**Profit and Loss (P&L)**

**Definition - What does *Profit and Loss (P&L)* mean?**

A profit and loss (P&L) statement is an accounting statement prepared at the end of a financial quarter or year which comprises revenue and expense items to indicate an accounting net profit or loss.

A profit and loss statement needs to be studied, along with the balance sheet and statement of cash flows, to get a comprehensive idea of the firm's financial position. Because P&L statements are based on accounting rules which can vary or be subject to estimates, investors need to fully understand how different estimates would affect the company's performance particularly if aggressive estimates have been used to show better profit.

A profit and loss statement is an indicator of the overall financial health of a firm. It summarizes the revenue costs and expenses incurred over a specific, fixed period of time. It discloses gains and losses that arise from commercial transactions. The cost of running the business — that is, the cost of goods sold, operating expenses, interest, tax, etc. — is subtracted from the revenue generated to arrive at profit and loss.

In order to assess the cash flow available, to repay existing debt, to finance additional debt for business expansion, or to reinvest in the company, a careful analysis of the components of a profit and loss statement is necessary. In many merger and acquisition transactions, these statements may be prepared to comply with buyers' requirements. In some cases, firms looking to dispose of only a portion of their operations prepare separate financial statements, called carve-out financial statements, of the section being sold.

In practice when assessing a business for sale, three to five year historical P&L statements are a minimum requirement. Buyers often attempt to estimate recurring EBITDA or EBIT from these statements. However, more important is estimated cash flows from these statements (which necessitates the balance sheets as well) and also figuring out what future performance would look like. In stable industries, the historical P&L may be a good proxy for future performance, but in growing businesses, projected P&L statements are often required.

**Features of Profit and Loss Account:**

1. This account is prepared on the last day of an account year in order to determine the net result of the business.
2. It is second stage of the final accounts.
3. Only indirect expenses and indirect revenues are shown in this account.
4. It starts with the closing balance of the trading account i.e. gross profit or gross loss.
5. All items of revenue concerning current year - whether received in cash or not - and all items of expenses - whether paid in cash or not - are considered in this account. But no item relating to past or next year is included in it.