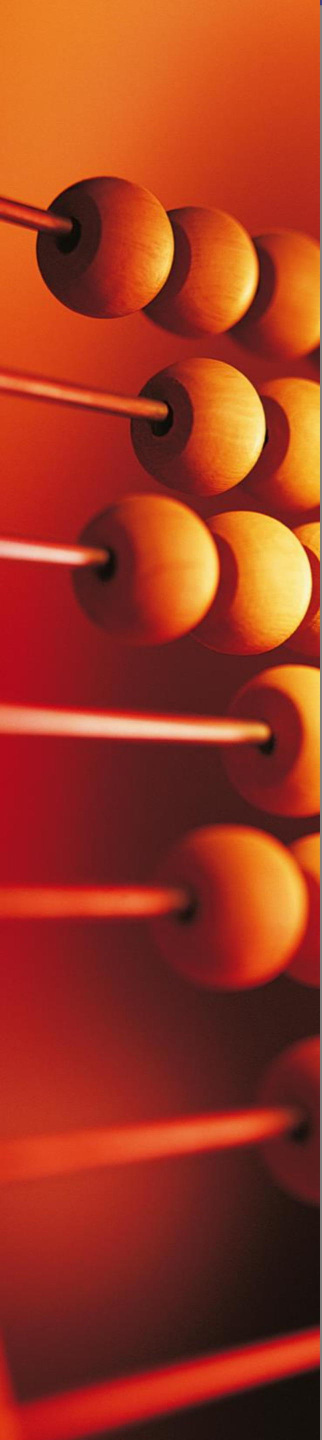

Double-entry accounting

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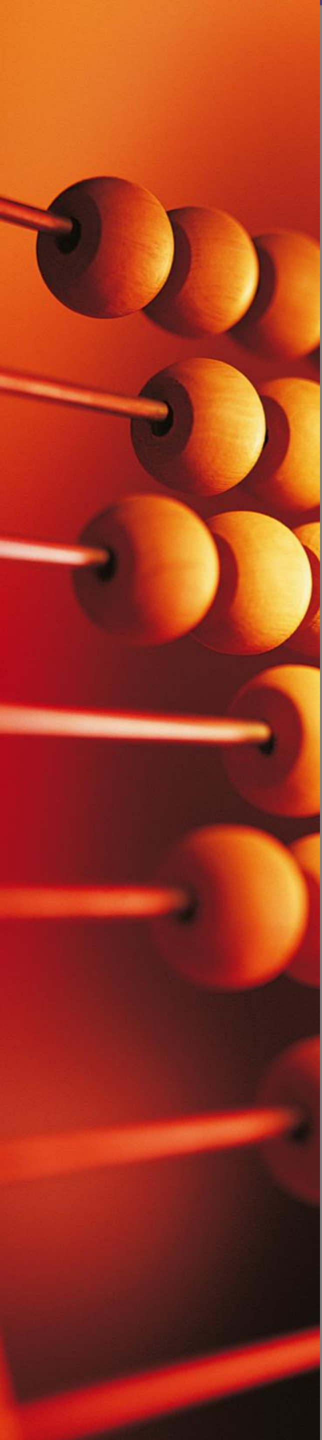


Introduction

Every financial accounting transaction must be recorded **twice** in the accounts of a business: it must have one **debit** entry and one **credit** entry.

Double-entry recording is entered in a book called a **ledger**. The ledger can be a manual or computerised system of recording.

At AS level, you need to know how to record accounting transactions using the double-entry system.

When the double-entry system of accounting is used, the accounting equation will **hold true.**

A double-entry account

An account

Debit	**Credit**

Double-entry rules

At AS level, you must apply double-entry rules to record the following:

- Assets and expenses
- Capital and liabilities
- Sales and purchases.

Assets, expenses and liabilities

- To increase an asset or expense, a **debit** is made to the account.
- To reduce an asset or expense, a **credit** is made to the account.
- To increase the capital or a liability, a **credit** is made to the account.
- To reduce the capital or a liability, a **debit** is made to the account.

Example 1

On 1 March 2008, Dave started a business by opening a business bank account with £30,000.

This transaction will increase the asset of the bank and increase the amount of capital.

Bank

1 March Capital 30,000	

Capital

	1 March Bank 30,000

If the bank is increased, then the bank account must be a **debit** and the other entry must be a **credit**.

Dave has increased his bank account balance on 1 March and a **debit** must be made to the bank account; the **credit** entry must be made in the capital account.

Example 2

On 2 March Dave bought a motor van, paying £10,000 by cheque.

Bank

1 March Capital 30,000	2 March Motor van 10,000

Motor van

2 March Bank 10,000	

The bank account must be reduced by paying the cheque and a **credit** must be made in the account.

Dave has now acquired a motor van for the business. The motor van is a fixed asset and a **debit** must be made to the account.

Purchases of goods for resale

A business will purchase goods for resale to make a **profit**.

Goods for resale must always be entered in the **purchases account**.

A business could purchase goods in the following ways:

- Cash
- Payment by cheque
- Credit terms from a trade supplier

Example: cash

Purchased a good for £1000 cash.
Debit the purchases account and credit the cash account.

Cash account	
	Purchases 1000

Purchases account	
Cash 1000	

Example: cheque

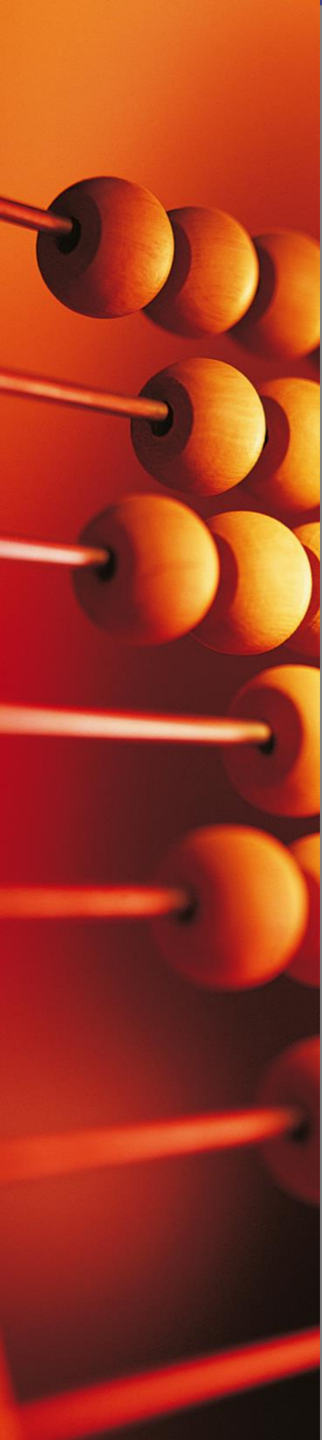
Bought good for resale, paying £5000 by cheque. Debit the purchases account and credit the bank account.

Purchases account

Bank 5000	

Bank account

	Purchases 5000



Example: credit

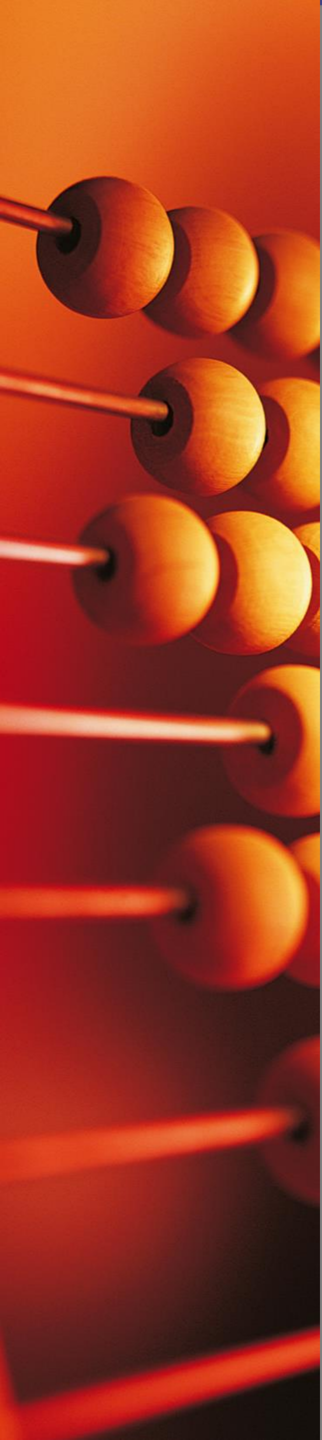
Bought good from M Barton on credit, for £4000.
Debit the purchases account and credit the supplier’s personal account.

Purchases account

M Barton 4000	

M Barton

	Purchases 4000



Accounting for sales

When a business makes a sale to a customer, the amount must be recorded in the **sales account** at the **selling price**.

A business could make sales in the following ways:

- Cash
- Payment received by cheque
- Credit terms.

Cash sales or payment by cheque:

Debit the cash account and credit the sales account.

Credit sales:

Debit the customer's personal account and credit the sales account.

A credit customer is a **debtor** in the accounts.

Example

On 1 March 2008, a business sold goods to L May on credit for £4000.

Sales account

	1 March L May 4000

L May

1 March Sales 4000	

Purchase returns

A business may return goods to a supplier.

Debit the supplier’s personal account. Credit the purchase returns account.

Purchase returns are also known as **returns outwards**.

Example

Returned goods to F Layton for £4000 on 5 March.

F Layton

Purchase returns 4000	

Purchase returns

	F Layton 4000

Sales returns

Credit customers may return goods to the business.

Debit the sales returns account. Credit the customer's personal account.

Sales returns are also known as **returns inwards**.

Example

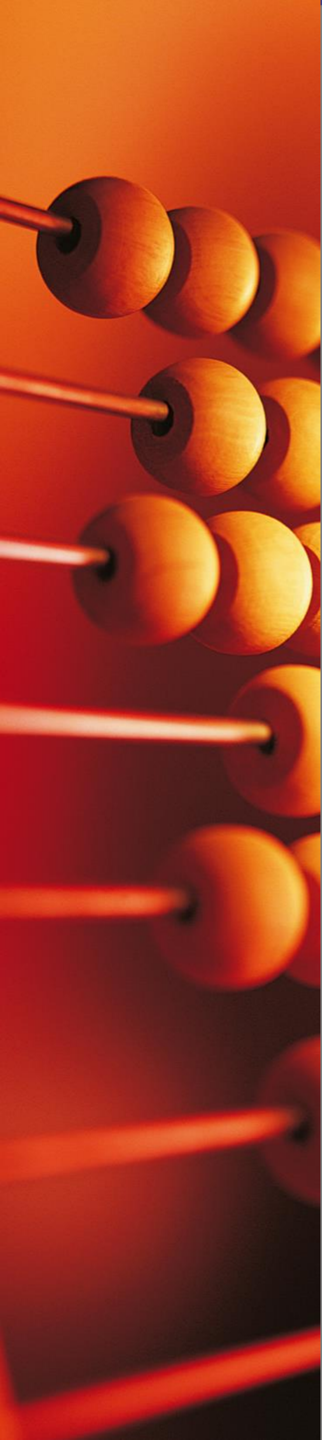
N Williams returned goods to the business for £ 5000.

N Williams

	Sales returns 5000

Sales returns

N Williams 5000	



Balancing off an account

At the end of the month, it is good practice to balance off each account and bring the balance forward to start the next month.

Bank

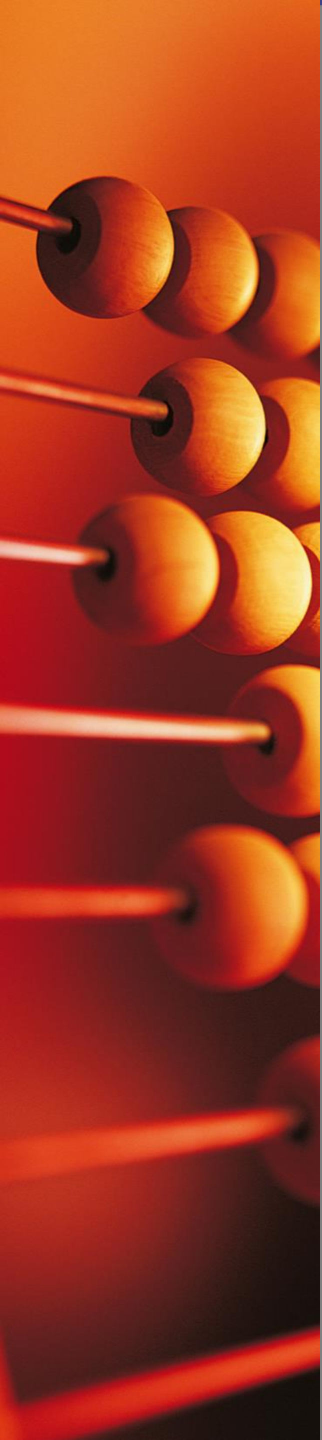
1 Capital	10,000	5 Motor car	2,000
24 Sales	2,000	12 Purchases	4,000
		20 Equipment	1,000
		32 Bal c/d	5,000
	12,000		12,000
1 Bal b/d	5,000		

Discount allowed

A business may decide to allow a debtor a discount if they pay their account within a given time period. A business will offer a discount to improve the **cash flow**.

Debit the discount allowed account. Credit the debtor's personal account.

Discount allowed is an **expense** and will reduce **profit**.

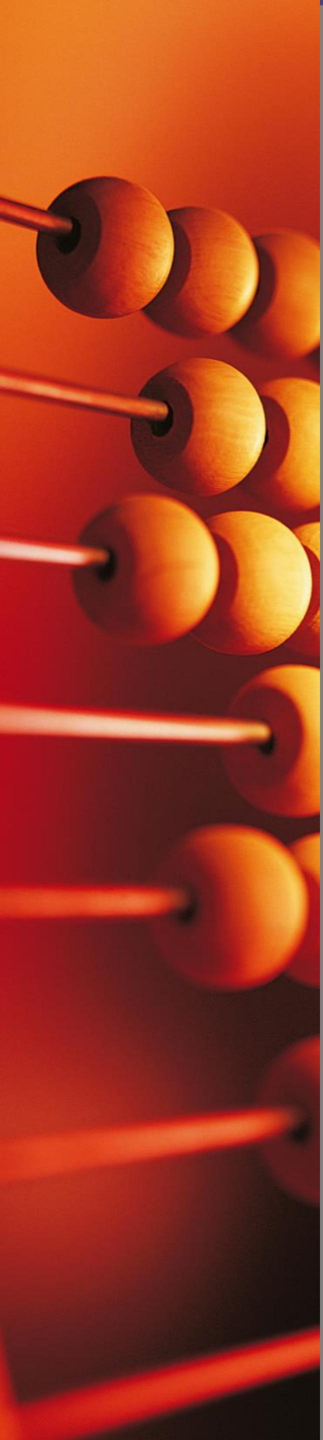


Example

Fred Smith is a debtor who owes £5000. He is allowed a 5% discount if he pays his account by cheque.

F Smith

Bal b/d	5000	Bank	4750
		Discount allowed	250
	5000		5000



Discount received

A business could receive a discount from a trade **creditor** if it pays within a given time period.

Debit the trade creditor. Credit the discount received account.

Discount received is an **income** and will increase the **profit**.

Example

S Wright, a creditor, is owed £10,000. If the business pays by cheque, it will receive a 5% discount from S Wright.

S Wright

Bank	9,500	Bal b/d	10,000
Discount received	500		
	10,000		10,000