CHAPTER - II

RECONSTITUTION OF PARTNERSHIP

(CHANGE IN PROFIT SHARING RATIO AMONG THE EXISTING PARTNERS, ADMISSION OF A PARTNER, RETIREMENT/DEATH OF A PARTNER)

Admission of a Partner

Learning objectives:-

After studying this lesson, the students will be able to:

- Identify and deal effectively with the situation of reconstitution of partnership.
- Identify the problem arising due to admission of a partner in the firm.
- Calculate new and sacrifice ratio in different cases.
- Understand, calculate and make treatment of goodwill in different cases.
- Make accounting treatment of the revaluation of assets and liabilities and distribute the profit and loss on revaluation among the old partners.
- Make accounting treatment of unrecorded assets and liabilities
- Prepare capital Accounts, Cash A/c and Balance Sheet of the New firm
- Adjust the Partners' Capital Accounts

Salient Points:-

1. Goodwill is the monetary value of business reputation. It is an intangible asset.
2. Goodwill may be of two types:
   a. Purchased goodwill
   b. Non-purchased goodwill
3. When existing firm faces problem of limited financial resources and man power then one new additional partner enters into firm.
4. There are three methods of valuation of goodwill:
   a. Average Profit Method
   b. Super Profit method
   c. Capitalisation Method
5. When new partner is admitted into existing partnership then existing partners have to sacrifice in favour of new partner, it is called sacrificing ratio.

6. Share of goodwill of new partner will be credited to sacrificing partners into their sacrificing ratio.
7. At the admission of new partner Profit & Loss on revaluation of assets and liabilities and balances of accumulated profits & losses will be distributed among old partners (only) in old ratio.

Ql. At the time of change in profit sharing ratio among the existing partners, where will you record an unrecorded liability?

Ans. Revaluation Account-Debit side

Q2. Anand, Bhutan and Chadha are partners sharing profits in ratio of 3:2:1. On 1st April 2007, they decided to share profits equally.Name the partners who is gaining on consequence of such change.

Ans. Chadha.

Q3. Give two characteristics of goodwill.

Ans. (i) it is an intangible asset having a definite value.

(ii) It helps in earning more profit.

Q4. Name any two factors affecting goodwill of a partnership firm.

Ans. (i) Favorable location (ii) Time period

Q5. In a partnership firm assets are Rs.5, 00,000 and liabilities are Rs. 2, 00,000. The normal profit rate is 15%. State the amount of normal profits.

Ans. Rs.45,000

Q6. State the amount of goodwill, if goodwill is to be valued on the basis of 2 years' purchase of last year's profit. Profit of the last year was Rs.20, 000.

Ans. Rs.40,000

Q7. Where will you record 'increase in machinery' in case of change in profit sharing ratio among the existing partners?

Ans. Revaluation Account- Credit Side.

Q8. Name two methods for valuation of goodwill in case of partnership firm.

Ans. (i) Average Profit Method (ii) Super Profit Method

Q9 Give formula for calculating goodwill under 'super profit method'.

Ans. Goodwill = Super Profit x Number of Years' Purchase.

Q 10. Pass the journal entry for increase in the value of assets or decrease in the value of liabilities in the Revaluation A/c?

Ans Assets A/c Dr. (with the amount of increase)

Liabilities A/c Dr. (with the amount of decrease)

To Revaluation A/c (with the total amount of gain)

(Being revaluation of assets and liabilities)

Qll. P,Q and R are partners in a firm sharing profits in the ratio of 2:2:1 on 1.4.2007 the partners decided to share future profits in the ratio of 3:2:1 on that day balance sheet of the firm shows General Reserve of Rs 50,000. Pass entry for distribution of reserve.

Ans.

General Reserve A/c	Dr.	50,000	
To P's Capital A/c			20,000
To Q's Capital A/c			20000
To R's Capital A/c			10000
(Being Reserve distributed)			

Q12. "The gaining partner's should compensate to sacrificing partner's with the amount of gain." Journalise this statement.

Ans. Gaining Partner's Capital A/c Dr

To Sacrificing Partner's Capital A/c

(Being compensation given by gaining partner to sacrificing partner)

Q13. What are the two main rights acquired by the incoming new partner in a partnership firm? ,

Ans, The two main rights are:

(i) Right to share the assets of the firm.

(ii) Right to share the future profits of the firm.

Q14. A and B are partners, sharing profits in the ratio of 3:2. C admits for 1/5 share . State the sacrificing ratio.

Ans. Sacrificing Ratio - 3:2.

Q15. How should the goodwill of the firm be distributed when the sacrificing ratio of any of the existing partner is negative (i.e. he is gaining)

Ans. In this case the partner with a negative sacrificing ratio, i.e. the gaining partner to the extent of his gain should compensate to the sacrificing partner to the extent of his gain.

Ql6. In case of admission of a partner, in which ratio profits or loss on revaluation of assets and reassessment of liabilities shall be divided?

Ans. Old ratio.

Q17. Give journal entry for distribution of 'Accumulated Profits* in case of admission of a partner.

Ans. Accumulated Profit A/c Dr.

To Old Partners Capital A/c

(Being distribution of accumulated profits among old partners)

Q18. At the time of admission of partner where will you record 'unrecorded investment'?

Ans. Revaluation Account- Credit side.

Q19. The goodwill of a partnership is valued at Rs.20,000. State the amount required by a new partner, if he is coming for 1/5 share in profits.

Ans. Rs.4,000.

Q20. What journal entries should be passed when the new partner brings his share of goodwill in kind?

And.

(i) Assets A/c Dr -
To Premium for goodwill A/c

(ii) Premium for goodwill A/c Dr -
To Sacrificing Partners' Capital A/c

Q21. What journal entries will be passed when the new partner is unable to bring his share of goodwill in cash?

Ans. New Partner's Capital A/c Dr. - -
To Sacrificing Partners' Capital A/c

Q22. In case of admission of a new partner, goodwill was already appearing in the books of the firm. Give journal entry for its treatment

Ans Old Partners Capital A/c Dr.
To Goodwill A/c -

(Being old goodwill written off among old partners)

Q23. At the time of admission of a new partner, workmen's compensation reserve in appearing in the Balance sheet as Rs 1,000. Give journal entry if workmen's compensation at the time of admission is estimated at Rs 1,200.

Ans: Revaluation A/c 200
To Workmen's Compensation Reserve A/c 200

(Being workmen's compensation estimated at Rs. 1,200)

Q24. Give journal entry for recording deceased partner's share in profit from the closure of last balance sheet till the date of his death.

Ans. Profit & Loss Suspense Account Dr.
To Deceased Partner's Capital Account

(Being share of profit to deceased partners)

Q25. Define gaining ratio.

Ans. Gaining ratio is the ratio in which remaining/continuing partners acquire the share of the outgoing partner(s).

Q26. Give two circumstances in which gaining ratio can be applied.

Ans. (i) Retirement of a partner (ii) Death of a partner. .

Q27. At the time of retirement of a partner give journal entry for writing off the existing goodwill.

Ans. All Partners Capital (including retiring) A/c Dr.

To Goodwill A/c

(Being old goodwill written off among all partners in, old ratio)

1 Mark Questions

Admission of a Partner

Q.1 State the two financial rights acquired by a new Partner?

Ans. New partner is admitted to the partnership if it provided in the partnership deed or all the existing partners agree to admit the new partner. Section 31 of the Indian Partnership Act 1932 Provides that a person may be admitted as a new partner into a partnership firm with the consent of all the Partners.

Q.2 Give the name of the compensation which is paid by a new Partner to sacrificing Partners for sacrificing their share of profits.

Ans. When a partner joins the firm, he gets the following two rights along with others:

i) Right to share future profit of the firm and

ii) Right to share the assets of the firm.

Q.3 Enumeration the matters that need adjustment at the time of admission of a new Partner.

Ans. The matter that needs adjustment of the time of admission of a new partner is:

i) Adjustment in profit sharing ratio and adjustment of capital

ii) Adjustment for goodwill

iii) Adjustment of Profit / Loss arising from the Revolution of Assets and Reassessment of Liabilities.

iv) Adjustment of accumulated profits, reserves and losses.

Q.4 Give two circumstances in which sacrificing Ratio may be applied.

Ans. Circumstances in which sacrificing Ratio may be applied are:

i) At the time of admission of a new partner for distributing goodwill brought in by the new partner.

ii) For adjustment goodwill in case of change in Profit - sharing ratio of existing partners.

Q.5 Why is it necessary to revalue assets and reassess liabilities of a firm in case of admission of a new partner?

Ans. The assets are revalued and liabilities of a firm are reassess, at the time of admission of a partner because the new partner should; neither benefit nor suffer because change in the value of assets and liabilities as on the date of admission.

Q.6 What are the accumulated profit and accumulated losses?

Ans. The profit accumulated over the years and have not been credited to partners' capital A/c are known as accumulated Profit or undistributed profit, e.g. the General Reserve, Profit and Loss A/c (credit balance).

The losses which have not yet been written off to the debit of Partners' Capital A/c are known as accumulated Losses, e.g. the Profit and Loss A/c appearing on the assets side of Balance Sheet, etc.

Q.7 Explain the treatment of goodwill in the books of a firm on the admission of a new Partner when goodwill already appears in the Balance sheet at its full value and the new partner brings his share of good will in cash.

Ans. By following accounting standard - 10, the existing goodwill (i.e. goodwill appearing in the Balance Sheet) is written off to the old partners Capital a/c in their old profit sharing ratio.

Old partners capital A/c Dr. .....
To Goodwill A/c [in old Ratio]

[Being the existing g/w written off in the old ratio.]

Q.8 Under what circumstances the premium for goodwill paid by the incoming Partner will not recorded in the books of Accounts ?

Ans. When the premium for goodwill is paid by the incoming partner privately, it is not recorded in the books of A/c as it is as a matter outside the business.

Q.9 A and B share profits and losses in the Ratio of 4:3, they admit C with 3/7th share; which he gets 2/7th from A and 1/7 from B. What is the new profit sharing ratio?

Ans. A : - = 4/7-2/7 =2/7
B : : = 3/7-1/7=2/7
C : =2/7+1/7=3/7
New Profit sharing Ratio is 2:2:3.

Q.10 The capital of A and B are Rs. 50,000 and Rs. 40,000. To Increase the Capital base of the firm to Rs. 1, 50,000, they admit C to join the firm; C is required to Pay a sum of Rs. 70,000, what is the amount of premium of goodwill?

Ans. The total capital of the firm is Rs. 90,000. To increase the capital base to Rs. 1, 50,000, C is to bring in Rs. 60,000 (Rs. 1, 50,000 - 9, 00, 00) But he bring in Rs. 70,000. Therefore, the excess of Rs. 10,000 represent premium for goodwill.

Q.11 Distinguish between New Profit - sharing ratio and sacrificing ratio?

Ans. Distinction between New Profit - Sharing ratio and sacrificing ratio:

	New Profit sharing Ratio		Sacrificing Ratio
1)	It is related to all the Partners (Including new)	1)	It is related to old partners only
2)	It is the ratio in which the all Partner (including new) will share Profit in future.	2)	It is the ratio in which old partners have sacrificed their share in favour Of new Partner or when profit

Sharing Ratio is changed.

3) New Profit sharing Ratio = Old Ratio - Sacrificing Ratio

3) Sacrificing Ratio = Old Ratio - New Ratio

2-3 marks questions:

Q 1 A & B are partners sharing in the ratio of 3:2. C is admitted. C gets 3/20th from A and 1/20th from B. calculate new and sacrifice ratio

Ans: 9: 7: 4

Q2 X & Y are partners share profits in the ratio of 5:3. Z the new partner gets 1/5 of X's share and 1/3rd of Y's share. Calculate new ratio.

Ans: 4:2:2

Q 3 P & Q are partners sharing in the ratio of 5:3. They admit R for 1/4th share and agree to share between them in the ratio of 2:1 in future. Calculate new ratio.

Ans: 2:1:1.

6-8 marks Questions

Q.1 Dinesh, Yasmine and Faria are partners in a firm, sharing profits and losses in

11:7:2 respectively. The Balance Sheet of the firm as on 31st Dec 2001 was as follows:

Liabilities	Rs.	Assets	Rs.
Sundry Creditors	800	Factory	7,350
Public Deposits	1,190	Plant & Machinery	1,800
Reserve fund	900	Furniture	2,600
Capital A/c		Stock	1,450
Dinesh	5,100	Debtors Rs. 1,500	
Yasmine	3,000	Less: bad debts Rs. 300 provisions	1,200
Faria	5,000	Cash in hand	1,590
	15,900		15,900

On the same date, Annie is admitted as a partner for one-sixth share in the profits with Capital of Rs. 4,500 and necessary amount for his share of goodwill on the following terms:-

a. Furniture of Rs. 2,400 was to be taken over by Dinesh, Yasmine and Faria equally.

b. A Liability of Rs. 1,670 is created against Bills discounted.

c. Goodwill of the firm is to be valued at 2.5 years' purchase of average profits of 2 years. The profits are as under:

2000:- Rs. 2,000 and 2001 - Rs. 6,000.

d. Drawings of Dinesh, Yasmine, and Faria were Rs. 2,750; Rs. 1,750; and Rs. 500 Respectively.

e. Machinery and Public Deposits are revalued to Rs. 2,000 and Rs. 1,000 respectively.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm.

Solution 1

Books of Dinesh, Yamine, Farte and Anie

REVALUATION ACCOUNT

Particulars	Rs.	Assets		Rs.
To Bills Discounted A/c	1670	By Public deposits A/c	190	
		By Machinery A/c		200
		By Loss transferred to		
		Dinesh's capital A/c	704	
		Yasmine's Capital A/c	448	
		Faria's Capital A/c	128	1280
	1670			**1670**

PARTNERS' CAPITAL ACCOUNTS

Dr. Particulars	Dinesh Rs.	Yasmine Rs.	Faria Rs.	Annie Rs.	Particulars	Dinesh Rs	Yasmine Rs.	Faria Rs.	Annie Rs. Cr.
To Revaluation A/c (Loss)	704	448	128		By Balance b/d	5100	3000	5000	--
To Furniture A/c	800	800	800		By Reserve A/c	495	315	90	--
To Drawings A/c	2750	1750	500		By Cash A/c	--	--	--	4500
To Balance c/d	2258	900	3829	4500	By Premium A/c	917	583	167	--

6512	**3898**	**5257**	**4500**	**6512**	**3898**	**5257**	**4500**

BALANCE SHEET

as at 31.12.2001

Liabilities		Rs.	Assets		Rs.
Sundry Creditors		800	Cash in Hand		2757
Public Deposits		1000	Factory Buildings		7350
Capitals :			Machinery		2000
Dinesh	2258		Furniture		200
Yashmine	900		Stock		1450
Faria	3829		Debtors	1500	
Annie	4500	11487	Less : Provision	300	1200
Bills Discounted		1670			
		14957			14957

Q.2 X and Y are partners as they share profits in the proportion of 3:1 their balance sheet as at 31.03.07 as follows.

BALANCE SHEET

Liabilities	Rs.	Assets	Rs.
Capital Account		Land	1,65,000
X	1,76,000	Furniture	24,500
Y	1,45,200	Stock	1,32,000
Creditors	91,300	Debtors	35,200
		Bills Receivable	28,600
		Cash	27,500
	4,12,500		4,12,500

On the same date, Z is admitted into partnership for 1/5th share on the following terms

* Goodwill is to be valued at 3½ years purchase of average profits of last for year which was Rs. 20,000 Rs. 17,000 Rs. 9,000 (Loss) respectively.
* Stock is fund to be overvalued by Rs. 2,000 Furniture is reduced and Land to be appreciated by 10% each, a provision for Bad Debts @ 12% is to be created on Debtors and a Provision of Discount of Creditors @ 4% is to be created.
* A liability to the extent of Rs. 1,500 should be created for a claim against the firm for damages.

* An item of Rs. 1,000 included in Creditors is not likely to be claimed, and hence it should be written off.

Prepare Revaluation Account, Partners: Capital Accounts and Balance Sheet of the new firm if Z is to contribute proportionate capital and goodwill. The capital of partners is to be in profit sharing ratio by opening current Accounts.

Solution 2

BOOK OF X, Y AND Z

REVALUATION ACCOUNT

Dr.				Cr.
Particulars		Amount	Particulars	Amount
To Stock A/c		2000	By land A/c	16500
To furniture A/c		2420	By creditors A/c	1000
To Provision for bad debts A/c		4224	By provision of discount on creditors A/c	3612
To claim against damages A/c		1500		
To profit transferred to				
X's capital A/c	8266			
Y's	2742	10968		
		21112		**21112**

PARTNER'S CAPITAL ACCOUNT

Dr.							Cr
Particulars	X Rs.	Y Rs.	Z Rs.	Particulars	X Rs.	Y Rs.	Z Rs.
Y's Current A/c	-	64,900	-	By Balance b/d	1,76,000	1,45,200	-
To Balance	2,54,901	84,967	84,967	By revaluation Profit	8,226	2,742	-
				By premium a/c	5,775	1,925	-
				By Cash a/c	-	-	84,967
				By X's current	64,900	-	-
	2,54,901	**1,49,867**	**84,967**		**2,54,901**	**1,49,867**	**84,967**

BALANCE SHEET AS AT 31.3.07

Liabilities		Rs.	Assets		Rs.
Claim against damages		1,500	Cash		1,20,167
Creditors	Rs. 91,300		Land		1,81,500
Less	Rs. 1,000		Furniture		21,780
	90,300		Stock		1,30,000
Less Prov.	3,612	86,688	Debtors	35,200	

Capital			Less provision.	4,224	30,976
X	Rs. 2,54,901		Bills receivables		28,600
Y	Rs. 84,967		X's current a/c		64,900
Z	Rs. 84,967	4,24,835			
Current A/c (Y)		64,900			
		5,77,923			**5,77,923**

Q.3. Rashmi and Pooja are partners in a firm. They share profits and losses in the ratio of 2:1. They admit Santosh into partnership firm on the condition that she will bring Rs. 30,000 for Goodwill and will bring such an amount that her capital will be 1/3 of the total capital of the new firm. Santosh will be given 1/3 share in future profits. At the time of admission of Santosh, the Balance Sheet of Rashmi and Pooja was as under:

Balance sheet

Liabilities	Rs.	Assets	Rs.
Capital Account		Cash	90,000
Rashmi	1,35,000	Machinery	1,20,000
Pooja	1,25,000	Furniture	10,000
Creditors	30,000	Stock	50,000
Bills Payable	10,000	Debtors	30,000
	3,00,000		3,00,000

It was decided to:

a. revalue stock at Rs. 45,000.

b. depreciated furniture by 10% and machinery by 5%.

c. make provision of Rs. 3,000 on sundry debtors for doubtful debts.

Prepare Revaluation Account, Partners: Capital Accounts and Balance Sheet of the new firm. Give full workings.

Solution : 3

REVALUATION ACCOUNTS

Dr. Cr.

Particulars	Rs.	Particulars	Rs.
To Stock	5000	By Loss on Revaluation distributed	
To Furniture	1000	Rashmi	10000
To Machinery	6000	Pooja	5000
To Debtors	3000		
	15000		**15000**

CAPITAL ACCOUNTS OF PARTNERS

Particulars	Rashmi	Pooja	Santosh	Particulars	Rashmi	Pooja	Santosh
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
To Revaluation A/c	10000	5000	--	By Balance b/d	115000	115000	--
To Adv Susp. A/c	2000	1000	--	By Cash A/c	--	--	--
To Balance C/d	145000	130000	--	By Premium a/c	20000	10000	--
				By Reserve	16000	8000	--
				By Work com.Res.	6000	3000	-
	157000	136000	--		157000	136000	--
To Balance c/d	145000	130000	137500	To Balance c/d	145000	130000	-
				By Cash A/c	--	--	137500
				½ of (Rs. 145000 + Rs. 130000)	--	--	137500
	145000	**130000**	**137500**		**145000**	**130000**	**137500**

BALANCE SHEET OF A, B & C AS AT

Dr. Cr.

Liabilities	Rs.	Assets		Rs.
Creditors	30000	Cash		257500
Bills Payable	10000	Machinery		114000
Rashmi's Capital	145000	Furniture		9000
Pooja's capital	130000	Stock		45000
Santosh's capital	137500	Debtors	30000	
		Less : Provision	3000	
	452500			**452500**

Q.4 A, B and C are equal partners in a firm, their Balance Sheet as on 31st March 2002 was as follows:

Liabilities	Rs.	Assets	Rs.

Sundry Creditors	27,000	Goodwill	1,17,000
Employees Provident Fund	6,000	Building	1,25,000
Bills Payable	45,000	Machinery	72,000
General Reserve	18,000	Furniture	24,000
Capitals:		Stock	1,14,000
A	2,17,000	Bad Debts	1,02,000
B	1,66,000	Cash	12,000
C	90,000	Advertisement Suspense A/c	3,000
	5,69,000		5,69,000

On that date they agree to take D as equal partner on the following terms:

a. D should bring in Rs. 1, 60,000 as his capital and goodwill. His share of goodwill is valued at Rs. 60,000.

b. Goodwill appearing in the books must be written off.

c. Provision for loss on stock and provision for doubtful debts is to be made at 10% and 5% respectively.

d. The value of building is to taken Rs. 2,00,000.

e. The total capital of the new firm has been fixed has been fixed at Rs. 4,00,000 and the partners capital accounts are to be adjusted in the profit sharing ratio. Any excess is to be transferred to current account and any deficit is to be brought in cash.

Required : Revaluation Account, Partners Capital Accounts, and the Balance Sheet of the new firm.

Solution 4

REVALUATION ACCOUNT

Dr.			Cr.
Particulars	Rs.	Particulars	Rs.
To Stock	11400	By land & building	75000
To provision for doubtful debtors	5100		
A's Capital A/c (1/3)	19500		
B's Capital A/c (1/3)	19500		
C's Capital A/c (1/3)	19500		
	75000		**75000**

CAPITAL ACCOUNTS OF PARTNERS

Particulars	Rashmi Rs.	Pooja Rs.	Santosh Rs.	Particulars	Rashmi Rs.	Pooja Rs.	Santosh Rs.
To Adver. Sus. A/c	1000	1000	1000	By Balance c/d	217000	166000	90000
to goodwill	39000	39000	39000	By Revaluation	19500	19500	19500
To Current A/c	122500	71500	--	By General Res.	6000	6000	6000
To Balance c/d	100000	100000	100000	By Premium A/c	20000	20000	20000
				By Current A/c	--	--	4500
	262500	**211500**	**140000**		**262500**	**211500**	**140000**

BALANCE SHEET OF M/S A, B & C as at 31st march 20x2

Dr. Cr.

Liabilities	Rs.	Assets		Rs
Sundry creditors	27000	Cash at bank		172000
Employees' Provident Fund	6000	Debtors	102000	
Bills Payable	45000	Less : Provision	5100	96900
A's Capital	100000	Mr. X		--
B's Capital	100000	Stock		102600
C's Capital	100000	Furniture & Fixtures		24000
D's Capital	100000	Plant & Machinery		72000
A's Current A/c	122500	Land & Building		200000
B's Current A/c	71500	C's Current A/c		4500
	672000			**672000**

Q.5 A, Band C were partners in a firm sharing profits equally: Their Balance Sheet on.31.12.2007 stood as:

BALANCE SHEET AS AT 31.12.07

Liabilities		Rs.	Assets		Rs.
A	Rs. 30,000		Goodwill		18,000
B	Rs. 30,000		Cash		38,000
C	Rs. 25,000	85,000	Debtors	. 43,000	

Bills payable	20,000	Less: Bad Debt provision	3,000	40,000
Creditors	18,000	Bills Receivable		25,000
Workers Compensation Fund	8,000	Land and Building		60,000
Employees provide4nt Fund	60,000	Plant and Machinery		40,000
General Reserve	30,000			
	2,21,000			**2,21,000**

It was mutually agreed that C will retire from partnership and for this purpose following terms were agreed upon.

i) Goodwill to be valued on 3 years' purchase of average profit of last 4 years which were 2004 : Rs.50,000 (loss); 2005 : Rs. 21,000; 2006: Rs.52,000; 2007 : Rs.22,000.

ii) The Provision for Doubtful Debt was raised to Rs. 4,000.

iii) To appreciate Land by 15%.

iv) To decrease Plant and Machinery by 10%.

v) Create provision of Rs;600 on Creditors.

vi) A sum of Rs.5,000 of Bills Payable was not likely to be claimed.

vii) The continuing partners decided to show the firm's capital at 1,00,000 which would be in their new profit sharing ratio which is 2:3. Adjustments to be made in cash

Make necessary accounts and prepare the Balance Sheet of the new partners.

Ans.5 REVALUATION ACCOUNT

Particulars		Rs.	Particulars	Rs.
To Provision for Debts A/c		1,000	By Land A/c	9,000
To Plant & Machinery A/c		4,000	By Provision on Creditors A/c	600
To Profit transferred to			By Bills Payable A/c	5,000
A's Capital A/c	Rs. 3,200			
B's Capital A/c	Rs. 3,200			
C's Capital A/c	Rs. 3,200	9,600		

	14,600		14,600

PARTNER'S CAPITAL ACCOUNTS

Particulars	ARs.	B Rs.	C Rs.	Particulars	A Rs.	B Rs.	C Rs.
To Goodwill A/c	6,000	6,000	6,000	By Balance b/d	30,000	30,000	25,000
To C's Capital A/c	2,250	9,000	-	By General Reserve	10,000	10,000	10,000
To C's Loan A/c	-	-	46,116	By Worksmen A/c Compensation Fund	2,667	2,667	2,666
To Balance c/d	40,000	60,000	-	By Revalu A/c (profit)	3,200	3,200	3,200
				By A's Capital A/c	-	-	2,250
				By B's Capital A/c	-	-	9,000
				By Cash A/c (Deficiency)	2,383	29,133	-
	48,250	**75,000**	**52,116**		**48,250**	**75,000**	**52,116**
				By Balance b/d	40,000	60,000	-

BALANCE SHEET

as at 31.12.07

Liabilities		Rs.	Assets		Rs.
Bills Payable		15,000	Debtors	Rs. 43,000	
Creditors		17,400	Less: Provision	Rs. 4,000	39,000
Employees Provident Fund		60,000	Bills Receivables		25,000
C's Loan		46,116	Land & Buildings		69,000
A's Capital	40000		Plant & Machinery		36,000
B'S Capital	60000	1,00,000	Cash		69,516
		2,38,516			2,38,516

Retirement of a Partner

LEARNING OBJECTIVES:

After studying this lesson, we are confident; you should be competent enough to:

- Identify adjustments arising due to retirement of a partner.
- Calculate new and gaining ratio.
- Make accounting treatment of goodwill in different cases.
- Make accounting treatment of the revaluation of assets and liabilities and distribution of profit or loss on revaluation among partners.
- Make accounting treatment of undistributed profit or loss.
- Determine the amount payable to retiring partner and make payment as per agreement and provisions of law.
- Make adjustment of partners' capital account

Salient Points:-

1. An existing partner may wish to withdraw from a firm for various reasons.
2. The amount due to a retiring partner will be the total of :-
   a. his capital in the firm
   b. His share in firm's accumulated profits and losses.
   c. His share of profit or loss on revaluation of assets and liabilities
   d. ;his share of profits till the date of retirement
   e. His remuneration and interest on capital.
   f. His share in firm's goodwill.
3. The ratio in which the continuing (remaining) partners have acquired the share from the outgoing partner is called gaining ratio.
4. Share of goodwill of outgoing partner will be debited to gaining partners in their gaining ratio.
5. At the retirement of a partner Profit & Loss on Revaluation of Assets and liabilities and balances of accumulated Profits and losses will be distributed among all partners (including outgoing partner) in their old ratio.
6. The outstanding balance of outgoing partner's capital A/C may be settled by fully or partly payment and (or) transferring into his loan account.

Q.1 What is meant by retirement of a partner?

Ans. Retirement of a partner is one of the modes of reconstituting the firm in which old partnership comes to an end and a new partner among the continuing (remaining) partners (i.e., partners other than the outgoing partner) comes into existence.

Q.2 'How can a partner retire from the firm?

Ans. A partner may retire from the firm;

i) In accordance with the terms of agreement; or

ii) With the consent of all other partners; or

iii) Where the partnership is at will, by giving a notice in writing to all the partners of his intention to retire.

Q.3 What do you understand by 'Gaining Ratio?

Ans. Gaining Ratio means the ratio by which the share in profit stands increased. It is computed by deducting old ratio from the new ratio.

Q.4 What do you understand by 'Gaining Partner'?

Ans Gaining Partner is a partner whose share in profit stands increased as a result of change in partnership.

Q.5 Give two circumstances in which gaining ratio is computed.

Ans. Gaining Ratio is computed in the following circumstances: (i) When a partner retires or dies. (ii) When there is a change in profit-sharing ratio.

Q.6 Why is it necessary to revalue assets and reassess liabilities at the time of retirement of a partner?

Ans. At the time of retirement or death of a partner, assets are revalued and liabilities are reassessed so that the profit or loss arising on account of such revaluation up to the date of retirement or death of a partner may be ascertained and adjusted in all partners' capital accounts in their old profit-sharing ratio.

Q.7 Why is it necessary to distribute Reserves Accumulated, Profits and Losses at the time of retirement or death of a partner?

Ans. Reserves, accumulated profits and losses existing in the books of account as on the date of retirement or death are transferred to the Capital Accounts (or Current Accounts) of all the partners (including outgoing or deceased partner) in their old profit-sharing ratio so that the due share of an outgoing partner in reserves, accumulated profits/losses gets adjusted in his Capital or Current Account.

Q.8 What are the adjustments required on the retirement or death of a partner?

Ans. At the time of the retirement or death of a partner, adjustments are made for the following:

(i) Adjustment in regard to goodwill.

(ii) Adjustment in regard to revaluation of assets and reassessment of liabilities.

(iii) Adjustment in regard to undistributed profits.

(iv) Adjustment in regard to the Joint Life Policy and individual policies.

Q.9 X wants to retire from the firm. The profit on revaluation of assets on the date of retirement is Rs. 10,000. X is of the view that it be distributed among all the partners in their profit-sharing ratio whereas Y and Z are of the view that this profit be divided between Y and Z in new profit-sharing ratio. Who is correct in this case?

Ans. X is correct because according to the Partnership Act a retiring partner is entitled to share the profit up to the date of his retirement. Since the profit on revaluation arises before a partner retires, he is entitled to the profit.

Q.10 How is goodwill adjusted in the books of a firm -when a partner retires from partnership?

Ans. When a partner retires (or dies), his share of profit is taken over by the remaining partners. The remaining partners then compensate the retiring or deceased partner in the form of goodwill in their gaining ratio. The following entry is recorded for this purpose:

Remaining Partners' Capital A/cs ...Dr.
[Gaining Ratio]

To Retiring/Deceased Partner's Capital A/c [With his share of goodwill]

If goodwill (or Premium) account already appears in the old Balance Sheet, it should be written off by recording the following entry:

All Partners' Capital/Current A/cs ...Dr. [Old Ratio]

To Goodwill (or Premium) A/c

Q.11 X, Y and Z are partners sharing profits and losses in the ratio of 3 : 2 :1. Z retires and the following Journal entry is passed in respect of Goodwill:

Y's Capital A/c ...Dr.	20,000	
To X's Capital A/c		10,000
To Z's Capital A/c		10,000

Q.21 The value of goodwill is Rs. 60,000. What is the new profit-sharing ratio between X and Y?

Ans. Without calculating the gaining ratio, the amount to be adjusted in respect of goodwill can be calculated directly with the help of following statement:

STATEMENT SHOWING THE REQUIRED ADJUSTMENT FOR GOODWILL

Particulars	X(Rs.)	V(Rs.)	Z(Rs.)
Right of goodwill before retirement (3:2:1)	30,000	20,000	10,000
(Old Ratio) Right of goodwill after retirement	20,000	40,000	—
(Balancing Figure) (New Ratio)			
Net Adjustment	(-) 10,000	(+) 20,000	(-) 10,000

The new ratio between X and Y is 1 : 2.

Q.13 State the ratio in which profit or loss on revaluation will be shared by the partners when a partner retires. ;

Ans. Profit or loss on revaluation of assets/liabilities will be shared by the partners (including the retiring partner) hi their old profit-sharing ratio.

Q.14 How is the account of retiring partner settled?

Ans. The retiring partner account is settled either by making payment in cash or by promising the retiring partner to pay in installments along with interest or by making payment partly in call and partly transferring to his loan account. The -following Journal entry is passed:

Retiring Partner's Capital A/c ...Dr.

To Cash* [If paid in cash] Or

To Retiring Partner's Loan [If transferred to loan]

6 to 8 marks questions

Q.1 The Balance Sheet of A, B and C on 31st December 2007 was as under :

BALANCE SHEET
as at 31.12.2007

Liabilities	Amount	Assets	Amount
A's Capital	400,00	Buildings	20,000
B's Capital	30,000	Motor Car	18,000
C's Capital	20,000	Stock	20,000
General Reserve	17,000	Investments	1,20,000
Sundry Creditors	1,23,000	Debtors	40,000
		Patents	12,000
	2,30,000		**2,30,000**

The partners share profits in the ratio of 8 : 4 : 5. C retires from the firm on the same date subject to the following term S and conditions:

i) 20% of the General Reserve is to remain' as a reserve for bad and doubtful debts. ;

ii) Motor)r Car is to be decreased by 5%.

iii) Stock is to be revalued at Rs.17, 500.

iv) Goodwill is valued at' 2 ½ years purchase of the average profits of last 3 years.

Profits were; 2001: Rs.11,000; 200l: Rs. 16,000 and 2003: Rs.24,000.

C. was paid in July A and B borrowed the necessary amount from the Bank on the security of Motor Car and stock to payoff C.

Prepare Revaluation Account, Capital Accounts and Balance Sheet of A and B.

Ans.2 SOLUTION

REVALUATION ACCOUNT

Particulars	Rs.	Particulars	Rs.
To Motor Cars A/C	900	By Loss transferred to	
To Stock A/C	2,500	A's Capital A/c Rs.	1,600
		B's Capital A/c Rs.	800
		C's Capital A/c Rs.	1,000
	3,400		**3,400**

PARTNERS CAPITAL ACCOUNT

Particulars	ARs.	B Rs.	C Rs.	Particulars	A Rs.	B Rs.	C Rs.
To C's Capital A/c	8,334	4,166	-	By Balance b/d	40,000	30,000	20,000
To Revaluation A/c (Loss)	1,600	800	1,000	By General Reserve A/c	6,400	3,200	4,000
To Bank A/c	-	-	35,500	By A's Capital A/c	-	-	8,334
Balance c/d	36,466	28,234	-	By B's Capital A/c	-	-	4,166
	46,400	**33,200**	**36,500**		**46,400**	**33,200**	**36,500**
				By Balance b/d	**36,466**	**28,234**	**-**

BALANCE SHEET OF A AND B

Liabilities	Rs.	Assets	Rs.
Sundry creditors	1,23,000	Building	20,000
Bank Loan	35,500	Motor Card	17,100

Capital A	36,466		Stock	17,500
B	28,234	64,700	Investment	1,20,000
			Debtors	36,600
			Patents	12,000
		2,23,200		**2,23,200**

Q.3 A, Band C were partners in a firm sharing profits equally: Their Balance Sheet on.31.12.2007 stood as:

BALANCE SHEET AS AT 31.12.07

Liabilities		Rs.	Assets		Rs.
A	Rs. 30,000		Goodwill		18,000
B	Rs. 30,000		Cash		38,000
C	Rs. 25,000	85,000	Debtors	. 43,000	
Bills payable		20,000	Less: Bad Debt provision	3,000	40,000
Creditors		18,000	Bills Receivable		25,000
Workers Compensation Fund		8,000	Land and Building		60,000
Employees provide4nt Fund		60,000	Plant and Machinery		40,000
General Reserve		30,000			
		2,21,000			**2,21,000**

It was mutually agreed that C will retire from partnership and for this purpose following terms were agreed upon.

i) Goodwill to be valued on 3 years' purchase of average profit of last 4 years which were 2004 : Rs.50,000 (loss); 2005 : Rs. 21,000; 2006: Rs.52,000; 2007 : Rs.22,000.

ii) The Provision for Doubtful Debt was raised to Rs. 4,000.

iii) To appreciate Land by 15%.

iv) To decrease Plant and Machinery by 10%.

v) Create provision of Rs;600 on Creditors.

vi) A sum of Rs.5,000 of Bills Payable was not likely to be claimed.

vii) The continuing partners decided to show the firm's capital at 1,00,000 which would be in their new profit sharing ratio which is 2:3. Adjustments to be made in cash

Make necessary accounts and prepare the Balance Sheet of the new partners.

Ans.3 REVALUATION ACCOUNT

Particulars		Rs.	Particulars	Rs.
To Provision for Debts A/c		1,000	By Land A/c	9,000
To Plant & Machinery A/c		4,000	By Provision on Creditors A/c	600
To Profit transferred to			By Bills Payable A/c	5,000
A's Capital A/c	Rs. 3,200			
B's Capital A/c	Rs. 3,200			
C's Capital A/c	Rs. 3,200	9,600		
		14,600		**14,600**

PARTNER'S CAPITAL ACCOUNTS

Particulars	A Rs.	B Rs.	C Rs.	Particulars	A Rs.	B Rs.	C Rs.
To Goodwill A/c	6,000	6,000	6,000	By Balance b/d	30,000	30,000	25,000
To C's Capital A/c	2,250	9,000	-	By General Reserve	10,000	10,000	10,000
To C's Loan A/c	-	-	46,116	By Workmen A/c Compensation Fund	2,667	2,667	2,666
To Balance c/d	40,000	60,000	-	By Revalu A/c (profit)	3,200	3,200	3,200
				By A's Capital A/c	-	-	2,250
				By B's Capital A/c	-	-	9,000
				By Cash A/c (Deficiency)	2,383	29,133	-

	48,250	**75,000**	**52,116**		**48,250**	**75,000**	**52,116**
				By Balance b/d	**40,000**	**60,000**	**-**

BALANCE SHEET

as at 31.12.07

Liabilities		Rs.	Assets		Rs.
Bills Payable		15,000	Debtors	Rs. 43,000	
Creditors		17,400	Less: Provision	Rs. 4,000	39,000
Employees Provident Fund		60,000	Bills Receivables		25,000
C's Loan		46,116	Land & Buildings		69,000
A's Capital	40000		Plant & Machinery		36,000
B'S Capital	60000	1,00,000	Cash		69,516
		2,38,516			**2,38,516**

DEATH OF A PARTNER

Learning Objectives:

After studying this Unit, students will be able to understand and prepare:

a) Deceased partners capital account
b) Deceased partners Executor account
c) Executors loan account
d) Calculation of share of profit and Goodwill of the deceased partner.

SALIENT POINTS:

- Gaining Ratio: When the partner retires or dies, his share of profit is taken over by the remaining partners.
- Gaining ratio is applied for the purpose of calculating Goodwill to be paid off to the deceased partner.
- The deceased partner s share of profit till the date of death will be calculated by preparing Profit and Loss Suspense account on the date of Death.

SHORT QUESTIONS--- (3-4 MKS)

1. A, B and C are partners sharing profits and losses in the ratio of 5:4:1. The profit for the year ending 31, March, 2010 was Rs 1, 00,000. B died on 30th June 2010. Calculate C's share of profit till the date of death and pass necessary journal entry.

Profit and Loss suspense a/c – Dr B's Capital Account	10,000	 10,000
(Being B's share of profit transferred to his		

capital account)		

C's share of profit = 1, 00,000 X 4/10 X 3/12 = 10,000

2. X, Y and Z are partners in a firm sharing profits and losses in the ratio of 5:4:1.The Partnership agreement provides that the share of profit of the deceased partner will be worked out on the basis of sales. The sales for the year 2009-10 was Rs 8,00,000 and the sales from April 1, 2010 to June 30, 2010 was Rs 1,50,000. The profit for the year ended 31st March 2010 amounted to Rs 1,00,000. Y died on 30th June 2010. Calculate his share of profit and pass necessary journal entry.

Profit and Loss suspense a/c – Dr Y's Capital Account	7500	 7500
(Being Y's share of profit transferred to his capital account		

Sales for the year 2009-10 ----8, 00,000 Profit for the year 2009-10 -----1,00,000
Sales from April 1,2010 to 30th June 2010 -----1,50,000 Profit upto 30th June 2010----?
C's share of profit = 1,00,000/8,00,000 X 1,50,000 = 18750 X 4/10 = 7500.

3. Ram, Mohan and Sohan were partners sharing profits and losses in the ratio of 5:3:2. On 31st March, 2006 their Balance Sheet was as under:

Liabilities	Rs	Assets	Rs
Capitals		Leasehold	1,25,000
Ram	1,50,000	Patents	30,000
Mohan	1,25,000	Machinery	1,50,000
Sohan	75,000	Stock	1,90,000
Workmen's Compensation Reserve	30,000	Cash at Bank	40,000
Creditors	1,55,000		
	5,35,000		5,35,000

Sohan died on 1st August, 2006. It was agreed that :
(i) Goodwill of the firm is to be valued at Rs. 1,75,000.
(ii) Machinery be valued at Rs. 1,40,000; Patents at Rs. 40,000; Leasehold at Rs. 1,50,000 on this date.
(iii) For the purpose of calculating Sohan's share in the profits of 2006-07, the profits should be taken to have accrued on the same scale as in 2005-06, which were Rs. 75,000.
Prepare Sohan's Capital Account and Revaluation Account. (6)

Revaluation Account

Particulars	Amt	Particulars	Amt
Machinery	10,000	Leasehold	25000
Capital Accounts		Patents	10,000
Ram	12500		
Mohan	7500		

Sohan	5000		
	35000		35000

Sohan's capital Account

Particulars	Rs	Particulars	Rs
		Balance b/d	75000
Sohan's Executor's account	1,26,000	Revaluation a/c	5000
		Ram's Capital a/c	21875
		Mohan's capital a/c	13125
		P & L Suspense A/c	13125
		Workmen's Compensation reserve a/c	6000
	1,26,000		1,26,000

Working Note :

a)Total Goodwill of the firm = 1,75,000

Sohan's share of goodwill = 1,75,000 X 2/10 = 35000 (to be divided in the ratio of 5:3 i.e gaining ratio)

b) Sohan's share of profit = 75000 X 4/12 x 2/10 = Rs 5000

4. Following is the Balance sheet of P , Q and R as on 31st December 2010 sharing profits in the ratio of 5:3:2.

Particulars	Rs	Particulars	Rs
Capital Accounts		Cash	13000
P	30000	Debtors	8000
Q	25000	Machinery	30000
R	15000	Stock	10000
Creditors	7000	Patents	6000
Reserve Fund	10000	Building	20000
	87000		87000

P died on 1st July 2011 on the following terms-

i) Patents are to be valued at Rs 8000, Machinery at Rs 28000 and Building at Rs 30,000.

ii) Interest on Capital is to be provided at 10% p.a.

iii) Goodwill of the firm is valued at 2 years purchase of the average profits of the last five years which were-

2006 - Rs 15,000 2007 – Rs 13000 2008 – Rs 12,000
2009—15,000 and 2010--- Rs 20,000

iv) Profit for the year 2011 has been accrued on the same scale as in 2010.

v) P's Executor is to be paid Rs 11,500 and balance transferred to his loan account.

Prepare Revaluation Account, P's Capital account and P's executors account. Also pass necessary journal entries.

Revaluation Account

Particulars	Rs	Particulars	Rs
Machinery	2000	Patents	2000
Capital Accounts-		Buildings	10000
P	5000		
Q	3000		
R	2000		
	12000		12000

P's Capital Account

Particulars	Rs	Particulars	Rs
P's Executors a/c	61500	Balance b/d	30000
		Reserve fund	5000
		Q's Capital a/c	9000
		R's Capital a/c	6000
		Revaluation a/c	5000
		Interest on capital	1500
	61500		61500

P's Executor's account

Particulars	Rs	Particulars	Rs
Bank/cash a/c	11500	P's Capital a/c	61500
P's Executor's Loan a/c	50000		
	61500		61500

Working Note :

a) Interest on Capital : 30,000 X 10/100 X 6/12 = Rs 1500

b) Reserve fund = 10,000 X 5/10 = Rs 5000

c) P's Share of profits = 20,000 X 5/10 X 6/12 = Rs 5000.(for 6 months)

d) Total Goodwill of the firm =
Average profits = 75000/5 = Rs 15000
Goodwill = 15000 X 2 = 30,000
P's share of Goodwill = 30,000 X 5/10 = 15000(to be divided in Gaining ratio 3:2)

Journal

SN	Particulars	LF	Amt	Amt
1	Revaluation a/c ----Dr Machinery a/c (Being machinery revalued)		2000	 2000
2	Patents a/c --Dr Building a/c - Dr Revaluation a/c (Being Assets revalued)		2000 10000	 12000
3	Revaluation a/c --- Dr P's Capital a/c Q's Capital a/c		10000	 5000 3000

	R's Capital a/c (Being Revaluation profit distributed)			2000
4	Reserve fund a/c –Dr P's Capital a/c (Being reserve distributed)		5000	 5000
5	Q's Capital a/c ---Dr R's Capital a/c ---Dr P's capital a/c (Being deceased partner 's account credited by his share of goodwill contributed by the gaining partners)		9000 6000	 15000
6	Interest on capital a/c – Dr P's Capital a/c (Being Interest on capital provided to the deceased partner)		1500	 1500
7	P's Capital a/c ---Dr P's executor's a/c (Being P's balance due transferred to his executor's a/c)		61500	 61500
8	P's executor's a/c --Dr Cash a/c P's executor's loan a/c (Being amount paid to the executor and balance transferred to his loan account)		61500	 11500 50000

5. X, Y and Z are partners sharing profits and losses in the ratio of 2:2:1 respectively. Their Balance Sheet as on 31st march 2007 was as follows—

Balance Sheet as on 31/03/10

Liabilities	Rs	Assets	Rs
Sundry Creditors	1,00,000	Cash at bank	20,000
Capital Accounts		Stock	30,000
X	60,000	Sundry Debtors	80,000
Y	1,00,000	Investments	70,000
Z	40,000	Furniture	35,000
General Reserve	50,000	Buildings	1,15,000
	3,50,000		3,50,000

Z died on 30th September 2007 and the following was provided—

a) "Z" will be entitled to his share of profit upto the date of death based on last year's profit.
b) Z's share of Goodwill will be calculated on the basis of 3 years purchase of average profits of last four years . The profits of the last four years was as follows—
   Year I – 80,000, Year II –Rs 50,000 Year III – Rs 40,000 and Year IV –Rs 30,000
c) Interest on Capital was provided at 12% p.a.
d) Drawings of the deceased partner upto the date of death was Rs 10,000.
e) Rs 15,400 should be paid immediately to the executor of the deceased partner and the balance in four equal yearly instalments with interest at 12% on remaining balance.
   Prepare Z's capital account and Z's executors account till the account is finally closed.

Z's Capital Account

Particulars	Rs	Particulars	Rs
Drawings	10,000	Balance b/d	40,000
Z's Executor's a/c	75,400	General Reserve	10,000
		Profit &Loss Suspense a/c	3,000
		Interest on capital	2400
		X's Capital a/c	15,000
		Y's capital a/c	15,000
	85400		85400

Z's Executor's Account

Date	Particulars	Rs	Date	Particulars	Rs.
30/09/07	Bank a/c	15400	30/09/07	Z's Capital a/c	75400
31/03/08	Balance c/d	63600	31/03/08	Interest on Loan (on Rs 60,000@12% for 6 months)	3600
		79000			79000
30/09/08	Bank a/c (15000+ 7200)	22,200	1/04/08	Balance b/d	63600
31/03/09	Balance c/d	47,700	30/09/08	Interest on Loan(On Rs 60,000 @ 12% for 6 months)	3600
			31/03/09	Interest on Loan(on Rs 45000 @12% for 6 months)	2700
		69900			69900
30/09/09	Bank a/c (15000+5400)	20,400	1/04/09	Balance b/d	47,700
31/03/10	Balance c/d	31800	30/09/09	Interest on loan(on Rs 45000 @ 12% for 6 months)	2700
			31/03/10	Interest on loan (on Rs 30,000@12% for 6 months)	1800
		52200			52200
30/09/10	Bank a/c(15000 + 3600)	18600	1/4/10	Balance b/d	31800
31/03/11	Balance c/d	15900	30/09/10	Interest on loan(on Rs 30,000 @12% for 6 months)	1800
			31/03/11	Interest on Loan(on Rs 15000 @12% for 6 months)	900
		34500			34500
30/09/11	Bank a/c (15000+1800)	16800	1/04/11	Balance b/d	15900
			30/09/11	Interest on loan(on Rs 15000 @12% for 6 months)	900
		16800			16800

6 Anil, Jatin and Ramesh were sharing profit in the ratio of 2:1:1. Their Balance Sheet as at 31.12.2001 stood as follows:-

Liabilities	**Rs**	**Assets**	**Rs**
Creditors	24,400	Cash	**1,00,000**
Bank Loan	10,000	Debtors 20000 Less : Provision 1600	18,400
Profit and Loss A/c	18,000	Stock	10,000
Bills Payable	2,000	Building	20,000
Anil's Capital	50,000	Investment	14,000
Jatin's Capital	40,000	Goodwill	22,000
Ramesh's Capital	40,000		
	1,84,400		1,84,400

Ramesh died on 31st March 2002. The following adjustments were agreed upon-

(a) Building be appreciated by Rs. 2,000

(b) Investments be valued at 10% less than the book value.

(c) All debtors (except 20% which are considered as doubtful) were good.

(d) Stock be increased by 10 %

(e) Goodwill be valued at 2 years' purchase of the average profit of the past five years.

(f) Ramesh's share of profit to the death be calculated on the basis of the profit of the preceding year. profit for the years 1997, 1998, 1999 and 2000 were Rs. 26,000, Rs. 22,000, Rs. 20,000 and Rs. 24,000 respectively.

Prepare revaluation account, partner's capital Account, Ramesh 's Executors' Account and Balance sheet immediately after Ramesh's death assuming that Rs. 18, 425 be paid immediately to his executors and balance to b left to the Ramesh's Executor's Account

Revaluation Account

Particulars	**Rs**	Particulars	**Rs**
Investment A/c	1,400	Building A/c	2,000
Provision for doubtful debt A/c	2,400	Stock A/c	1,000
		Loss transferred to	
		Anil's Capital A/c	400
		Jatin's Capital A/c	200
		Ramesh's Capital A/c	200
	3800		3800

Partners Capital Accounts

Particulars	**Anil**	**Jatin**	**Ramesh**	**Particulars**	**Anil**	**Jatin**	**Ramesh**
Goodwill A/c	11000	5500	5500	By Balance b/d	50000	40000	40000
Ramesh Capital A/c	7333	3667		Profit and Loss A/c	9000	4500	4500
Revaluation A/c (Loss)	400	200	200	Profit &Loss Susp A/c			1125
Ramesh's Executor's A/c			50925	Anil's Capital A/c			7333
Balance c/d	40,267	35,133	----	Jatin's Capital A/c			3667
	59,000	41,500	56,625		59,000	41,500	56,625

Ramesh's Executor's account

Particulars	**Rs**	**Particulars**	**Rs**
Cash Account	18425	Ramesh's Capital account	50925
Balance c/d	32500		
	50925		50925

Balance sheet

Liabilities	Rs	Assets	Rs
Bank Loan	10, 000	Cash	81,575
Creditors	20,400	Debtors 20000 Less Provision 4000	16000
Bills Payable	2,000	Stock	11000
Ramesh's Executor's Loan	32,500	Building	22000
Anil's Capital	40,267	Investments	12600
Jatin's Capital	35,133	Profit &Loss Suspense A/c	1125
	1,44,300		1,44,300

DISSOLUTION OF PARTNERSHIP FIRM

Learning Objectives

After Studying this unit, the students will be able to understand:

*Meaning of Dissolution

* Distinction between Dissolution of Partnership and Dissolution of Partnership firm.

* Preparation of Realisation Account

* Procedure of settlement of accounts

* Preparation of Memorandum Balance sheet (to find out missing figures)

* Necessary journal entries to close the books of the firm.

SALIENT POINTS:

- Dissolution : Dissolution of the firm is different from Dissolution of Partnership.
- Realisation account : It is prepared to realize the various assets and pay off the liabilities.
- Closure of the Books of Accounts : When the firm is dissolved, finally all the books of accounts are closed through Bank Account.

1. Distinguish between Dissolution of Partnership and Dissolution of Partnership firm

Dissolution of Partnership	Dissolution of partnership firm
a)The Partnership is dissolved but the business continues. The Business is not terminated	a)The firm winds up the business.
b) Assets and liabilities are revalued through revaluation account and the Balance sheet is prepared	b)Assets are sold and the liabilities are paid off through Realisation account.
c) The Books of accounts are not closed as the business is not terminated.	d) The Books of accounts are closed.

2.State the provisions of Section 48 of the Partnership Act 1932 regarding settlement of Accounts during the Dissolution of Partnership firm.

Ans. According to section 48—

a) Losses including the deficiencies of Capitals are to be paid---
   i) First out of profits
   ii) Next out of Capitals of the partners
   iii) Lastly if required, by the partners individually in their profit sharing ratio(as their liability is unlimited)

b) The Assets of the firm and the amount contributed by the partners to make up the deficiency of capital shall be applied for –
   i) First to pay the debts of the firm to the third parties.
   ii) Next, Partners Loan(Partner has advanced to the firm)
   iii) Partners capitals
   iv) The residue, if any shall be distributed among the partners in their profit sharing ratio.

3. Distinguish between Realisation account and Revaluation account

Realisation Account	Revaluation Account
a) It is prepared in the case of Dissolution of Partnership firm.	a)It is prepared in the case of Dissolution of Partnership.
b) This account is prepared to realise the assets & pay off the liabilities .	b) This Account is prepared to revalue the assets and liabilities during Admission, Retirement and Death of the partner.

4. A and B are partners sharing profits and losses equally. They decided to dissolve their firm. Assets and Liabilities have been transferred to Realisation Account. Pass necessary Journal entries for the following.

a) A was to bear all the expenses of Realisation for which he was given a commission of Rs 4000.
b) Advertisement suspense account appeared on the asset side of the Balance sheet amounting Rs 28000
c) Creditors of Rs 40,000 agreed to take over the stock of Rs 30,000 at a discount of 10% and the balance in cash.
d) B agreed to take over Investments of Rs 5000 at Rs 4900
e) Loan of Rs 15000 advanced by A to the firm was paid off.
f) Bank loan of Rs 12000 was paid off.

JOURNAL

SN	Particulars	LF	Debit(Rs)	Credit(Rs)
a)	Realisation account –Dr A's Capital account (Being commission given to A)		4000	 4000
b)	A's Capital account –Dr B's Capital account –Dr Advertisement Suspense account (Being Advertisement suspense written off)		14000 14000	 28000
c)	Realisation account –Dr Cash account (Being creditors paid off)		13000	 13000
d)	B's Capital account –Dr Realisation account (Being asset taken over by the partner)		4900	 4900
e)	A's Loan account –Dr Cash account (Being partners loan paid off)		15000	 15000
f)	Realisation account -- Dr Cash account (Being Bank loan paid off)		12000	 12000

4.X and Y are partners in the firm who decided to dissolve the firm. Assets and Liabilities are transferred to Realisation account. Pass necessary journal entries—

a)Creditors were Rs 1,00,000. They accepted Building valued Rs 1,40,000 and paid cash to the firm Rs 40,000

b) Aman, an old customer whose account of Rs 1000 was written off as bad in the previous year paid 40% of the amount.

c)There were 300 shares of Rs 10 each in ABC Ltd which were acquired for Rs 2000 were now valued at Rs 6 each. These were taken over by the partners in the profit sharing ratio.

d) Profit on Realisation Rs 42000 was divided among the partners.

e) Land and Building (Book value Rs 1, 60,000) was sold for Rs 3,00,000 through a broker who charged 2% commission on the deal.

f) Plant and machinery (Book value Rs 60,000) was handed over to the creditor in full settlement of his claim.

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S.N	Particulars	LF	Debit(Rs)	Credit(Rs)
a)	Cash account –Dr Realisation account (Being cash received from the creditor)		40000	40000
b)	Cash a/c –Dr Realisation a/c (Being cash received from a debtor whose account was wriiten off earlier)		400	400
c)	X's Capital a/c –Dr Y's Capital a/c –Dr Realisation a/c (Being Investments taken over by the partners)		900 900	1800
d)	Realisation a/c –Dr X's Capital a/c Y's capital a/c (Being profit on Realisation distributed among the partners)		42000	21000 21000
e)	Cash a/c—Dr Realisation a/c (Being Land and Building realized)		294000	294000
f)	NO JOURNAL ENTRY			

LONG QUESTIONS—6-8 MKS

6) Following is the Balance sheet of Karan and Sandeep who share profits and losses equally as on 31st march 2010

Liabilities	Rs	Assets	Rs
Capitals--		Bank	40,000
Karan	1,00,000	Debtors	25,000
Sandeep	50,000	Stock	35,000
Creditors	30,000	Machinery	60,000
Workmen compensation fund	15,000	Furniture	40,000
Bank loan	5000		
	2,00,000		2,00,000

The firm was dissolved on the above date.

1. Karan agreed to take over 50% of the stock at 10% less on its book value, the remaining stock was sold at a gain of 15%. Furniture and machinery realized for Rs 30,000 and 50,000 respectively.
2. There was unrecorded Investments which was sold for Rs 25,000.
3. Debtors realized Rs 31,500 (with interest) and Rs 1200 was recovered for bad debts written off last year.
4. There was an outstanding bill for repairs which had to be paid Rs 2000.

Prepare necessary Ledger accounts to close the books of the firm.

Realisation account

Particulars	Rs	Particulars	Rs
Sundry assets Debtors-25000 Stock-35,000 Furniture-40,000 Machinery-60,000	1,60,000	Liabilities: Creditors : 30,000 Bank loan : 5000	35000
Bank a/c(outstanding repair bill)	2000	Karan's Capital a/c	15750
Bank(Creditors & Bank loan)	35,000	Bank a/c(stock)	20125
Capital accounts- Karan : 5787.5 Sandeep: 5787.5		Bank a/c(Assets realized)	80,000
	11575	Bank a/c(Debtors)	32700
		Bank a/c(Investments)	25,000
	208575		208575

Partners Capital accounts

Particulars	Karan	Sandeep	Particulars	Karan	Sandeep
Realisation a/c(stock)	15750		Balance b/d	1,00,000	50,000
			Workmen's compensation fund	7500	7500
Bank account	97537.5	63287.5	Realisation a/c	5787.5	5787.5
	113287.5	63287.5		113287.5	63287.5

Bank account

Particulars	Amount	Particulars	Amount
Balance b/d	40,000	Realisation a/c (repair bill, creditors and bank loan)	37000
Realisation a/c(stock)	20125	Karan's capital	97537.5
Realisation a/c(Machinery & furniture)	80,000	Sandeep's capital	63287.5
Realisation a/c(Debtors)	32700		
Bank(Investments)	25,000		
	197825		197825

5. Following is the Balance sheet of X and Y who share profits in the ratio of 4:1 as on 31st march 2010

Balance sheet

Liabilities	Rs	Assets	Rs
Sundry Creditors	8,000	Bank	20,000
Bank overdraft	6,000	Debtors 17,000 Less provision 2000	15,000
X's Brother's loan	8,000	Stock	15,000
Y's Loan	3,000	Investments	25,000
Investment Fluctuation fund	5,000	Building	25,000
Capitals- X-50,000 y-40,000	90,000	Goodwill	10,000
		Profit and Loss a/c	10,000
	1,20,000		1,20,000

The firm was dissolved on the above date and the following was decided—

a) X agreed to pay off his brother's loan

b) Debtors of Rs 5000 proved bad.

c) Other assets realized as follows—Investments 20% less, and Goodwill at 60%.

d) One of the creditors for Rs 5000 was paid only Rs 3000.

e) Building was auctioned for Rs 30,000 and the auctioneer's commission amounted to Rs 1000.

f) Y took over part of the stock at Rs 4000(being 20% less than the book value)Balance stock realized 50%

g) Realisation expenses amounted to Rs 2000.

Prepare Realisation account, Partners capital accounts and Bank account.

Realisation account

Particulars	Amt(Rs)	Particulars	Amt(Rs)
Sundry Assets Debtors 17,000 Stock 15,000 Investments 25,000 Building 25,000 Goodwill 10,000	92,000	Sundry Liabilities Creditors – 8000 Bank overdraft - 6000 X's Brothers loan- 8000 Investment Fluctuation fund – 5,000 Provision for doubtful debts - 2000	29000
X's Capital(Brothers loan)	8000	Bank a/c (Assets realized)	72,000
Bank(Liabilities paid off) Creditors- 6000 Bank overdraft 6000	12000	Y's Capital(stock) Loss transferred to capitals X- 7200 Y- 1800	4000 9000
Bank(Realisation expenses)	2000		
	1,14000		1,14,000

Partner's Capital Accounts

Particulars	X	Y	Particulars	X	Y
Profit & Loss a/c	8,000	2,000	Balance b/d	50,000	40,000
Realisation a/c		4,000	Realisation a/c	8,000	
Realisation a/c(loss)	7,200	1,800			
Bank a/c	42,800	32,200			
	58,000	40,000		58,000	40,000

Bank account

Particulars	Amt (Rs)	Particulars	Amt(Rs)
Balance b/d	20,000	Y's loan a/c	3,000
Realisation a/c(assets realized)	72,000	Realisation a/c(liabilities paid off)	12,000
		Realisation a/c(expenses)	2,000
		X's Capital a/c	42,800
		Y's capital a/c	32,200
	92,000		92,000

6. A, B and C commenced business on 1st January 2008 with capitals of Rs 50,000, 40,000 and Rs 30,000 respectively. Profits and losses are shared in the ratio of 4:3:3. During 2008 and 2009 they made profit of Rs 20,000 and Rs 25000 respectively. Each partner withdrew Rs 5000 per year.

   On 31st December 2009, they decided to dissolve the firm. Creditors and cash on that date were Rs 12,000 and Rs 2000 respectively. The Assets realized Rs 1,50,000. Creditors were settled for Rs 11,500 and realization expenses were Rs 500.

   Prepare Realisation a/c, Capital accounts and Cash account.

Realisation account

Particulars	Rs	Particulars	Rs
Sundry Assets	1,45,000	Creditors	12,000
Cash a/c(Creditors)	11,500	Cash a/c(Assets realized)	1,50,000
Cash a/c(Expenses)	500		
Capital Accounts- A- 2,000 B- 1,500 C- 1,500	5,000		
	1,62,000		1,62,000

Partners Capital Accounts

Particulars	A	B	C	Particulars	A	B	C
Cash a/c	60,000	45,000	35,000	Balance b/d	58,000	43,500	33,500
				Realisation a/c	2,000	1,500	1,500
	60,000	45,000	35,000		60,000	45,000	35,000

Cash account

Particulars	Rs	Particulars	Rs
Balance b/d	2,000	Realisation(Creditors)	11,500
Realisation a/c	1,50,000	Realisation a/c(expenses)	500
		A's Capital a/c	60,000
		B's Capital a/c	45,000
		C's Capital a/c	35,000
	1,52,000		1,52,000

Working Note: Calculation of Closing capital(Capital as on 31/12/2009)

Particulars	A	B	C
Opening Capital	50,000	40,000	30,000
Add Profits(of two yrs)	18,000	13,500	13,500
Less Drawings(of 2 yrs)	10,000	10,000	10,000
Closing Capital	58,000	43,500	33,500

Memorandum Balance sheet as on 31/12/2009

Liabilities	Rs	Assets	Rs
Capitals- X-58000 Y-43500 Z-33500	1,35,000	Cash	2000
Creditors	12,000	Sundry Assets(Balancing fig)	1,45,000
	1,47,000		1,47,000

UNIT 4: Company Accounts- Share capital

LEARNING OBJECTIVES

Understand the meaning and features of company

I) Classification of share capital

II) Understand the accounting treatment of over subscription, calls in arrears, premium and discount on issue of shares.

III) Understand the meaning of forfeiture of shares

IV) Pass journal entries regarding forfeiture and reissue of shares

V) Calculate capital reserve

VI) Differentiate between capital reserve and reserve capital

VII) Understand the disclosure of the share capital in the balance sheet

Salient Features
*A company is an artificial person having separate legal entity.
*A company is created by law and effected by law.
*A private company can be formed with minimum two members and maximum fifty.
*For a public company minimum members required are 7 and there is no maximum limit.