

Politicians need to do double-entry

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Double-entry bookkeeping is based on a fundamental economic truth: that every action has a reaction.

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This is the audio version:

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This is the transcript:

I believe in double entry.

Now, that's hardly surprising. I have, for over 40 years, been an accountant. I was a chartered accountant in practice for most of that period of time. Of course, I believe in double-entry bookkeeping.

That is the way in which every set of books, of every organisation, in almost every country around the world, is recorded because it reflects a fundamental truth , and that is that for every action in the economy, there is a reaction. And that is what double-entry records.

People get confused about what debits and credits mean. They wonder whether they should be on the left or right when they're learning accounting, but it doesn't matter.

What matters is that fundamental understanding that if you're going to undertake a transaction, there isn't just one consequence; there will always be two.

There will be two within your organisation, but for any transaction that is of any significant consequence in the world, you will be transacting with somebody else. So not only is there a reaction for you, there is a reaction for someone else. And what you have to think about, particularly if you are a politician, and this is where I get to my point, if you are a politician, you have to think about what is the reaction to your action? And our politicians don't do that.

And that is why I want to talk about double entry, because if our politicians began to understand this fact that every action has a reaction, I believe that we would get vastly better politics than we've got.

Just think about it. If somebody sells something, somebody has to buy it.

If the government wants to tax, somebody has to pay it.

If somebody wants to trash our climate, then at some time in the future, somebody's going to bear the consequence.

If you want to balance the state's books, you're going to probably unbalance the private sector's books because they're going to suffer the consequence.

And, if you want to cut government spending, as is so often the desperate desire of most neoliberal politicians, somebody's not going to get the benefit of the money that you might have otherwise spent and, as a consequence, there is going to be less money in the private sector economy, which is probably going to shrink in size as a result.

For every debit, there is a credit. For every action, there is a reaction. That's the way the world works and the way it will always work.

And yet our politicians aren't told that.

Even worse, governments try to pretend that this isn't true, and nowhere is this more apparent than when we look at the government's accounts. Take the UK for example, but the same model is basically used throughout Europe, in the USA, and in other developed countries, right around the world. When we look at those accounts, they are prepared on a single-entry basis. There is no double-entry accounting in the data produced by the Office for National Statistics for the UK Treasury to advise ministers upon, month in, month out, throughout the year, and on which we are told whether the economy is growing or not.

There are, therefore, no checks and balances in this data. There is no recognition of consequences in this data, and some of that data is absolutely stupid as a result of there being no double entry reflected in the way in which it is constructed.

Let me take a simple example. Over 10% of the UK's national income is supposedly made up of rent that people like me, who own their own house, whether with a mortgage or not, pay ourselves for the right to live in our own properties month in, month out.

Let me assure you of something. I do not pay myself rent to live in my own house. Nor does anybody else I know in the entire UK economy pay rent to live in their own house.

What's even more important is that recording a transaction between a person and themselves is about as meaningful in economic terms as shifting a £10 note from your left pocket to your right pocket. It is utterly economically inconsequential, and yet, according to our Office for National Statistics, 10% of our national income is made up of this completely made-up transaction between one person and themselves.

This is ludicrous, and that is the consequence of making up economic data that does not follow the rules of double entry.

There is no double entry here because a person can't do a transaction with themselves: it nets out to zero, always. Therefore, there is nothing to record, and yet our politicians are told that this matters.

And at the same time, they are also given data, which is fundamentally wrong.

For example, the figures for the UK national debt are not prepared on the basis of double-entry bookkeeping. There is debt in there that does not exist. At one point, well over £200 billion of the UK national debt was made up of something called the 'Bank of England contribution'. It is still significant. It's around a hundred billion plus, and yet the Bank of England contributes precisely nothing to the UK's national debt.

This is a made-up figure representing the supposed consequence, which has not occurred, of transactions involving quantitative easing, which might not ever happen, either.

And yet at the same time, there are liabilities that genuinely exist in the economy, which are not recorded, like some pension data, and as importantly, there is no data in the figure for national debt about what the national debt actually funds.

In other words, our schools, our hospitals, our infrastructure, our roads, our transport systems, our electricity networks, if they are state-owned, and everything else that is paid for by the government.

This is a singular and inappropriate view of the government as a consequence, because

it fails to take into account that there is double entry or that there is the balancing figure on every balance sheet of every organisation in the country, which is the equity of those to whom the organisation is accountable, in this case, us, the people of the country.

So we have a crazy situation where politicians are told that they may take actions which have no consequences. But, that's not true. We know that, and I'll go back to the issue of cutting government expenditure, this does have consequences. Cut benefits, and immediately shops do not have as much spent in them because everybody who gets benefits in this country spends the benefit that they get to support their lifestyle, and yet ministers apparently don't know that because they don't know that actions have reactions.

And at the same time, they are taught to think purely about the silo in which they operate. So, a minister for the NHS only thinks about the NHS when they think about health. They don't think about the consequences for work, for the economy, for how social care is impacted, because that's in another department. The 'action has a reaction' idea is simply not present in their thinking.

And in my opinion, this is a national economic scandal. Not only is the data that we are using for national decision making wrong because it doesn't reflect the fact that double entry bookkeeping is the core of good accounting, but ministers are being told that there is no consequence of their action because there is no reaction to the entry that they effectively make in the nation's accounts by the decisions that they make.

Until we understand this, we are going to have poor decision-making.

Until ministers are taught this most basic accounting truth, they will not realise that they have to think rather more broadly than most of them do at present.

This might challenge their little minds, and I'm afraid to say, many of them appear to have rather small economic minds, but this fundamental truth has to be at the core of our economic management, or we're going to continue to be in deep economic trouble.

Accountancy has a purpose.

Double-entry bookkeeping has a purpose.

Politicians need to learn it.

If they did, they would be better at their jobs.