**Double entry bookkeeping**

There are three skills to be mastered when learning double entry bookkeeping.

**Skill 1**

**The ability to recognise the accounts involved in a transaction**

An account is a place where financial (money) information is recorded.

A transaction is an action taken by a business and the effect of this action can be measured in money.

Every transaction has an effect on at least two accounts in a business. In the table below transactions for Ryan Ltd (a seller of computer games) are listed.

|  |  |
| --- | --- |
| **The transactions of Ryan Ltd** | **The Accounts affected** |
|  |  |
| **Issued** €200,000 **ordinary shares**. The money was **lodged.** | Ordinary share capital account  Bank account |
|  |  |
| Purchased **premises** for €70,000. Paid **by cheque.** | Premises account  Bank account |
|  |  |
| **Purchased goods** (games) for €5,000. Paid for **by cheque**. | Purchases account  Bank account |
|  |  |
| **Sold goods** (games) for **cash** €6,000 | Sales account  Cash account |
|  |  |
| Paid **wages** by **cheque** €3,000 | Wages account  Bank account |
|  |  |
| **Sold goods** (games) **on credit to** M Tector €600 | Sales account  Debtor (M Tector) account |
|  |  |
| **Purchased goods (**games**)** from Scanlon Ltd **on credit** for €500 | Purchases account  Creditor (Scanlon Ltd) account |
|  |  |
| M. Tector (**Debtor**) **returned faulty goods** worth €100 | Sales returns account  Debtor (M Tector) account |
|  |  |
| Paid **by cheque** €500 to **Scanlon Ltd** (Creditor) | Creditor (Scanlon Ltd) account  Bank account |
|  |  |
| **M Tector** paid the money owed. The money was **lodged**. | Debtor (M Tector) account  Bank account |
|  |  |
| The manager praised a worker | Why are there no accounts |

Note that there are two sets of key words highlighted in each transaction. You must learn how to recognise accounts from these clues. The following table will help you interpret these key words.

|  |  |
| --- | --- |
| Key words | Name of account |
|  |  |
| Lodged | **Bank account.** Lodged means putting money into the bank account. |
|  |  |
| Issued Ordinary Shares | **Ordinary Share Capital Account** |
|  |  |
| Paid by cheque | **Bank account** |
|  |  |
| Purchased Premises | **Premises account**. When any fixed asset is bought this is recorded in an account named after the asset. e.g. Vehicles |
|  |  |
| Purchased goods (for resale) | **Purchases account**. Goods are those items bought for sale in the companies shop. They must not be confused with the purchase of an asset. |
|  |  |
| Sold goods | **Sales account** |
|  |  |
| For cash | **Cash account** |
|  |  |
| Paid wages | **Wages account**. When any expense is paid this is recorded in an account named after the expense. E.g. rent, insurance. |

**There are a special group of transactions, which take place on credit**. These are transactions where no payment takes place, the buyer promise to pay at a later date. It is important that the business keeps a record of the money owed as a result of these transactions.

|  |  |
| --- | --- |
| Key words | Name of accounts |
|  |  |
| Sold goods on credit | Sales account |
|  | Debtors account |
|  |  |
| Purchased goods on credit | Purchases account |
|  | Creditor account |
|  |  |
| Returned goods to a creditor | Purchase Returns account |
|  | Creditors account |
|  |  |
| A debtor returned goods | Debtors account  Sales Returns account |
|  |  |
| Lodged money from a Debtor | Bank account / Debtor account |
| Paid a Creditor by cheque | Bank account / Creditor account |

In the case of each of the transactions below indicate the accounts affected in the space provided.

Griffin Ltd (Sports Shop)

|  |  |  |
| --- | --- | --- |
| Transactions of Griffin Ltd | First account | Second account |
|  |  |  |
| Issued €440,000 ordinary shares. This money was lodged. |  |  |
|  |  |  |
| Purchased a van €50,000 paid by cheque. |  |  |
|  |  |  |
| Purchased goods €70,000 paid by cheque |  |  |
|  |  |  |
| Sold goods €55,000. This money was lodged. |  |  |
|  |  |  |
| Cash sales €6,000 |  |  |
|  |  |  |
| Bought goods €20,000 on credit from Gordon Ltd |  |  |
|  |  |  |
| Paid rent €500 in cash |  |  |
|  |  |  |
| Returned goods to Gordon Ltd €1,000 |  |  |
|  |  |  |
| Paid insurance €3,000 by cheque |  |  |
|  |  |  |
| Paid Gordon Ltd €19,000 by cheque |  |  |

In the case of each of the transactions below indicate the accounts affected in the space provided.

Pleass Ltd (Clothes Shop)

|  |  |  |
| --- | --- | --- |
| Transactions of Pleass Ltd | First account | Second account |
| Issued €530,000 ordinary shares. This money was lodged. |  |  |
| Purchased Premises €250,000 paid by cheque. |  |  |
| Purchased goods €40,000 paid by cheque |  |  |
| Cash sales €4,500 |  |  |
| Sold goods on credit €5,000 to McDonald Ltd |  |  |
| Paid wages €3,000 by cash |  |  |
| McDonald Ltd returned goods €500 |  |  |
| McDonald Ltd paid the money owed. The money was lodged |  |  |

In the case of each of the transactions below indicate the accounts affected in the space provided.

McMurray Ltd (Grocery Shop)

|  |  |  |
| --- | --- | --- |
| Transactions of McMurray Ltd | First account | Second account |
| Issued €40,000 ordinary shares. This money was lodged. |  |  |
| Purchased Equipment €10,000 paid by cheque. |  |  |
| Purchased goods €20,000 on credit from Rigney Ltd |  |  |
| Sold goods €8,000. This money was lodged. |  |  |
| Sold goods on credit €5,000 to Huston Ltd. |  |  |
| Bought Stationary €20. Paid in cash. |  |  |
| Borrowed €15,000. The money was lodged. |  |  |
| Returned goods to Gordon Ltd €1,000 |  |  |

**The second skill of double entry bookkeeping.**

The ability to recognise if the monetary value recorded in an account has increased or decreased.

Monetary Value: Monetary value simply means the ability to measure something in terms of money. In Ireland the EURO is used to indicate monetary value. It is important to realise that because something is measured in money terms it does not represent cash or money in the bank unless the account concerned is the CASH account or the BANK account.

A premises account with €500,000 recorded in it means the value of the premises is €500,000. A wages account with €6,000 recorded in it means that the expense of wages amounts to €6,000 if a further €2,000 is spent on wages the expense increases to €8,000.

An increase in monetary value: an account will have its monetary value increased if there is MORE in the account as a result of the transaction. In the following exercises a + is used to represent an increase in monetary value.

A decrease in monetary value: an account will have its monetary value decreased if there is LESS in the account as a result of the transaction. In the following exercises a - is used to represent a decrease in monetary value.

The table below interprets what a + or a - means in different accounts.

|  |  |
| --- | --- |
| Sales + | The business has sold MORE goods |
|  |  |
| Purchases + | The business has purchased MORE goods |
|  |  |
| Bank + | The business lodged MORE money in the Bank |
|  |  |
| Bank - | The business has LESS money in the Bank |
|  |  |
| Rent + | The business has paid MORE rent |
|  |  |
| Debtor + | The business is owed MORE money by a customer |
|  |  |
| Debtor - | The business is owed LESS by a customer |
|  |  |
| Creditor + | The business owes MORE money to a supplier |
|  |  |
| Creditor - | The business owes LESS money to a supplier |
|  |  |
| Vehicles + | The business owns MORE vehicles |
|  |  |
| Vehicles - | The business owns LESS vehicles |
|  |  |
|  |  |

In the exercises you have already completed enter if the monetary value in each of the accounts has increased (+) or decreased (-).

To summarise, we know that every transaction a business enters affects at least two accounts whose monetary value may increase or decrease.

It is now necessary to examine what an account looks like.

# DEBIT SIDE An Account CREDIT SIDE

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| Date | Details | Folio | € | Date | Details | Folio | € |
|  |  |  |  |  |  |  |  |
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## Debit side: The left-hand side of an account

Date: Records the date of the transaction

Details: Records the other account involved in the transaction

Folio: States where to find the other account involved in the transaction

€: Records the amount of money involved in the transaction

## Credit side: The right-hand side of an account

Date: Records the date of the transaction

Details: Records the other account involved in the transaction

Folio: States where to find the other account involved in the transaction

€: Records the amount of money involved in the transaction

**The third skill of double entry bookkeeping:**

**Recording information correctly on the debit or credit side of an account.**

Every transaction that affects a business can be recorded in just four different types of account:

**ASSETS**: the resources **owned** by a business

**EXPENSES**: the **cost** of items that have been **used up** **completely** in the process of earning revenue

**REVENUES**: how a firm **earns** money through normal business activity

**LIABILITIES**: money **owed** by the business

There are therefore only four rules in double entry bookkeeping:

Debit **ASSET**  Credit

|  |  |
| --- | --- |
| INCREASE IN VALUE **+** | DECREASE IN VALUE **-** |

Debit **EXPENSE** Credit

|  |  |
| --- | --- |
| INCREASE IN VALUE **+** | DECREASE IN VALUE **-** |

Debit **REVENUE**  Credit

|  |  |
| --- | --- |
| DECREASE IN VALUE **-** | INCREASE IN VALUE **+** |

Debit **LIABILITY** Credit

|  |  |
| --- | --- |
| DECREASE IN VALUE **-** | INCREASE IN VALUE **+** |

These rules can also be expressed as:

|  |  |
| --- | --- |
| DEBIT | CREDIT |
| E+ | E- |
| A+ | A- |
| R- | R+ |
| L- | L+ |

It is now possible to look at the transactions of Ryan Ltd introduced earlier and indicate which accounts need to be debited and credited.

The first transaction of Ryan ltd is examined in detail below.

Issued €200,000 ordinary Shares. The money was lodged.

Skill 1 Identify the accounts involved in the transaction

|  |  |  |
| --- | --- | --- |
|  | First Account | Second account |
| Issued €200,000 ordinary Shares. The money was lodged. | Bank Account | Ordinary Share Capital account |

Skill 2 Identify whether the monetary value recorded in the account has increased (+) or decreased (-)

|  |  |  |
| --- | --- | --- |
|  | First Account | Second account |
| Issued €200,000 ordinary Shares. The money was lodged. | Bank Account (+) | Ordinary Share (+) Capital account |

|  |  |
| --- | --- |
| DR | CR |
| E+ | E- |
| A+ | A- |
| R- | R+ |
| L- | L+ |

Skill 3 Apply the rules

|  |  |  |
| --- | --- | --- |
|  | Account to be debited | Account to be credited |
| Issued €200,000 ordinary Shares. The money was lodged. | Bank Account (A+) | Ordinary Share (L+) Capital account |

The Bank account has been debited because it is an asset and there is MORE money in the account.

The Ordinary Share account has been credited because it is a liability and MORE money is owed to the shareholders.

All the transactions for Ryan Ltd have been entered in the correct Debit and Credit account in the table below. The rule used to decide if it is a debit or credit entry is in brackets after the account name.

|  |  |  |
| --- | --- | --- |
| **The transactions of Ryan Ltd** | Account to be debited | Account to be credited |
|  |  |  |
| **Issued** €200,000 **ordinary shares**. The money was **lodged.** | BANK A/C (A+) | ORDINARY SHARE  CAPITAL A/C (L+) |
|  |  |  |
| Purchased **premises** for €70,000. Paid **by cheque.** | PREMISES A/C (A+) | BANK A/C (A-) |
|  |  |  |
| **Purchased goods** (games) for €5,000. Paid for **by cheque**. | PURCHASES A/C  (E+) | BANK A/C (A-) |
|  |  |  |
| **Sold goods** (games) for **cash** €6,000 | CASH A/C (A+) | SALES A/C (R+) |
|  |  |  |
| Paid **wages** by **cheque** €3,000 | WAGES A/C (E+) | BANK A/C (A-) |
|  |  |  |
| **Sold goods** (games) **on credit to** M Tector €600 | DEBTOR A/C (A+)  (M Tector) | SALES A/C (R+) |
|  |  |  |
| **Purchased goods** from Scanlon Ltd **on credit** for €500 | PURCHASES A/C  (E+) | CREDITOR A/C (L+)  (Scanlon Ltd) |
|  |  |  |
| M. Tector (**Debtor**) **returned faulty goods** worth €100 | SALES RET A/C  (E+) | DEBTOR A/C (A-)  (M Tector) |
|  |  |  |
| Paid **by cheque** €500 to **Scanlon Ltd** (Creditor) | CREDITOR A/C (L-)  Scanlon Ltd | BANK A/C (A-) |
|  |  |  |
| **M Tector** paid the money owed. The money was **lodged**. | BANK A/C (A+) | DEBTOR A/C (A-)  (M Tector) |
|  |  |  |
| The manager praised a worker |  |  |

You will have noticed for each transaction above there is always a debit and a credit entry. This is sometimes stated as

"For every debit there must be a credit." This means if you think a transaction is recorded on the debit side of two accounts you must think again.

Skill 3 can only be mastered if you can recognise if an account is an Expense, an Asset, a Revenue or a Liability.

Here is list of the most common accounts used in the Junior Certificate. Enter them in the correct column in the table below.

Premises, Creditors, Ordinary Share Capital, Rent, Interest, Purchases, Vehicles, Debtors, Light & Heat, Bank overdraft, Wages, Sales Equipment, Rent Received, Advertising, Bank, Sales Returns, Machinery, Term Loan, Insurance, , Commission Received, General Expenses, , Cash, Stationary.

|  |  |  |  |
| --- | --- | --- | --- |
| + Expenses - | + Assets - | - Revenues + | - Liabilities + |
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|  |  |  |  |

Complete the following exercises using the 3 skills of double entry bookkeeping.

Skill 1 Identify the accounts involved in the transaction

Skill 2 Identify whether the monetary value recorded in the account has increased (+) or decreased (-)

|  |  |
| --- | --- |
| DR | CR |
| E+ | E- |
| A+ | A- |
| R- | R+ |
| L- | L+ |

Skill 3 Apply the rules

In the case of the transactions indicated below decide on which account is to be debited and which is to be credited.

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| --- | --- | --- |
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| Paid insurance €3,000 by cheque |  |  |
| Paid Gordon Ltd €19,000 by cheque |  |  |