AS Business
Profit and Loss Accounts

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Profit and Loss Accounts

Profit and Loss Account

Definition: An accounting statement showing an organisation's sales revenue over a trading period, and all the relevant costs incurred in earning that revenue (income and expenditure).

	Sales Revenue
(minus)	Cost of Sales
(equals)	Gross Profit
(minus)	Expenses
(equals)	Net Profit

Cost of Sales: All costs of production used when manufacturing guitars and ukuleles. Any direct costs, such as raw materials, wages, used in the production process.

Formula: Opening stock + Purchases - Closing Sales

Gross Profit: The difference between the revenue from selling the product and the direct costs of making it.

Formula: Sales Revenue - Costs of Sales

Net Profit: It is the profit that belongs to the sole trader following the reduction of all expenses from the gross profit. The sole trader has to pay income tax on this profit.

Formula: Gross Profit - Expenses

Example of a P+L Question

Calculate the value of each of the following items for the profit and loss account for 2014:

Miles Guitars' Profit and Loss Accounts for the years ended 31.3.14 and 31,3,201

	2014 (£)	2013 (£)
Sales Turnover	1 106 540	900 500
Opening Stock	44 000	52 800
Purchases	440 500	352 200
Less Closing Stock	35 000	52 000
Cost of Sales	449 500	353 000
	(i)	547 500
Gross Profit		
Less:		
Wages/Bonuses	509 000	475 000
Vehicle expenses	16 000	14 000
Marketing	(ii)	3 000
Telephone	1 010	1 200
Insurance	2 200	2 000
Training	10 000	1 500
Business rates	4 150	4 000
Accountancy fees	1 700	1 500
Depreciation	3 500	3 500
Electricity	2 900	2 750
Total Expenses	(iii)	508 450
Net Profit	(iv)	39 050

Gross Profit = Sales Revenue – Costs of Sales
= £1106540 – £449500
= £657040

Marketing = *increased his marketing expenditure by 75% compared with the previous year*
= £3000 x 1.75
= £5250

Total expenses = *Add up all the expenses!*
= £555710

Net Profit = Gross profit – Expenses
= £101330

Profitability Ratios

Profitability measures a business' total profit against resources used in making that profit. On its own, profit is a relatively meaningless figure – it needs comparing against figures such as turnover.

These profitability ratios are used to asses how well the business is performing. They concentrate on profit, capital employed and turnover.

Gross Profit %

Definition: Measures the proportion of money left over from revenues after accounting for the cost of goods sold.

Calculation: $\frac{\text{Gross Profit}}{\text{Sales Revenue}} \times 100$

If the gross profit margin is 30%, this means that the business' cost of sales are 70% of its turnover (because turnover = cost of sales + gross profit).

Reasons for change:
- increase or decrease in sales turnover
- increase or decrease in cost of goods sold.

Net Profit %

Definition: Measures how much out of every pound of sales a company actually keeps in earnings.

Calculation: $\frac{\text{Net Profit}}{\text{Sales Revenue}} \times 100$

Reasons for change:
- increase or decrease in sales turnover
- increase or decrease in cost of goods sold
- increase ore decrease in expenses.