide business deductions; for individuals, income less itemized deductions and personal exemptions.

temporary investments Those investments in which a company might place excess cash, to earn interest on that cash before it is needed—investments that the company intends to maintain for less than a year.

10-K The form that publicly traded companies must submit each year to the Securities and Exchange Commission. Financial statements, supporting documents, important disclosures, and general information about the business are included.

tender offer An attempt to buy a large block of shares at a specified price, usually one in excess of the current market price. The objective is to gain a sufficient number of shares to takeover a target company. Usually a tender offer is made directly to the company's stockholders. If the company making the offer accumulates more than 5 percent of the shares, that company must disclose its ownership position to the Securities and Exchange Commission.

term loan A long-term business loan that is paid off in installments (i.e., is amortized).

termination benefits Any benefits that are owed to an employee when he or she leaves a particular employer (e.g., what the employee is owed by the company's pension plan).

throughput The rate of production—how long it takes to make a particular product come into existence; also, the act of that production.

tick mark Symbol that an auditor uses to designate that certain work in the audit has been completed, so that others using the work papers of the audit do not do the same work again.

time and motion study An analysis of the length of time and human activities involved in a particular business process. The purpose of the analysis is to determine whether the process could be performed in a more efficient way.

time deposit An account at a financial institution that earns interest but from which the money may not be withdrawn at will: the depositor can withdraw funds only at the maturity date. If the depositor wishes to withdraw before that date, the depositor must give notice to the institution and must pay a penalty.

time value of money The idea that a dollar held now is more valuable than a dollar earned in the future, not just because inflation may erode value but because a dollar-in-hand can earn interest before the future dollar is earned.

total cost The sum of all costs incurred (not just direct costs) in the creation, administration, sale, and distribution of goods or services.

total fixed costs The sum of all costs that remain constant in any business

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operation.

trace To determine whether an item on a financial statement is valid in the sense that it is the result of an accountant's or bookkeeper's following accepted practice.

trade credit Credit that is extended by one company to another, allowing the second company to buy goods from the other without a requirement to pay for those goods immediately.

trade discount Reduction in price by the seller if the buyer buys a large quantity of goods.

trademark Legal protection—by the U.S. Patent Office—that covers unique names or symbols that designate a particular company. The Patent Office allows the company numerous 20 year renewals once it has granted trademark protection.

trading on equity Operating on borrowed money: the company's assumption is that it will earn more with that money than it will pay in interest for its use.

transactions Financial events in a business that change its financial position (e.g., a sale or collecting a debt).

transcribe Transferring a record from one financial document to another (e.g., posting entries from a journal to a ledger).

transfer agent A corporation's designated agent—often a bank or a trust company—authorized to make transfers of stocks and bonds.

transfer price/pricing Putting a dollar value on the services that one division of a company provides to another division as a way of getting a clearer idea of how well the divisions are performing as income centers.

transfer tax The federal tax on the sale of stocks and bonds, gifts, and estates or the state tax on the transfer/sale of a security.

treasurer That person in a company who deals with its financial problems, different from a controller who supervises all of its accounting functions. In all but large companies, the two jobs are usually combined.

treasury bill A short-term obligation of the federal government, commonly known as "t-bills." They are auctioned weekly by the U.S. Treasury at discount rates; they have maturities of 91 or 182 days. T-bills do not offer great yields, but they are popular because supported by the federal government they are virtually risk-free.

treasury bond Long-term instrument issued by the U.S. Treasury; they are issued in denominations of $1,000, and mature in 10 years or longer.

treasury stock Shares issued by a company that are purchased back by that company.

trial balance The listing, at the end of an accounting period, of the various accounts in a company's general ledger. If it is accurate, total assets will equal total liabilities. The trial balance is not a formal financial statement but

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a worksheet, a first step toward an income statement and balance sheet

trust An agreement in which a trustee is given title to property owned by the person doing the granting, so that the trustee may administer it and hold it for either the grantor or, more usually, the grantor's beneficiary.

turnover The frequency with which any financial item was replaced during an accounting period (e.g., if the constant value of a company's inventory is $100,000, the cost of which is $50,000, and a company spent $150,000 on inventory during the course of a year, then its inventory turnover rate for the year was 3). In Great Britain, the term is a synonym for sales.

UCC See uniform commercial code.

unappropriated retained earnings Those earnings not allocated to a retained earnings account and therefore available to be paid as dividends.

unaudited statement A statement that an auditor may help in accumulating and preparing but does not thoroughly examine according to usual standards. The auditor therefore cannot form an audit opinion.

unavoidable costs Those costs incurred regardless of the products a company decides to produce or sell or the services it provides (e.g., rent expense or utilities costs).

uncollectible account A receivable that almost certainly will not be paid.

underwriting Acceptance of risk as a means of making money if the risk pays off. An underwriter, in this instance an investment banker, buys a new issue of shares at a fixed, discounted price from the company issuing them. The underwriter's goal is to sell them at a higher offering price, thereby making a profit. The company has its money, but the underwriter is taking a risk—the shares may not be popular, may not sell.

unearned revenue In the terminology of taxation, income received from sources other than personal services (e.g., the interest on money loaned).

unfavorable variance Costs that exceed standard costs, those established as the norm for a particular job.

uniform commercial code (UCC) Legal code that came into effect in 1952 and regulates business law in the United States. It is the body of law that is followed by U.S. lawyers when they are dealing with business questions.

unissued stock Shares that have been authorized by a corporation's board of directors but have not yet been offered to the public.

unit cost The cost of producing one unit of product or services. It is usually an average.

unlimited liability The circumstance that a person involved in a sole proprietorship or partners involved in a general partnership are personally responsible for all the debts of their companies.

unqualified opinion The auditor believes in the rightness of a company's financial statements.

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unsecured loan A loan that is not secured by collateral; it is "backed" only by the borrower's credit record and/or by the lender's experience of the borrower. Such loans are usually short-term and carry a higher interest rate than would a secured loan.

unsystematic risk One that is peculiar to a particular security.

utility The characteristic of some product satisfying a perceived want.

validate To make something legal (e.g., the purchaser of property signs the mortgage on that property) or to swear to the correctness of a particular financial item.

value Amounts at which items are recorded in financial statements.

value added The difference, in the various stages of production, between the cost of materials to make the product and all the other components (e.g., design or labor that has been added since the purchase of materials).

value chain The progress of all the activities that go into making a product or creating a service from inception until delivery to the customer.

variable annuity An annuity in which the periodic payments vary because the source of income involves variables (e.g., one that is based on a portfolio of securities that change in value and in the amount of dividends earned).

variable costs Costs other than fixed costs: those that can differ in the production of goods and services.

variance Difference between budgeted forecasts of costs and expenses and actual costs and expenses.

venture capital Funding from wealthy individuals or from investment companies (that have generally pooled funding from numerous such individuals) who money in new businesses or those businesses in an early stage of development. The risk is great, but so is the potential for substantial returns if the companies funded are successful.

verifiable/verification The act of validating or confirming that an item in financial records or statements is correct.

vertical merger A merger that combines a parent company with either a supplier or a purchaser of its products.

vested An employee with full rights to pension benefits regardless of whether that employee stays with the his or her current employer.

voucher A form used in an internal financial control system to explain and control cash outflow in a company—an explanation about each bill paid is included on the voucher; sometimes these comments explain why the bill was necessary.

W-2 form A form sent by an employer to an employee at the end of the calendar year; it shows gross earnings, taxes paid, and FICA deductions. The employer sends copies of the W-2 to the relevant tax authorities; the employee attaches copies to the various income tax returns the employee is obliged to file.

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W-4 form A form filled out by a new employee to show the employer what deductions the employee is claiming against tax and other relevant information.

warrant An option to buy additional shares in a company—codified on a certificate that sets out the number of shares involved, their price, and the period of time during which these shares must be purchased.

WIP See work in process.

withholding tax Deductions from an employee's salary for payment of federal and state income taxes, which is then remitted by the employer to the Internal Revenue Service or to an IRS-designated bank account.

Word Popular word processing software created by the Microsoft Company.

word processing Using a computer to do what a typewriter used to do. The advantage of word processing is that it allows more flexibility than a

typewriter (e.g., it allows the person doing the "input" to rearrange easily the various parts of a business letter).

work in process/work in progress (WIP) That which is started but not completed. Work in process is shown as an asset on a company's balance sheet.

work measurement Determining the length of time that it should take to do a particular job, which is turn is the basis of planning, of employee allocation, and scheduling.

work papers Documents created by auditors (and their staff) in working toward a company's final financial statements. They are, incidentally, an indication of the quality of the auditor's work.

worksheet A schedule on which an accountant/auditor gathers information about a particular account balance and demonstrates the procedures by which the accountant/auditor arrived at certain conclusions. In effect, an auditor bases an audit opinion on accumulated worksheets.

workers' compensation A national program that provides payments to workers if they are involved in job-related injuries. These payments are not taxed.

working capital See net working capital.

World Bank See International Bank for Reconstruction and Development.

write-down The act of decreasing the value of an asset in a company's financial records.

write-off To cancel a customer's account balance because the customer cannot pay it or to cancel any value formerly attributed to a company asset (e.g., an inventory of products that have been superseded by a superior product, rendering the original product unsellable).

year-end adjustment Changing any entry in a financial record to ensure

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that it is properly stated in the end-of-year financial statements. A common example is the book value of inventory after a physical count has taken place—to make the book value conform to the undamaged inventory on hand.

yield The return to an investor from a security.

zero-sum game A kind of competition in which the gains to the winner are exactly the same as the loss to the loser. For example, a limited number of lawnmowers are sold each year in a small town by two different merchants—say 10; each merchant normally sells 5. If in one year one of the merchants sells 6 but the total number sold has not increased, then the second merchant has sold only 4—a zero-sum game.

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