

## LESSON-4 ACCOUNTING FOR BUSINESS TRANSACTIONS

### SUMMARY

Activities which are in cash terms are called business transactions.

A business transaction is a transaction, which involves exchange of values between two parties. Every transaction involves Give and Take aspect.

### Source Documents and vouchers

All business transactions are based on documentary evidence. A Cash memo showing cash sale, an invoice showing sale of goods on credit, the receipt made out by the payee against cash payment, are all examples of source documents. A Voucher is documentary evidence in support of a transaction.

### Types of Accounting Vouchers

Accounting vouchers are the written documents, containing the analysis of business transactions for accounting and recording purpose.

#### Transaction Voucher Firm Name

**Voucher No.**

**Date:**

**Debit account:**

**Credit account:**

**Amount (₹):**

**Narration:**

**Authorised By:**

**Prepared By:**

### Accounting Equation

The recording of business transaction in the books of account is based on a fundamental equation called Accounting Equation.

The recording of business transactions in the books of account is based on a fundamental equation called Accounting Equation. Whatever business possesses in the form of assets is financed by proprietor or by outsiders. This equation expresses the equality of assets on the one side and equity on the other side *i.e.*, the claims of outsider [liabilities] and owners or proprietors funds on the other side.

$$\text{Assets} = \text{liabilities} + \text{Capital}$$

### Rules of Accounting Using Debit and Credit

Two Fundamental Rules are followed to record the changes in these accounts:

*For recording changes in Assets/Expenses /Loses*

“Increase in Asset is debited, and decrease in Asset is credited.”

“Increase in Expenses/Loses is debited, and decrease in Expenses/Loses is credited.”

*For recording changes in Liabilities and Capital/Revenue/Gains*

"Increase in Liabilities is credited and decrease in Liabilities is debited."

"Increase in Capital is credited and decrease in Capital is debited."

"Increase in revenue/gains is credited and decrease in revenue/gain is debited".

## BASIS OF ACCOUNTING

As we are aware that one of the most significant functions of accounting is to make us know true and fair amount of profit earned by the business entity in a particular period. This Profit or income figure can be ascertained by following

### There can be three basis of Accounting

#### 1. Cash basis

This is a system in which accounting entries are recorded only when cash is received or paid. Revenue is recognized only on receipt of cash. Similarly, expenses are recorded as incurred when they are paid.

#### 2. Accrual basis

The accrual basis makes a distinction between actual receipts of cash and the right to receive cash for revenues and the actual payment of cash and the legal obligation to pay expenses. It means the income accrued in the current year becomes the income of the current year whether the cash for that item is received in the current year or it was received in the previous year or it will be received in the next year.

#### 3. Hybrid Basis

This is an accounting system which is the combination of both cash as well as on cred

### Double Entry Book Keeping Mechanism

Double Entry Book Keeping Mechanism entails recording of transactions keeping in mind the debit and credit aspect of the transaction.

The Double entry Book-Keeping seeks to record every transaction in money or money's worth in its dual aspect.

### The advantages of double entry mechanism are

- **Systematic Record:** It records, classifies, and synthesizes the business trans-action in a systematic manner. It provides reliable information for sound de-cision making. It meets the needs of users of accounting information.
- **Complete Record:** It maintains complete record of a business transaction. It records both the aspects of the transaction with narration.
- **Accurate records:** By Preparing a Summarised Statement of Account the arithmetical accuracy of the records can be checked.
- **Operational Results:** By preparing Income Statement (Profit and Loss Account) the business can know profit or loss due to its operations during an accounting period.
- **Financial Position**
- **Possibility of Fraud:**