Is net profit same as profit after tax

Net income is a type of profit. It is typically known as the “bottom line” figure for small businesses on their income statement after all expenses are removed. Net profit, on the other hand, is slightly different because it is the pure profit that a business earns after deducting various classes of expenses. Net profit is used to calculate the firm’s tax liability on its revenue as well as business profitability. The differences between net income and net profit are subtle, but they are important to understand as you develop your knowledge of a business’s financial statements. Net income is calculated on the income statement and shows what a business has earned after subtracting expenses such as operating expenses, cost of goods sold (COGS), depreciation, interest, and taxes along with allowable deductions during a specific accounting period. This period could be a month, a quarter, six months, or one year. Net income is considered the “bottom line” figure on the income statement. Net income is calculated by the equation: Revenue - Expenses = Net Income Net income is the total income from revenue (sales and other income) after all business expenses are deducted. Both the revenue and expense figures can be obtained from the business’s income statement. The first, and arguably the most important business expense is COGS, which can be defined as the firm’s direct production costs like raw materials, labor, and overhead. If a business sells services instead of products, it does not have cost of goods sold. After you report your total revenue from your business and COGS, you can then follow the traditional income statement format to report your business expenses. It is crucial to keep good bookkeeping or accounting records year-round so you will be able to quickly summarize your business expenses. Following the income statement format, here are some examples of business expenses you might incur: Selling and operating expenses: Examples are commissions paid to salespeople, advertising, contract labor, rent, insurance, repairs and maintenance, and travel and meals.General and administrative expenses: Examples are car and truck expenses, depreciation, interest on mortgages, lease expenses, legal and professional expenses, office expenses and supplies, taxes and licenses, and utilities.Other: Examples are any income the business receives that is not counted as a sale. Selling an asset for a profit would be an example.Interest expense: This is the interest the business has to pay if it has any outstanding debt.Income tax expense: This is the business’s tax liability based on profit. The “foreign currency” line item on the income statement is usually not applicable for small businesses. You can look at IRS Form Schedule C to see these and other categories of business expenses. The most obvious difference between net income and net profit is that net income is the “bottom line” of the firm’s income statement from which all expenses have been deducted. Net profit, however, indicates the profitability of the business for a specific time period. Another difference is that net profit can be calculated in stages. For example, if you look at an income statement you will see that profitability, in dollars, is calculated after each section of expenses. The three components of profit on an income statement are gross profit, operating profit, and finally, net profit. The calculations for each are as follows: Gross profit: Revenue - COGSOperating profit: Gross profit - operating expenses - depreciation - amortizationNet profit: Total revenue - total expenses Here is a comparison table outlining the differences between net income and net profit: Comparison Net Income Net Profit Definition Net income is the bottom line number on the income after all expenses are deducted. Net profit indicates the profitability of the firm. Expenses are deducted from revenue to arrive at a net profit for each type of expense. What Does It Show? It shows the total cash inflow of revenue minus expenses during an accounting period. It shows the dollar profitability of the business.. Types Earned and unearned Gross profit or net profit Dependency Dependent on revenue and profit Dependent on revenue only Uses Allows you to calculate total actual earnings and give investors the ability to assess revenue and expenses of your business. Allows you to calculate the profitability and tax liability of the business for a particular time period. Both net profit and net income are important financial metrics and should be calculated each accounting period for the business firm. There is really no magic number. A good net profit depends on the business itself and the industry in which the business operates. You can compare your net profit to the industry average net profit as a benchmark. Economic conditions can also impact net profit. In a general sense, we can say that a good net profit margin exceeds 10%. Gross profit is what you have left on your income statement after you deduct COGS from revenue. Net profit is what you have left after you deduct all your expenses including operating expenses, depreciation, and amortization. FIFO will report higher gross profit and net income when the assumption is made that the products that make up COGS are lesser in value since they were purchased in the past. Reading Time: 4 minutesProfit is the money that a business brings in. Comparing current profits to profits from previous accounting periods helps you understand the growth of the business. To create accurate financial statements and monitor your business’s financial health, you should understand the two types of profits: gross profit and net profit. Gross profit is the profit a business makes after subtracting all the costs that are related to manufacturing and selling its products or services. You can calculate gross profit by deducting the cost of goods sold (COGS) from your total sales. While calculating the total sales, include all goods sold over a financial period, but exclude sales of fixed assets such as buildings or equipment. What does gross profit tell you? Gross profit is a measure of how efficiently an establishment uses labor and supplies for manufacturing goods or offering services to clients. It is an important figure when checking the profitability and financial performance of a business. Gross profit helps you understand the costs needed to generate revenue. When the value of the cost of goods sold (COGS) increases, the gross profit value decreases, so you have less money to deal with your operating expenses. When the COGS value decreases, there will be an increase in profit, meaning you will have more money to spend for your business operations. Net profit is the amount of money your business earns after deducting all operating, interest, and tax expenses over a given period of time. To arrive at this value, you need to know a company’s gross profit. If the value of net profit is negative, then it is called net loss. What does net profit tell you? Net profit is another important parameter that determines the financial health of your business. It shows whether the business can make more than what it spends. You can use your net profit to help you decide when and how to work towards expanding your business and when to reduce your expenses. For a business owner, it is important to know the difference between profit and profitability. Profit is an absolute number which is equal to revenue minus expenses. Profitability, on the other hand, is a relative number (a percentage) which is equal to the ratio between profit and revenue. Profitability is a measure of efficiency and it is useful in determining the success or failure of a business. Net profit tells you about the profitability of your business. Knowing about the same has several advantages beneficial for the business. Most government forms and tax forms require you to declare your net profit. Based on your net profit, the financial institutions, like banks, decide whether to issue a loan or not. This stands true because net profit is a common field found on business tax forms. Furthermore, lenders and investors look at your company’s net profit to check if you own the capability to pay your future debts. Importance of knowing the difference between gross profit and net profit Net profit tells your creditors more about your business health and available cash than gross profit does. When investors want to invest in your company, they will refer to the net profit of your business to check whether it is worth investing their money. Understanding gross profit trends, on the other hand, can help you find ways to minimize the cost of goods sold or raise your product prices. And if your gross profit is less than your net profit, then you know that you need to find a way to cut down your expenses. You need to know the correct values of gross and net profit to generate an income statement: a financial statement that reflects the health of your business. Not knowing the difference between the two may result in inaccurate financial documents that present an unrealistic picture of your business. The three main financial documents aid the management in making important business decisions, so if they show incorrect profit information, it will affect their decision-making. How to calculate gross and net profit? You can calculate both gross and net profit using your income statement. An income statement shows your company’s total revenue and cost of goods sold, followed by the operating expenses, interest and taxes. In the following example, we are looking at an annual income statement for Excel Technologies for the year 2018. The company records a total revenue of $200,000. Gross profit = Total revenue – Cost of goods sold = $200,000 – $50,000 = $150,000 Successful businesses show a positive value for gross profit. The money accounted as gross profit pays for expenses like overhead costs and income tax. To calculate the net profit, you have to add up all the operating expenses first. Then you add the total operating expenses, including interest and taxes, and deduct it from the gross profit. In the above example, the total operating expenses including taxes and interest are $110,000. Net profit = Gross profit – Expenses = $150,000 – $110,000 = $40,000 When the value of net profit is positive, then the business owners can pay themselves and their partners after paying off their expenses. When the value of net profit is negative, then it is called a net loss. This usually occurs in the case of new businesses that do not earn enough to pay off their overhead costs or income taxes. In such cases, keep track of each type of expenses so that you can find areas to cut down without sacrificing the company’s operations and efficiency. To avoid facing a net loss after tax payments, the company should track expenses by developing a budget that includes potential tax payments per year. This will help them develop sales goals that meet their financial needs. Gross profit vs net profit – A comparison chart Here’s a quick review of the differences between gross and net profit : Your takeaway Net profit reflects the amount of money you are left with after having paid all your allowable business expenses, while gross profit is the amount of money you are left with after deducting the cost of goods sold from revenue. You need to calculate gross profit to arrive at net profit. Once you know the correct values of your gross and net profit, you can generate an income statement. Gross profit and net profit are inter-dependent, so calculating the right values is important. This would keep the records maintained and help in determining if your business is performing efficiently. Using Zoho Books, you can easily generate real-time business overview reports like P&L statements to evaluate the values of gross and net profit. Try out our cloud accounting software for free to know how it will help you generate and maintain your records while performing business activities efficiently.

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