SML Bookkeeping & Tax

Understanding Profit and Loss Statements

KS-011

How business owners can read income, expenses and profit at a basic level.

TOPIC	PREPARED BY	FORMAT
Small business education	SML Bookkeeping & Tax	Knowledge Sheet

Key message

A Profit and Loss Statement shows income, expenses and profit over a period. It helps business owners understand whether trading activity is profitable, which costs are increasing, and whether pricing or margins need review.

Profit and loss - reading workflow

1 **Check period**
Confirm the report date range and accounting basis.

2 **Review income**
Compare sales, service revenue and other income.

3 **Review costs**
Look at direct costs, overheads and unusual expenses.

4 **Compare**
Compare results with prior periods, budget or expectations.

What a Profit and Loss Statement shows

A Profit and Loss Statement, often called a P&L;, summarises income and expenses for a period. It may show gross profit, operating expenses and net profit depending on the report setup.

Key areas to review

- Income or revenue for the period.
- Cost of goods sold or direct costs where relevant.
- Gross profit and gross profit margin.
- Operating expenses such as rent, wages, software and marketing.
- Net profit before tax or other final adjustments.

Questions business owners should ask

- Did sales increase or decrease compared with last period?
- Are direct costs rising faster than sales?
- Which expenses changed significantly?
- Is the report complete and reconciled?
- Does profit match the cash position, or is cash tied up elsewhere?

Common mistakes to avoid

- Reading profit before bookkeeping is complete.
- Comparing periods with different date ranges.
- Ignoring one-off or unusual expenses.
- Assuming profit equals available cash.

Example

A cafe shows higher sales this quarter but lower profit. The owner should review food costs, wages, discounts, wastage and price changes instead of only focusing on total revenue.

Common Questions

Does the P&L; show cash in the bank?

No. It shows income and expenses for the period. Cash position is affected by payment timing, loans, tax, drawings and other balance sheet items.

Why does profit change when sales increase?

Costs may have increased faster than revenue, or some expenses may have been recorded in the period.

How often should I review the P&L;?

Monthly review is useful for many businesses, especially when bookkeeping is up to date.

Reference Sources

Source	Used for
Xero	Practical profit and loss report context.
MYOB	Small business reporting and bookkeeping guidance.
CPA Australia	Professional context on reading financial reports.

Important note

This Knowledge Sheet provides general information only. It does not take into account the full circumstances of any business. Speak with SML Bookkeeping & Tax before making tax, payroll or compliance decisions.