3.1 | Double entry system

- **Dual aspect of a transaction**
- **Principles of double entry**
- **Account and its format**
- **Types of ledger accounts**
- **Main elements of financial statements**

Double entry system	
Dual aspect of a transaction	• The double entry system was first introduced by an Italian priest named Father Luca Pacioli in the year 1494 AD. • The economic result of the dual aspects of each transaction affects the business in two ways, and the recording of the two aspects is known as the double entry system.
Principles of double entry	• The principle of double entry guides the recording of the dual aspects of each transaction as 'debit' and 'credit'. • The increase or decrease in assets, liabilities, and capital, as a result of each business transaction is recorded as a 'debit' or 'credit'. • Whether an entry should be recorded as a 'debit' to show either an increase or decrease is guided by the double entry principles. • The double entry system also requires that for all transactions, the amounts entered as debits must be equal to the amounts entered as credits.

| Ledger accounts	
Account	• When recording financial transactions, the standard format that is followed is known as an "account". It shows the dual aspects of all transactions recorded in chronological order. • A ledger account takes the form of the letter "T" and hence, is also called a T account. • Transactions can be categorized into 5 types of ledger accounts: Assets, Liabilities, Equity, Income, and Expenses. These accounts also constitute the basic elements of financial statements.
Ledger	• Ledger is the record in which all of the accounts are stored in. This can be maintained in a book, as individual account sheets, or in electronic devices.

Format of an account:

(i) Account format:

Debit	Account Name	Credit

(ii)

DR ....Account **CR**

Date	Details	Folio Ref	Amount	Date	Details	Folio Ref	Amount

(iii)

.................Account

Date	Details	Folio Ref	Amount		Balance	
			Debit	Credit	Debit	Credit
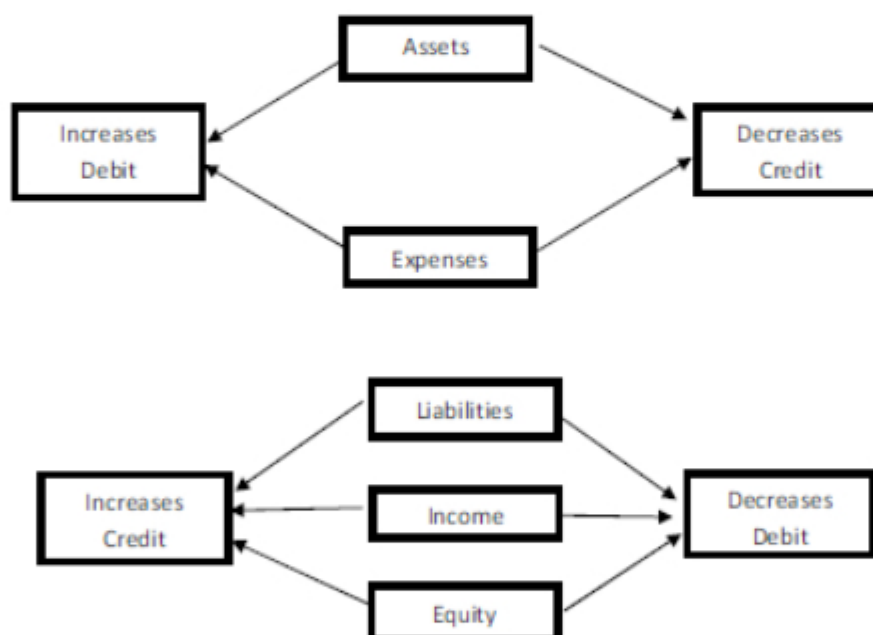
Transaction	Dual aspect	Double entry
Eg: 1. Obtaining bank loan of Rs.100,000.	1. Bank asset increases 2. Bank loan liability increases	1. Bank account – Debit 2. Bank loan account - Credit

1	Owner introduces Rs. 2,000,000 to start the business	
2	Owner withdrew Rs. 50,000 for personal reasons	
3	Owner withdrew Rs. 5,000 worth of goods for his personal use	
4	Purchasing goods for Rs. 50,000	
5	Purchasing goods on credit from Amanda's business for Rs. 80,000	
6	Paid Rs. 20,000 to Amanda	
7	Cash sales for Rs. 100,000	
8	Credit sales to Dilum for Rs. 10,000	
9	Received Rs. 10,000 from Dilum	
10	Purchase of office equipment worth Rs. 150,000	
11	Obtaining bank loan of Rs. 200,000	
12	Deposited Rs. 100,000 in a fixed deposit	
13	Paid staff wages for Rs. 10,000	
14	Paid electricity expense of Rs. 8,000	
15	Electricity payable of Rs. 1,000	
16	Prepaid electricity of Rs. 2,000	
17	Received rent income of Rs. 5,000	
18	Commission receivable Rs. 1,000	
19	Machinery depreciation expense Rs. 10,000	
20	Bad debt of Rs. 10,000	
21	Discount allowed of Rs. 2,000 when Nalaka settled Rs. 10,000 in cash	
22	Discount received Rs. 1,000 when settling Silva's account of Rs. 5,000	