Types of Accounting Transactions based on the Exchange of Cash

Based on the exchange of cash, there are three types of accounting transactions, namely cash transactions, non-cash transactions, and credit transactions.

1. Cash transactions

They are the most common forms of transactions, which refer to those that are dealt with cash. For example, if a company purchases office supplies and pays for them with cash, a debit card, or a check, then that is a cash transaction.

2. Non-cash transactions

They are unrelated to transactions that specify if cash's been paid or if it will be paid in the future. For example, if Company A purchases a machine from Company B and sees that it is defective, returning it will not entail any cash spent, so it falls under non-cash transactions. In other words, transactions that are not cash or credit are non-cash transactions.

3. Credit transactions

They are deferred cash transactions because payment is promised and completed at a future date. Companies often extend credit terms for payment, such as 30 days, 60 days, or 90 days, depending on the product or service being sold or industry norms.

Types of Accounting Transactions based on Objective

There are three types of accounting transactions based on objective, namely business or non-business.

1. Business transactions

These are everyday transactions that keep the business running, such as sales and purchases, rent for office space, advertisements, and other expenses.

2. Non-business transactions

These are transactions that don't involve a sale or purchase but may involve donations and social responsibility.

3. Personal transactions

Personal transactions are those that are performed for personal purposes such as birthday expenditures.

Effect of Business Transactions on Accounting Equations:

Overnight's Accounting Policies McBryan has taken several courses in accounting and maintains Overnight's accounting records himself. He knows that small businesses such as his are not required to prepare formal financial statements, but he prepares them anyway. He believes they will be useful to him in running the business. In addition, if Overnight is successful, McBryan plans to open more locations. He anticipates needing to raise substantial amounts of capital from investors and creditors. He believes that the financial history provided by a series of monthly financial statements will be very helpful in attracting investment capital.

The Company's First Transaction McBryan officially started Overnight on November 1, 2001. On that date, he opened a bank account in the name of the business, into which he deposited *$80,000* of his personal savings.

This transaction provided Overnight with its first asset—Cash—and also created the initial owner's equity in the business entity. A balance sheet showing the company's financial position after this initial transaction follows:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 1, 2001

Assets		Owner's Equity	
Cash	$80,000	Michael McBryan, Capital	$80,000

Overnight's next two transactions involved the acquisition of a suitable site for its business operations.

Overnight's next two transactions involved the acquisition of a suitable site for its business operations.

Purchase of an Asset for Cash Representing the business, McBryan negotiated with both the City of Santa Teresa and the Metropolitan Transit Authority (MTA) to purchase an abandoned bus garage. (The MTA owned the garage, but the city owned the land.)

On November 3, Overnight purchased the land from the city for *$52,000 cash.* This transaction had two immediate effects on the company's financial position: first, Overnight's cash was reduced by $52,000; and second, the company acquired a new asset—Land. The company's financial position after this transaction was as follows:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 3, 2001

Assets		Owner's Equity	
Cash	$28,000	Michael McBryan, Capital	$80,000
Land	52,000		
Total	$80,000	Total	$80,000

Purchase of an Asset and Financing Part of the Cost On November 5, Overnight purchased the old garage building from Metropolitan Transit Authority for *$36,000.* Overnight made a cash down payment of *$6,000* and issued a 90-day non-interest-bearing note payable for the *$30,000* balance owed.

As a result of this transaction, Overnight had (1) $6,000 less cash; (2) a new asset, Building, which cost $36,000; and (3) a new liability, Notes Payable, in the amount of $30,000. This transaction is reflected in the following balance sheet:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 5, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 22,000	Liabilities:	
Land	52,000	Notes Payable	$ 30,000
Building	36,000	Owner's equity:	
		Michael McBryan, Capital	80,000
Total	$110,000	Total	$110,000

Purchase of an Asset "On Account" On November 17, Overnight purchased tools and automotive repair equipment from Snap-On Tools Corp. The purchase price was *$13,800*, due within 60 days. After this purchase, Overnight's financial position was as follows:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 17, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 22,000	Liabilities:	
Land	52,000	Notes Payable	$ 30,000
Building	36,000	Accounts Payable	13,800
Tools and Equipment	13,800	Total liabilities	$ 43,800
		Owner's equity:	
		Michael McBryan, Capital	80,000
Total	$123,800	Total	$123,800

Sale of an Asset After taking delivery of the new tools and equipment, Overnight found that it had purchased more than it needed. Ace Towing, a neighboring business, offered to buy the excess items. On November 20, Overnight sold some of its new tools to Ace for *$1,800*, a price equal to Overnight's cost.[2] Ace made no down payment but agreed to pay the amount due within 45 days. A balance sheet as of November 20 appears below.

OVERNIGHT AUTO SERVICE
Balance Sheet
November 20, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 22,000	Liabilities:	
Accounts Receivable	1,800	Notes Payable	$ 30,000
Land	52,000	Accounts Payable	13,800
Building	36,000	Total liabilities	$ 43,800
Tools and Equipment	12,000	Owner's equity:	
		Michcel McBryan, Capital	80,000
Total	$123,800	Total	$123,800

Collection of an Account Receivable On November 25, Overnight received $600 from Ace Towing as partial settlement of its account receivable from Ace. This transaction caused an increase in Overnight's cash but a decrease of the same amount in accounts receivable. This transaction converts one asset into another of equal value: there is no change in the amount of total assets. After this transaction, Overnight's financial position may be summarized as follows:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 25, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 22,600	Liabilities:	
Accounts Receivable	1,200	Notes Payable	$ 30,000
Land	52,000	Accounts Payable	13,800
Building	36,000	Total liabilities	$ 43,800
Tools and Equipment	12,000	Owner's equity:	
		Michael McBryan, Capital	80,000
Total	$123,800	Total	$123,800

Payment of a Liability On November 26, Overnight made a partial payment of $6,800 on its account payable to Snap-On Tools. This transaction reduced Overnight's cash and accounts payable by the same amount, leaving total assets and the total of liabilities plus owner's equity in balance. Overnight's balance sheet at November 26 appears below:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 26, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 15,800	Liabilities:	
Accounts Receivable	1,200	Notes Payable	$ 30,000
Land	52,000	Accounts Payable	7,000
Building	36,000	Total liabilities	$ 37,000
Tools and Equipment	12,000	Owner's equity:	
		Michael McBryan, Capital	80,000
Total	$117,000	Total	$117,000

Earning of Revenue By the middle of the month, McBryan had acquired the assets Overnight needed to start operating, and he began to provide repair services for customers. Rather than recording each individual sale of repair services, he decided to accumulate them and record them twice a month—the 15th and the last day of each month. Sales of repair services for the last half of November were $2,200, all of which was received in cash.

Earning of revenue represents the creation of value for Overnight and an increase in McBryan's ownership interest in the company. As a result, cash is increased by $2,200 and McBryan's capital is increased by the same amount, resulting in the following balance sheet at November 30 (before the payment of expenses, which follows):

OVERNIGHT AUTO SERVICE
Balance Sheet
November 30, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 18,000	Liabilities:	
Accounts Receivable	1,200	Notes Payable	$ 30,000
Land	52,000	Accounts Payable	7,000
Building	36,000	Total liabilities	$ 37,000
Tools and Equipment	12,000	Owner's equity:	
		Michael McBryan, Capital	82,200
Total	$119,200	Total	$119,200

Payment of Expenses In order to earn the $2,200 of revenue that we have just recorded, McBryan had to pay some operating expenses, namely utilities and wages. He decided to pay operating expenses twice a month—the 15th and the last day of the month. For November, he owed $200 for utilities and $1,200 for wages to his employees, which he paid on November 30. Paying expenses has an opposite effect from revenues on McBryan's value in the company—his investment is reduced. Of course, paying expenses also results in a decrease of cash. The November 30 balance sheet, after the payment of utilities and wages, is as follows:

OVERNIGHT AUTO SERVICE
Balance Sheet
November 30, 2001

Assets		Liabilities & Owner's Equity	
Cash	$ 16,600	Liabilities:	
Accounts Receivable	1,200	Notes Payable	$ 30,000
Land	52,000	Accounts Payable	7,000
Building	36,000	Total liabilities	$ 37,000
Tools and Equipment	12,000	Owner's equity	
		Michael McBryan, Capital	80,800
Total	$117,800	Total	$117,800

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Effects of These Business Transactions on the Accounting Equation

As we learned earlier, the statement of financial position, or balance sheet, is a detailed expression of the accounting equation:

Assets = Liabilities + Owner's Equity

As we have progressed through a series of business transactions, we have illustrated the effects of Overnight's November transactions on the balance sheet.

To review, Overnight's transactions during November were as follows:

Nov. 1	Michael McBryan started the business by depositing $80,000 in a company bank account.
Nov. 3	Purchased land for $52,000, paying cash.
Nov. 5	Purchased a building for $36,000, paying $6,000 in cash and issuing a note payable for the remaining $30,000.
Nov. 17	Purchased tools and equipment on account, $13,800.
Nov. 20	Sold some of the tools at a price equal to their cost, $1,800, collectible within 45 days.
Nov. 25	Received $600 in partial collection of the account receivable from the sale of tools.
Nov. 26	Paid $6,800 in partial payment of an account payable.
Nov. 30	Recorded $2,200 of sales revenue received in cash.

Nov. 30 Paid $1,400 of operating expenses in cash—$200 for utilities and $1,200 for wages.

The table below shows the effects of these transactions on the accounting equation. The effect of each transaction is shown in red. Notice that the "balances," shown in black, are the amounts appearing in Overnight's balance sheets on pages 48–52. Notice also that the accounting equation *always* remains in balance.

	Assets					=	Liabilities		+ Owner's Equity
	Cash	+ Accounts Receivable	+ Land	+ Building	+ Tools and Equipment		Notes Payable	+ Accounts Payable	+ Michael McBryan, Capital
Nov. 1	$80,000					=			$80,000
Balances	$80,000					=			$80,000
Nov. 3	-52,000		$52,000			=			
Balances	$28,000		$52,000			=			$80,000
Nov. 6	-6,000			-$36,000		=	-$30,000		
Balances	$22,000		$52,000	$36,000		=	$30,000		$80,000
Nov. 17					-$13,800	=		-$13,800	
Balances	$22,000		$52,000	$36,000	$13,800	=	$30,000	$13,800	$80,000
Nov. 20		-$1,800			-1,800	=			
Balances	$22,000	$1,800	$52,000	$36,000	$12,000	=	$30,000	$13,800	$80,000
Nov. 25	-600	-600				=			
Balances	$22,600	$1,200	$52,000	$36,000	$12,000	=	$30,000	$13,800	$80,000
Nov. 30	6,800					=		6,800	
Balances	$15,800	$1,200	$52,000	$36,000	$12,000	=	$30,000	$7,000	$80,000
Nov. 30	2,200					=			2,200
Nov. 30	1,400					=			1,400
Balances	$16,600	$1,200	$52,000	$36,000	$12,000	=	$30,000	$7,000	$80,800

Income Statement

Statement of Cash Flows

INCOME STATEMENT

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The income statement is a separate representation of the company's revenue and expense transactions for the year. It is particularly important for the company's owners, creditors, and other interested parties to understand the income statement. Ultimately the company will succeed or fail based on its ability to earn revenue in excess of its expenses. Once the company's assets are acquired and business commences, revenues and expenses are important sources of cash flows for the enterprise. **Revenues** are increases in the company's assets from its profit-directed activities, and they result in positive cash flows. Similarly, **expenses** are decreases in the company's assets from its profit-directed activities, and they result in negative cash flows. *Net income* is the difference between the two. Should a company find itself in the undesirable situation of having expenses greater than revenues, we call the difference a *net loss.*

Overnight's income statement for the month of November is relatively simple because the company did not have a large number of complex revenue and expense transactions.[3] Taking information directly from the Owner's Equity column of the previous table, we can prepare the company's income statement as follows:

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ime*

OVERNIGHT AUTO SERVICE
Income Statement
For the Month Ended November 30, 2001

Sales Revenue		$2,200
Operating expenses:		
Wages	$1,200	
Utilities	200	1,400
Net Income		$ 800

Accounting Equation Problems and Solutions:

Problem 2.1

Listed below in random order are the items to be included in the balance sheet of Mystery Mountain Lodge at December 31, 2001:

Equipment	$ 29,200	Buildings	$450,000
Land	425,000	Stanley Gardner, Capital	-?-
Accounts Payable	54,800	Cash	21,400
Accounts Receivable	10,600	Furnishings	58,700
Salaries Payable	33,500	Snowmobiles	15,400
Interest Payable	12,000	Notes Payable	620,000

Instructions

a. Prepare a balance sheet at December 31, 2001. Include a proper heading and organize your balance sheet similar to the illustration on page 42. (After "Buildings," you may list the remaining assets in any order.) You will need to compute the amount to be shown for owner's equity.

b. Assume that no payment is due on the notes payable until 2003. Does this balance sheet indicate that the company is in a strong financial position as of December 31, 2001? Explain briefly.

Solution (part A)

Mystery Mountain Lodge			
Balance Sheet			
December 31, 2001			
Assets		**Liabilities and Owner's Equity**	
Cash	$21,400	Notes Payables	$620,000
Account Receivables	$10,600	Accounts Payables	$54,800
Land	$425,000	Salaries Payables	$33,500
Buildings	$450,000	Interest Payables	$12,000
Equipment	$29,200	Total Liability	$720,300
Furnishings	$58,700	Owner's Equity	
Snowmobile	$15,400	Stanley Gardner's Capital	$290,000
Total Assets	**$1,010,300**	Total Liability & Owner's Equity	**$1,010,300**

	Stanley Gardner's Capital = Total Assets - Total Liabilities		
		= $ 1,010,300.00 - $ 720,300.00	
	Stanley Gardner's Capital	$	290,000.00

(Part B)

No, the financial position of Mystery Mountain lodge is not good as the owner's equity is lesser as compared to total liability. The financial risk is very high and the company can go into bankruptcy due to the fact that it is highly indebted.

Problem 2.3….

ROBLEM 2.3
ecording the Effects of
ransactions

Nova Communications was organized on December 1 of the current year and had the following account balances at December 31, listed in tabular form:

	Assets				= Liabilities		+ Owner's Equity
	Cash +	Land +	Building +	Office Equipment =	Notes Payable +	Accounts Payable +	C. Sagan, Capital
Balances	$37,000	$95,000	$125,000	$51,250	$80,000	$28,250	$200,000

Early in January, the following transactions were carried out by Nova Communications:

1. C. Sagan, the owner, deposited $25,000 of personal funds into the business's bank account.
2. Purchased land and a small office building for a total price of $90,000, of which $35,000 was the value of the land and $55,000 was the value of the building. Paid $22,500 in cash and signed a note payable for the remaining $67,500.
3. Bought several computer systems on credit for $8,500 (30-day open account).
4. Obtained a loan from Capital Bank in the amount of $10,000. Signed a note payable.
5. Paid the $28,250 account payable owed as of December 31.

Instructions

a. List the December 31 balances of assets, liabilities, and owner's equity in tabular form shown.
b. Record the effects of each of the five transactions in the format illustrated on page 53. Show the totals for all columns after each transaction.

Problem 2.3 Solution (Part A & B)

Tabular Form of Balance sheet of Nova Communication

Tabular Form of Balance Sheet							
	Assets				Liabilities		Owner's Equity
	Cash	Land	Building	Office Equipment	Notes Payables	Accounts Payables	C. Sagan Capital
Bal. Dec 31	$37,000	$95,000	$125,000	$51,250	$80,000	$28,250	$200,000
1	$25,000						$25,000
Balances	$62,000	$95,000	$125,000	$51,250	$80,000	$28,250	$225,000
2	-$22,500	$35,000	$55,000		$67,500		
Balances	$39,500	$130,000	$180,000	$51,250	$147,500	$28,250	$225,000
3				$8,500		$8,500	
Balances	$39,500	$130,000	$180,000	$59,750	$147,500	$36,750	$225,000
4	$10,000				$10,000		
Balances	$49,500	$130,000	$180,000	$59,750	$157,500	$36,750	$225,000
5	-$28,250					-$28,250	
Balances	$21,250	$130,000	$180,000	$59,750	$157,500	$8,500	$225,000

Problem 2.4 (Homework)

The items making up the balance sheet of Triad Truck Rental at December 31 are listed below in tabular form similar to the illustration of the accounting equation on page 53.

PROBLEM 2.4
An Alternate Problem on Re ing the Effects of Transactio
LO 3

	Assets				= Liabilities		+ Owner's Equity
	Cash +	Accounts Receivable +	Trucks +	Office Equipment =	Notes Payable +	Accounts Payable +	Bill Foreman, Capital
Balances	$9,500	$8,900	$58,000	$3,800	$20,000	$5,200	$55,000

During a short period after December 31, Triad Truck Rental had the following transactions:

1. Bought office equipment at a cost of $2,700. Paid cash.
2. Collected $4,000 of accounts receivable.
3. Paid $3,200 of accounts payable.
4. Borrowed $10,000 from a bank. Signed a note payable for that amount.
5. Purchased two trucks for $30,500. Paid $15,000 cash and signed a note payable for the balance.
6. Bill Foreman, the owner, invested $20,000 cash in the business.

Instructions

a. List the December 31 balances of assets, liabilities, and owner's equity in tabular form as shown above.

b. Record the effects of each of the six transactions in the tabular arrangement illustrated above. Show the totals for all columns after each transaction.

Problem 2.5 HERE COME THE CLOWNS; is the name of a traveling circus owned by Red Costello. The ledger accounts of the business at june 30, 2001 are listed below in alphabetical order: **(Homework)**

Accounts Payable	$ 26,100	Notes Payable	$180,000
Accounts Receivable	7,450	Notes Receivable	9,500
Animals	189,060	Props and Equipment	89,580
Cages	24,630	Red Costello, Capital	337,230
Cash	?	Salaries Payable	9,750
Costumes	31,500	Tents	63,000
		Trucks & Wagons	105,840

Instructions

a. Prepare a balance sheet by using these items and computing the amount of Cash at June 30, 2001. Organize your balance sheet similar to the one illustrated on page 42. (After "Accounts Receivable," you may list the remaining assets in any order.) Include a proper balance sheet heading.

b. Assume that late in the evening of June 30, after your balance sheet had been prepared, a fire destroyed one of the tents, which had cost $14,300. The tent was not insured. Explain what changes would be required in your June 30 balance sheet to reflect the loss of this asset.