

CHAPTER-7

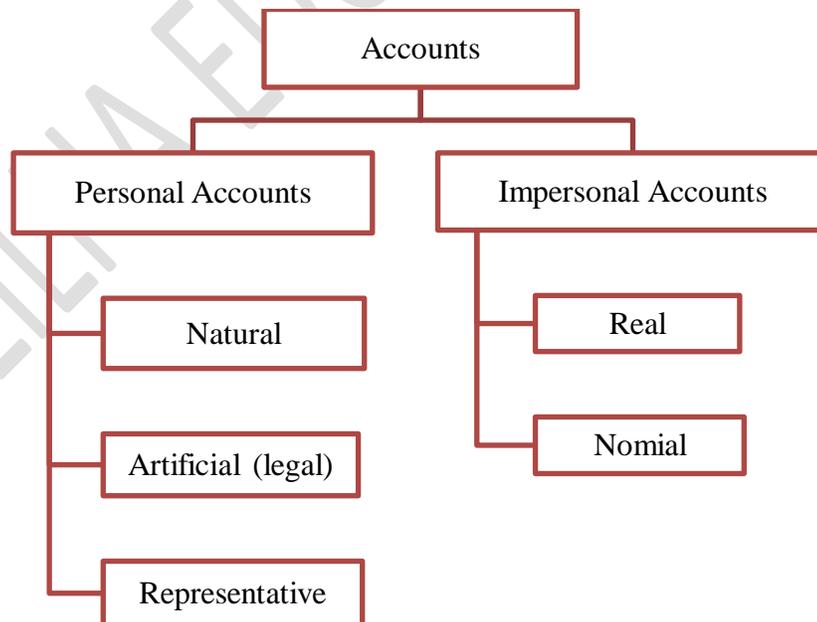
DOUBLE ENTRY SYSTEM

"Every transaction involving money or money's worth has a two fold aspect the receiving of a value on the one hand and the giving or the same value on the other This two fold nature in all transactions must be recorded in the books, and this gives rise to the term Double Entry Book-keeping"
- *Munro and Palmer*

Double entry system is the most progressive scientific and complete system of regarding the financial transactions or business. The rules of recording transactions under this system are so definite and clearly stated that the system is being used extensively in all countries According to this system there are two accounts involved in every business transaction. One of them is debited and the other is credited.

Meaning of Double Entry System- According to this system every business transaction affects at least two accounts in opposite directions. For example, if the furniture is purchased in the business, furniture is increased whereas the cash is decreased. There can be no transaction in the business which affects only one account or which has only one aspect. As such, both the aspects of every transaction are recorded under this system. It may, however, be noted that the double entry does not mean that a transaction is recorded twice. But it means that at least two accounts are affected by a transaction - one account receiving a benefit and the other account yielding a benefit. The person or the account receiving a benefit is debited and the person or the account who gives something to the business is credited. The amount of every transaction is written twice, once as a debit and again as a credit.

Classification of Account



Personal Accounts -The accounts which relate to an individual, firm, company or an institution are called personal accounts. Account of Mohan, Account of Ram ChanderKrishanChander, Account of D.C.M. Limited, Account of Delhi University, Bank Account, Capital Account of the proprietor, Drawings Account of the proprietor etc. are examples of Personal Accounts.

Rule

Rule for recording a transaction in personal accounts in simple words is "Debit the receiver and credit the giver". In other words, "Debit that person's account who receives something from the business and credit that person's account who gives something to the business".

(A) **Natural Personal Accounts** - Accounts of 'Natural Persons' means the accounts of human beings. For example, Mohan's Account, Sohan's Account, Seema's Account, Nirmla's Account etc. Proprietor's Capital Account, Proprietor's Drawings Account, Debtors Accounts and Creditors Accounts are also included in this category.

B) **Artificial Personal Accounts**-These account do not have physical existence as human beings. But they work as personal accounts. For example, any Firm's account, any limited company's account, any institution's account and any bank's account. These are treated as artificial persons for the recording of business transactions, these accounts also include the accounts of Clubs, Insurance Companies and the accounts of Government Departments which are recognised as 'person in the business dealings.

Representative Personal Account- When an account represent a particular person particular person or group of persons, it is termed as a representative personal account. For example, if the salaries for the month of December are not paid to the employees, the amount payable to these employee will be added and put under one common title "Salaries Outstanding Account."

Real Account- The accounts of all those things whose value can be measured in terms of money and which are the properties of the business are termed as Real Accounts. Such as, Cash Account, Furniture Account, Machinery Account, Building Account, Goodwill Account etc.

Rule- Rule for recording a transaction in real account is 'Debit what come in and Credit what goes out'.

(a) **Tangible Real Accounts**- Tangible Real Accounts are the accounts of those things which can be touched, felt, measured, purchased, sold etc.

Example of such accounts are cash account, Stock Account, Furniture Account, Land Account, Building Account etc.

(b) **Intangible Real Account**- These accounts represent such things which cannot be touched, but, course, their value can be measured in terms of money.

Example are Goodwill account, Patents account, Trade Marks account, Copyrights account etc.

Nominal Account-These accounts include the account of all expenses and incomes.

The example of nominal accounts relating to expenses are Salaries paid, Rent paid, Discount allowed, Bad Debts etc.

Rule-Rule for recording in nominal account is “Debit the expenses and losses and Credit incomes and gains.”



Advantages of Double Entry System or Causes of its Popularity

- (1) **Scientific System:** - The transactions are recorded according to certain specified rules and as such, the system is more scientific us compared to any other systems of Book-Keeping.
- (2) **Complete record of every transaction:** - The complete record of every transaction are maintained in this system, so that if the need arises full details of every transaction can be easily made available at any time in future.
- (3) **Prepared of Trail Balance:** - In double entry system, the amount recorded to the debit sides of various accounts will always be equal to the amounts recorded on the credit sides of various accounts.
- (4) **Preparation of Trading and Profit & Loss Account:** - With the help of the trail balance, a Trade can prepare a Trading Account to find out the amount of gross profit or gross loss.
- (5) **Knowledge of financial position of the business:** - In double entry system, separate accounts are opened for each and every asset and liability of the firm and as such, a Balance Sheet can be prepared which is a screen picture of the financial position of a business at a certain moment. A Balance Sheet reports the property values owned by the enterprise and the claims of the creditors and owners against these properties.

(6) **Knowledge of various informations:** - In double entry system the accounts are maintained in such a way that the information regarding the following is readily available at any point of time: -

- (i) What is the amount of sales, purchase and closing stock?
- (ii) What amount is due to be received from customers or in other words, the total number of debtors and the amount in each case?
- (iii) What amount is due to be paid to suppliers or in other words, the total number of creditors and the amount in each case?

(7) **Lesser possibility of fraud:** - This system of book-keeping records each transaction in two accounts, as such there is hardly any scope of forgery and manipulation as compared to other systems. If at all some manipulation takes place, it can be easily detected.

(8) **Legal Approval:** - Complete record of each transaction is maintained under this system according to certain specified rules. As such, the system meets legal requirements and books of accounts maintained under this system are accepted as true and reliable by the Companies Act and various other Acts.

(9) **Comparative Study:** - The management can compare the expenditure of the current year with those of the previous years and can know on what head of expenditure the money spent is unreasonable and can take step to check the unnecessary expenditure.

(10) **Help management in Decision Making:** - The management can obtain all the requisite information quickly and also the information provided by the system is most reliable. Hence, the management can use the information for making decisions.

(11) **Suitable for all Types of Businessmen:** - the system is so flexible that it can be conveniently introduced in small as well as big type of business.

Disadvantages of Double Entry System

(1) A number of books are to be kept under this system, as such, the system is quite expensive.

(2) It is quite difficult to apply the rules of debit and credit. Proper education, practical knowledge and training is required in order to have command over the rule of double entry system.

(3) Only the arithmetical accuracy of the account is checked by preparing a trial balance under the double entry system, following types of errors are not disclosed under the system: -

- (i) **Errors of Omission:** - If a transaction remains altogether unrecorded in the books of original entry.
- (ii) **Errors of Commission:** - If wrong amount is recorded in the books of original entry.
- (iii) **Errors of Principle:** - If the amount is recorded on the correct side though in a wrong account. For example, if purchase of machinery is debited to purchase account instead of machinery account.

(iv) **Compensating Errors:** - If the effect of one error is cancelled by the effect of some other errors.

VERY SHORT ANSWER QUESTION

1. What is Double Entry System of Book –Keeping ?

Ans : Double entry system refers to a system of accounting in which every transaction affects atleast two account two accounts simultaneously . One of them is debited and other is credited .

2. State the Type of Accounts.

Ans : (i) Personal Accounts ;,(ii) Real Account and (iii)Nominal accounts

3. What are personal account ?

Ans The accounts which relate to an individual , firm , company or institution are called personal account .

4. What are Real Account ?

Ans :The account of all those things whose value can be measured in terms of money and which are the business are termed as Real Accounts such as Cash Account , furniture Account etc.

5. What are the Nominal Accounts ?

Ans :These are the accounts which are in name only and which do not really exist such as the accounts of all expenses and incomes.

6. What are Natural Personal Account ? Give one example .

AnsAccount of ‘Natural Persons’ means the accounts of human being . For example ,Mohans’s Account .

7. What are Artificial Personal Account? Give one Example .

Ans :These accounts do not have physical existence as human being but they work as personal account . For example , any firm’s account

8. What are Representative Personal Account? Give one example ?

Ans: When an account represents a particular or group of person ,it is termed as a representative personal account. For example , ‘Outstanding Rent’ account.

9. What is the rule of recording transactions in personal accounts?

Ans: debit the receiver and Credit the giver.

10. What is the rule of recording transaction in Real Accounts?

Ans: Debit what comes in and Credit what goes out.

11. What is the rule of recording transaction in Nominal Accounts?

Ans: Debit the expenses and losses and Credit incomes and gains.

OBJECTIVE TYPE QUESTIONS

1. Classify the following accounts into Personal , Real or Nominal accounts:-

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|--------------|--------------|
| I. Machinery | VII. Drawing |
| II. Capital | VIII. Salary |

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| III. Stock | IX. Outstanding Salary |
| IV. Bad Debts | X. Insurance |
| V. Good Will | XI. Prepaid Insurance |
| VI. Sales | XII. Interest Received |

Ans :

Personal Account	II , VII , IX , XI
Real Account	I , III , V
Nominal Account	IV, VI , VIII , X, XII

2. State to which class of accounts does each of the following relate:-

- | | |
|------------------|-------------------------------------|
| I . Cash | V, Creditors |
| II . Bank | VI Commission Received |
| III. Trade Marks | VII Accrued Commission |
| IV Debtors | VIII Commission Received in Advance |

Ans :

Personal Account	II , IV , V , VII , VIII
Real Account	I , III
Nominal Account	VI

3. Classify the following into three types of personal accounts:

- I. Capital
- II. Tata Steel Company
- III. Debtors Account
- IV. Outstanding Expenses Account
- V. Bank Account
- VI. Haryana Education of Commerce
- VII. Shri Ram College of Commerce

Ans:

Natural Personal Account	I , III
Artificial Personal Account	II , V , VI , VII
Representative Personal Account	IV