Name of the Course: Financial Accounting

Name of the Chapter

ACCOUNTING FOR ADMISSION, RETIREMENT AND DEATH OF A PARTNER IN PARTNERSHIP FIRM

Name of the Authors:

Dr. Rabindra Kumar Swain
P.G. Department of Commerce
Utkal University, Bhubaneswar
Odisha-751004
Email: rabindraswain2@gmail.com
Mobile No.: 9437375400
IAA Membership No.- BH-50

&

Dr. Chandrika Prasad Das
P.G. Department of Commerce
Berhampur University, Berhampur
Odisha-760007
Email: chandrika.das9@gmail.com
Mobile No.: 9439441941
IAA Membership No.- BH-84

&

Dr. Suman Bindu
Department of Commerce
S.B.R. Govt. (Auto) Women's College
Berhampur, Odisha-760001
Email: sumanbindu43@gmail.com
Mobile No.: 9489245532
IAA Membership No.- BH-122

ACCOUNTING FOR ADMISSION, RETIREMENT AND DEATH OF A PARTNER IN PARTNERSHIP FIRM

1.0 LEARNING OBJECTIVES

After going through this chapter, you should be able to:
• define the rights that a new partner gets on his admission;
• know the effects of admission of a partner into the firm;
• calculate new profit-sharing ratio and sacrificing ratio among the partners;
• state the different methods of valuation of goodwill and make adjustment of Goodwill on admission of a new partner;
• determine the gain or loss on revaluation of assets and reassessment of liabilities and its treatment in the books of firm;
• prepare Memorandum revaluation account;
• distinguish between revaluation account and memorandum revaluation account;
• make adjustment of accumulated profits and losses and reserves appearing in the books of firm;
• prepare partners' capital accounts after admission of a new partner;
• prepare new balance sheet after admission;
• define the meaning and liability of retiring partner
• get an idea about the adjustments need to be done in case of retirement of a partner
• know the accounting treatments on death of a partner
• distribution of profit in case of death of partner
• prepare revaluation account
• prepare the executor's account

1.1 KEYWORDS

Accumulated Profits: In the Balance Sheet, undistributed profits appear as a general reserve or a credit balance in the Profit & Loss Account.

Goodwill: The reputation of the business, which is earned by a firm through the hard work and honesty of its owners.

Normal Profits: The amount of profit that can be predicted based on the normal rate of return.

Revaluation Account: An account created to determine the profit or loss resulting from asset and liability revaluation.

Sacrificing Ratio: Ratio in which the old partners sacrifice their share in favour of new partner

Super Profits: Excess of average expected profits over normal profits

Executors: The representatives of a deceased partner who are entitled to a share of the deceased partner's estate.

1.2 SUMMARY OF THE CHAPTER

A partnership is an arrangement between two or more people (referred to as partners) for sharing the profits of a business that is operated by all of them individually or by one of them acting on their behalf. Any change in the existing agreement will lead to the reconstitution of the partnership firm. This results in an end of the existing agreement and a new agreement comes into place with a changed relationship among the partners of the partnership firm and/or their composition. The business, however, continues. The partners often restructure the firm in a number of ways, including the admission of a new partner, a change in the profit-sharing ratio, the retirement of a partner, and their death.

On the retirement or death of a partner, the existing partnership deed comes to an end, and a new partnership deed must be prepared to continue the business with the remaining partners under new terms and conditions. The accounting treatment at the time of retirement and in the event of death is not much different. In both cases, we are required to determine the sum due to the retiring partner (in case of retirement) and to the legal representatives (in case of deceased partner) after making necessary adjustments in respect of goodwill, revaluation of assets, and liabilities and transfer of accumulated profits and losses. Furthermore, we might need to compute the new profit-sharing ratio for the remaining partners as well as their gaining ratio. In this chapter we shall have a brief idea about all these and in detail about the accounting implications of admission of a new partner, retirement and death of a partner.

1.3 INTRODUCTION

A new partner may be admitted when the partnership firm needs more capital or persons with better managerial ability or both. With the admission of a new partner, existing agreement comes to an end and new agreement among all the partners including the new partner comes into existence. According to section 31 of Indian partnership Act, 1932, “A person can be admitted as a new partner if it is so agreed in the partnership deed or if all the existing partners agree for the admission in the absence of partnership deed.

After admission the new partner gets the following two rights:

1. Right to share future profits or losses of the firm
2. Right to share in the assets of the firm

At the same time, the new partner is liable for any liability of the firm that incurs after the admission.

New partner pays premium for goodwill for receiving share in future profits which is sacrificed by old partners and brings in capital to get right in the assets of the firm.

1.4 EFFECTS OF ADMISSION OF A PARTNER

When a new partner is admitted into a partnership firm, it has the following effects on the firm:

1. Old partnership agreement comes to an end and a new partnership agreement comes into force. But the firm continues.
2. New partner gets right to share future profits of the firm and the combined share of old partners in profits gets reduced. For the right to share future profits, new partner brings premium for goodwill.
3. New partner contributes agreed amount of capital in the firm.
4. New partner gets right to share in the assets of the firm and at the same time becomes liable for the liabilities of the firm.
5. Adjustment for accumulated profits (Losses) and reserves is made.
6. Assets and liabilities are revalued and necessary adjustments are made in the books of accounts
7. Goodwill of the firm is valued and adjusted through the partners' capital account.
8. Capital accounts of partners may be adjusted as per the agreement.

1.5 ADJUSTMENTS REQUIRED AT THE TIME OF ADMISSION OF A PARTNER

The following adjustments are required on admission of a new partner into the firm:

1. Change in profit sharing ratio: Determining new profit-sharing ratio and sacrificing ratio
2. Valuation and adjustment of goodwill
3. Adjustment of gain or loss arising on revaluation of assets and liabilities
4. Adjustment of reserves and accumulated profits and losses
5. Adjustment of capital on the basis of new profit-sharing ratio or as agreed

1.5.1 Calculation of new profit-sharing ratio and sacrificing ratio

When a new partner is admitted in the firm, he gets shares in future profits of the firm and share of old partners in future profits gets reduced. As a result, there is change in the profit-sharing ratio among the partners including new partner. Therefore, it is required to calculate new profit-sharing ratio and also the sacrificing ratio.

1. ***New profit-sharing ratio***: The ratio in which all partners including new partner will share future profits and losses of the firm.
2. ***Sacrificing Partner:*** The partners whose shares have decreased as a result of change are known as sacrificing partners. They are usually the old partners of the firm
3. ***Sacrificing Ratio:*** Ratio in which the old partners sacrifice their share in favour of new partner is called sacrificing ratio. This ratio is calculated by taking out the difference between old profit shares and new profit shares

Sacrificing ratio = Old Profit-sharing ratio - New Profit-sharing ratio

Following cases may arise for the calculation of new profit-sharing ratio:

Case I: When new partner's share is given but the question is silent about the sacrifice made by the old partners: In this case it is assumed that the old partner will share the remaining share in their old profit-sharing ratio.

Illustration 1

A and B are partners sharing profits in the ratio 3:2. They admit C for 1/3rd share in future profits. Calculate the new ratio.

Solution:

Share in Firm = 1

C's Share = 1/3

Remaining Profit = 1 - 1/3 = 2/3

This remaining share of 2/3 is divided between A and B in the ratio 3:2

So, A's new share = 2/3 × 3/5 = 6/15

B's new share = 2/3 × 2/5 = 4/15

C's share = 1/3 × 5/5 = 5/15

New ratio = 6/15: 4/15: 5/15 = 6:4:5

Sacrificing ratio= old profit-sharing ratio of old partners – new profit sharing of old partners

A= 3/5 – 6/15 =3/15

B= 2/5 – 4/15 = 2/15

So, sacrificing ratio of A and B partners is 3/15: 2/15 i.e., 3:2

Case II: When new partner purchases his share from old partners in a particular ratio: In this case the new ratio of the old partners will be calculated by deducting the proportion given to the new partner from the shares of old partner.

Illustration 2

A and B are partners sharing in the ratio 3:2. They admit C as a new partner for 1/3rd share in future profits which he gets 1/9 from A and 2/9 from B. Calculate the new ratio.

Solution:

A's old share = 3/5; A sacrifices in favour of C = 1/9

So, A's new share = 3/5 - 1/9 = 22/45

B's old share = 2/5; B sacrifices in favour of C = 2/9

So, B's new share = 2/5 - 2/9 = 8/45

C's new share = 1/9 + 2/9 = 3/9 or 15/45

New ratio = 22: 8: 15

Case III: When the old partners surrender a particular fraction of their share in favour of new partner: In this case following steps are followed:

1. Determine the share surrendered by the old partners.
2. Find the new share of the old partners by deducting share surrendered from their old share.
3. Calculate share of the new partner by taking the sum of surrendered share of old partners.
4. Calculate the new ratio.

Illustration 3

A and B are partners sharing in the ratio 3:2. They admit C as the new partner. A surrender 1/3rd of his share and B surrenders 2/3rd of his share in favour of C. Calculate the new ratio.

Solution:

A's old share = 3/5; A surrenders in favour of C = 3/5 x 1/3 = 3/15

A's new share = 3/5 - 3/15 = 6/15

B's old share = 2/5; B surrenders in favour of C = 2/5 x 2/3 = 4/15

B's new share = 2/5 - 4/15 = 2/15

C's share = 3/15 + 4/15 = 7/15

New ratio = 6:2:7

Case IV: When the new partner acquires his share entirely from the old partners: In this case the sacrificing partner share is calculated by deducting his sacrifice from his old share.

Illustration 4

A and B are partners sharing in the ratio 3:2. They admit C for 1/5th share in profits which he acquires entirely from A. Calculate the new ratio.

Solution:

A's old share = 3/5; Sacrifice in favour of C = 1/5

A's new share = 3/5 - 1/5 = 2/5

B's share = 2/5

C's share = 1/5

New ratio = 2:2:1

Case V: When the new partner acquires his share from the old partners in the certain ratio: In this case the sacrifice of each partner is deducted from their old shares.

Illustration 5

A and B are partners sharing profits in the ratio 3:2. C is admitted for 1/3rd share which he acquires from A and B in the ratio of 2:1. Calculate the new ratio.

Solution:

A's old share = 3/5, A's sacrifice = 1/3 × 2/3 = 2/9

A's new share = 3/5 - 2/9 = 17/45

B's old share = 2/5, B's sacrifice = 1/3 × 1/3 = 1/9

B's new share = 2/5 - 1/9 = 13/45

C's share = 1/3 × 15/15 = 15/45

New ratio = 17:13:15

Illustration 6

X and Y are partners in a firm sharing profits and losses in the ratio 5:3. They admit Z into partnership. The new ratio 3:2:1. Calculate the Sacrificing Ratio.

Solution:

X's sacrifice = X's old share - X's new ratio = 5/8 - 3/6 = 6/48

Y's sacrifice = Y's old share - Y's new ratio = 3/8 - 2/6 = 2/48

Thus, sacrificing ratio = 6:2 or 3:1

Valuation and Adjustment of Goodwill

Goodwill

Goodwill is the good name or the reputation of the business, which is earned by a firm through the hard work and honesty of its owners. If a firm renders good services to the customers, the customers who feel satisfied will come again and again and the firm will be able to earn more profits in future. Goodwill is the value of reputation of a firm in respect of profits expected in future over and above the normal rate of profits earned by other firms in the same trade.

Features of Goodwill

1. It is an intangible asset.
2. It is helpful in earning excess profits.
3. Its value is liable to constant fluctuations.
4. It cannot be sold separately like other physical assets.

Categories of Goodwill

I. Purchased Goodwill: Purchased goodwill means goodwill for which a consideration has been paid e.g., when business is purchased the excess of purchase consideration paid over its net assets i.e. (Assets – Liabilities) is the Purchased Goodwill. It is separately recorded in the books because it is purchased by paying in the form of cash or kind.

Characteristics

(i) It arises on purchase of a business or brand.

(ii) Consideration is paid for it so it is recorded in books.

(iii) It is shown in the balance sheet as an asset.

(iv) It is amortised (depreciated).

(v) Value is a subjective judgment & ascertained by agreement of seller & purchaser. It is approximate value and cannot be sold separately in the market or in parts.

II. Self-generated Goodwill: It is also called as inherent goodwill. It is an internally generated goodwill which arises from a number of factors that a running business possesses due to which it is able to earn more profits in the future.

Features

(i) It is generated internally over the years.

(ii) A true cost cannot be placed on this type of goodwill.

(iii) Value depends on subjective judgment.

(iv) It is shown in the balance sheet as an asset because proper cannot be assigned to it.

Need for Valuing Goodwill

Whenever the mutual rights of the partners change the party which makes a sacrifice must be compensated. This basis of compensation is goodwill, so we need to calculate goodwill.

Mutual rights change under following circumstances:

1. When profit sharing ratio changes
2. On admission of a partner
3. On Retirement or death of a partner
4. When amalgamation of two firms takes place
5. When partnership firm is sold.

<u>Methods of Calculating Goodwill</u>

The following are the key methods of calculating goodwill:

1. Average Profit Method

2. Super Profit Method

3. Capitalisation Method

<u>Average Profit Method</u>

Under this method, the goodwill is valued at agreed number of 'years' of purchase of the average profits of the past few years. It is based on the assumption that a new business will not be able to earn any profits during the first few years of its operations. Hence, the person who purchases a running business must pay in the form of goodwill a sum which is equal to the profits he is likely to receive for the first few years. The goodwill is calculated as follows:

Value of goodwill = Average Profit × Number of years of purchase

Illustration 7

The profit for the last five years of a firm were as follows: year 1999 Rs.5,00,000; year 2000 Rs.4,45,000; year 2001 Rs.4,50,000; year 2002 Rs.3,98,000 and year 2003 Rs.4,00,000. Calculate goodwill of the firm on the basis of 4 years purchase of 5 years average profits.

Solution:

Total Profit = 5,00,000 + 4,45,000 + 4,50,000 + 3,98,000 + 4,00,000 = Rs. 21,93,000

Average Profit = Total Profit/No. of years= 21,93,000/5 = Rs. 4,38,600

Goodwill = Average Profit × No. of years of Purchase= 4,38,600 × 4 = Rs. 17,54,400

<u>Super Profit Method</u>

The goodwill under the super profit method is ascertained by multiplying the super profits by certain number of years' purchase. Super profit is the excess profits earned over normal profit. The steps involved under the method are:

1. Calculate the average profit,

2. Calculate the normal profit on the capital employed on the basis of the normal rate of return,

3. Calculate the super profits by deducting normal profit from the average profits, and

4. Calculate goodwill by multiplying the super profits by the given number of years' purchase.

Normal profit = (Capital employed x Normal rate of return)/100

Super Profit = Actual Profit/Average profit – Normal Profit

Illustration 8

A firm earns profit of 65,000 on a capital of 4,80,000 and the normal rate of return in similar business is 10%. Then the normal profit is 48,000 [10% of the 4,80,000]. The actual profit is 65,000(Average profit).

Solution:

Super profit = Actual profit – Normal profit= 65,000 – 48,000= Rs17,000

If value of Goodwill is calculated by 3 years' purchase of super profit then,

Goodwill = super profit x 3 years' purchase =17000 × 3 = Rs.51,000

<u>Capitalization Method</u>

Under this method the goodwill can be calculated in two ways:

(a) By capitalising the average profits

(b) By capitalising the super profits

(a) Capitalisation of Average profit: In this method, the value of goodwill is assumed to be excess of the capital value of average profit over the actual capital employed. The key steps involved in this method are as follows:

1. Computation of capitalised value of average profit = Average Profits × 100/Normal Rate of Return

2. Computation of capital employed= Total Assets (excluding goodwill) – outside liabilities

3. Computation of goodwill = Capitalised value of average profits – Capital employed

Illustration 9

A business has earned average profits of 40,000 during the last few years and the normal rate of return in a similar type of business is 10%. Ascertain the value of goodwill by capitalization method, given that the value of net assets of the business is 3,10,000.

Solution:

Capital Employed = Net assets= Rs. 3, 10,000

Capitalised value of average profit = Average Profit × 100/Normal rate of profit

= 40,000 × 100/10= Rs 4,00,000

Goodwill = Capitalised value – Capital employed = 4, 00,000 – 3,10,000= Rs. 90,000

(b) Capitalisation of Super profit: In this method, the value of goodwill is calculated on the basis of super profit method. Following formula is applied:

Goodwill = Super profit × 100/Normal rate of profit

Illustration 10

A firm earns a profit of 25,000 and has invested capital amounting to 2,20,000. In the same business normal rate of earning profit is 15%. Calculate the value of goodwill with the help of Capitalisation of super profit method.

Solution:

Actual profit = Rs. 25,000

Normal profit = 2, 20,000 x 10/ 100 = Rs. 22,000

Super Profit = Actual Profit – Normal Profit

= 25,000 – 22,000= Rs 3,000

Goodwill = Super profit × 100/Normal rate of profit

= 3,000 × 100/15= Rs 20,000

1.5.2 Accounting Treatment of Goodwill

1.Goodwill (Premium) Paid Privately

If the goodwill premium is paid privately by the new partner to the old partners outside the business, then the same is not recorded in the books of accounts and hence no journal entry is recorded.

2.Goodwill/Premium brought in Cash by the New Partner

When, the new partner brings his/her share of goodwill in cash, the amount brought in by the new partner is transferred to the existing partner in the sacrificing ratio. If there is any goodwill account in the balance sheet of existing partner, it will be written off immediately in existing ratio among the old partners. The journal entries are as follows:

a. For bringing premium (share of goodwill of new partner)

Cash/Bank A/c Dr

To Goodwill A/c

b. For transferring goodwill to the capital accounts of the old partners in their sacrificing ratio.

Goodwill A/c Dr

To Sacrificing Partner's Capital A/c (Individually)

However, instead of these two entries one can record only one entry given below:

Cash/Bank A/c Dr

To Sacrificing Partner's Capital A/c (Individually)

c. For writing off existing goodwill in balance sheet, if any, in old profit-sharing ratio

Existing/ Old Partner's Capital A/c (Individually) Dr.

To existing Goodwill A/c

3.When the new Partner does not bring his/her share of Goodwill in Cash

Sometimes the new partner is not able to bring goodwill in cash. In this case, the new partner's share of goodwill brought in is debited to his capital account and is transferred to the existing old partners in the sacrificing ratio. Also, the amount of goodwill existing in the books, if any, is written off by debiting the capital account of existing partners in their existing profit-sharing ratio.

1. For transferring new partner's share of goodwill to the capital accounts of the old partners in their sacrificing ratio.

New Partner's Capital A/c Dr

To Sacrificing Partner's Capital A/c (Individually)

2. For writing off existing goodwill in balance sheet, if any, in old profit-sharing ratio

Existing/ Old Partner's Capital A/c (Individually) Dr.

To existing Goodwill A/c

1. When goodwill at full value is raised, it is credited to old partners' capital accounts and then it is written off by debiting all partners' capital accounts. In that case no goodwill is shown in the balance sheet. The following entries are recorded:
   (a) Goodwill a/c Dr (Full Value)
   To Old partners' capital a/c (old ratio)
   (b) All partners' capital a/c Dr (including new partner in new ratio)
   To Goodwill a/c

4.Hidden or Inferred or Implied Goodwill

Sometimes the value of goodwill is not specifically given and has to be inferred or implied from the arrangement of capital or profit-sharing ratio.

For example, A's capital is Rs 20,000 and B's Capital is Rs 15,000 and they share profits equally. C is admitted as a partner with Rs 18,000 as his capital for 1/4 share in the profits. The total capital of the firm now ought to be Rs 72,000 for the simple reason that if C contributes Rs 18,000 for 1/4 share, then for full or unit profit he ought to have contributed Rs 72,000 (18,000 x 4). But the total capital of A, B and C becomes only Rs 53,000 (20,000+15,000+18,000). So, the hidden value of the goodwill should be taken as Rs 19,000(72,000-53,000), so that the total capital becomes Rs 72,000.

1.5.3 Accounting treatment of accumulated profit, reserves and accumulated loss

Accumulated profits and reserves, if any existing in the Balance Sheet at the time of admission of a new partner, are distributed to existing partners in their old profit-sharing ratio. The following journal entry is made:

Accumulated profits and reserves A/c Dr
To old partner's capital A/c (Old profit-sharing ratio)

Illustration 11

Following is the balance sheet as at 31st March, 2020 of A and B sharing profits and losses in the ratio of 3:2

Liabilities	Amount	Assets	Amount
Sundry creditors	95,000	Cash at Bank	10,000
General Reserve	15,000	Stock	20,000
Profit and Loss	20,000	Debtors	30,000
Capital Accounts		Plant and Machinery	50,000
A		Building	1,70,000
B	80,000		

	70,000		
Total	2,80,000	Total	2,80,000

On the above date C joined as a new partner for 1/5th share in future profits and losses on the following terms:

(i) C will bring in Rs. 1,00,000 for his capital
(ii) Goodwill of the firm was valued at Rs. 1,40,000 and C brings his share of goodwill
(iii) New profit-sharing ratio is 5:3:2

Pass necessary journal entries to record capital introduced by new partner, goodwill and accumulated profit and reserve. And also prepare new balance sheet.

Solution:

Sacrificing ratio

Particulars	Old ratio=3:2	New ratio =5:3:2	Sacrificing ratio= Old- New=1:1
A B C	3/5 2/5 -	5/10 3/10 2/10	3/5-5/10=1/10 2/5-3/10=1/10

Journal Entries

1. Bank a/c Dr 1,00,000
   To C's Capital a/c 1,00,000
   (Being capital brought in by C)
2. Bank a/c Dr. 28,000 (1/5th of 1,40,000)
   To A's capital a/c 14,000
   To B's Capital a/c 14,000
   (Being goodwill brought in by C transferred to old partners' capital accounts in their sacrificing ratio)
3. General reserve a/c Dr 15,000
   Profit and Loss a/c Dr 20,000
   To A's Capital a/c 21,000
   To B's capital a/c 14,000
   (Being accumulated profit and general reserve transferred to old partners' capital accounts in their old profit-sharing ratio)

Partners' capital Account

Particulars	A	B	C	Particulars	A	B	C
To Balance c/d	1,15, 000	98,000	1,00, 000	By Balance b/d By Bank By accumulated profits and GR	80,000 14,000 21,000	70,000 14,000 14,000	- 1,00,000 ----
Total	1,15,	98,000	1,00,	Total	1,15,0	98,000	1,00,000

	000		000		00		

New Balance sheet

Liabilities	Amount	Assets	Amount
Sundry creditors	95,000	Cash at Bank 10,000+1,00,000+ 28,000	1,38,000
Capital Accounts		Stock	20,000
A	1,15,000	Debtors	30,000
B	98,000	Plant and Machinery	50,000
C	1,00,000	Building	1,70,000
Total	4,08,000	Total	4,08,000

1.5.4 Accounting Treatment of Revaluation of Assets and Re-Assessment of Liabilities

When a new partner is admitted into the partnership, assets are revalued, and liabilities are reassessed. A Revaluation Account (or Profit and Loss Adjustment Account) is opened for the purpose. This account is debited with all reduction in the value of assets and increase in liabilities and credited with increase in the value of assets and decrease in the value of liabilities. The difference in two sides of the account will show profit or loss. This is transferred to the Capital Accounts of old partners in the old profit-sharing ratio. The entries to be passed are:

1. For increase in assets
   Assets a/c Dr (Individually)
   To Revaluation a/c (with increase in assets)
2. For decrease in assets
   Revaluation a/c Dr (with decrease in assets)
   To Assets a/c (individually)
3. For increase in Liabilities
   Revaluation a/c Dr (with increase in liability)
   To liabilities a/c (individually)
4. For decrease in liabilities
   Liabilities a/c Dr (individually)
   To Revaluation a/c (with decrease in liabilities)
5. For Profit on revaluation
   Revaluation a/c Dr
   To old partners' capital a/c (old profit-sharing ratio)
6. For loss on revaluation
   Old partners' capital a/c Dr (old profit-sharing ratio)
   To Revaluation a/c

As a result of the above entries, the capital account balances of the old partners will change, and the assets and liabilities will have to be adjusted to their proper values. They will now appear in the New Balance Sheet (After admission) at revised figures.

Table 1.1 Proforma of Revaluation Account

particulars	Amount	Particulars	Amount
• Assets (decrease in value) • Liabilities (increase in value) • Liabilities (unrecorded) • Profit transferred to old partners' capital a/c(BF) (individually in their old profit-sharing ratio)		• Assets (increase in value) • Liabilities (decrease in Value) • Assets (unrecorded) • Loss transferred to old partners' capital a/c(BF) (individually in their old profit-sharing ratio)	

Illustration 12

Given below is the Balance Sheet of A and B, who are carrying on partnership business as on March 31, 2019. A and B share profits in the ratio of 2:1

Balance Sheet of A and B as at March 31, 2019

Liabilities	Amount	Assets	Amount
Bills payable	10,000	Cash in Hand	10,000
Sundry creditors	58,000	Cash at Bank	40,000
Outstanding expenses	2,000	Sundry debtors	60,000
Partners' capital accounts		Stock	40,000
A	1,80,000	Plant and machinery	1,00,000
B	1,50,000	Building	1,50,000
Total	4,00,000	Total	4,00,000

C is admitted as a new partner on the date of the balance sheet on the following terms:

1. C will bring in 1, 00,000 as his capital and 60,000 as his share of goodwill for 1/4th share in profits.

2. Plant is to be appreciated to 1, 20,000 and the value of buildings is to be appreciated by10%.

3. Stock is found overvalued by 4,000.

4. A provision for bad and doubtful debts is to be created at 5% of debtors.

5. Creditors were unrecorded to the extent of 1,000.

Prepare the revaluation account and new balance sheet after admission

Solution:

Revaluation Account

Particulars	Amount	Particulars	Amount
Stock	4,000	Plant and Machinery	20,000
Provision for Bad and Doubtful Debts	3,000	Building	15,000
Creditors	1,000		
Profit on revaluation transferred to capital a/c of-			
A	18,000		
B	9,000		
Total	35,000	Total	35,000

Journal Entries in books of the firm

1. Entry for capital contribution
   Cash a/c Dr 1,00,000
   To C's Capital a/c 1,00,000
2. Entry for bringing goodwill
   Cash a/c Dr 60,000
   To A's Capital a/c 40,000
   To B's Capital a/c 20,000
   (in Sacrificing Ratio)

Balance sheet of the firm after admission as on 31st march 2019

Liabilities	Amount	Assets	Amount
Bills payable	10,000	Cash in Hand (1,00,000+10,000+60,000)	1,70,000
Sundry creditors (58,000+1,000)	59,000	Cash at Bank	40,000
Outstanding expenses	2,000	Sundry debtors (60,000-3,000)	57,000
Capital		Inventory (40,000-4,000)	36,000
A (1,80,000+18,000+40,000)	2,38,000	Plant and Machinery (1,00,000+20,000)	1,20,000
B (1,50,000+9,000+20,000)	1,79,000		
C	1,00,000	Building (1,50,000+15,000)	1,65,000
Total	5,88,000	Total	5,88,000

When the revised values are not to be recognized in the Books (Memorandum Revaluation Account)

Sometimes all the partners including the new partner may agree to keep the assets and liabilities at the old values even when they agree to revalue them. To record these adjustments, a Memorandum Revaluation Account is opened. This account is divided into two parts.

(a) In the first part the entries for the revaluation of assets and liabilities are made in the usual way as explained earlier.
The resultant profit or loss on revaluation in the first part of this account is transferred to the capital accounts of old partners only in the old profit-sharing ratio.

1. Revaluation A/c Dr.
   To Assets A/c (Individually) (Amount of reduction in value)
   To Liabilities A/c (Individually) (Amount of increase in value)
2. Assets A/c (Individually) Dr. (Amount of increase in value)
   Liabilities A/c (Individually) Dr. (Amount of reduction in value)
   To Revaluation A/c
3. Revaluation A/c Dr. (Balancing Figure i.e., Profit)
   To Old Partners' Capital A/c (Individually in Old Profit ratio)
   OR
   Old Partners' Capital A/c Dr. (Individually in Old Profit Ratio)
   To Revaluation A/c (Balancing Figure i.e., Loss)

(b) Now, to complete the double entry, entries made in the first part of Memorandum Revaluation Account are reversed in the second part so that the values of the assets and liabilities remain unchanged.
The balance of the second part is transferred to the capital accounts of all the partners including new partner in their new profit-sharing ratio.

1. Assets A/c (Individually) Dr. (Amount of reduction in value)
   Liabilities A/c (Individually) Dr. (Amount of increase in value)
   To Memorandum Revaluation A/c
2. Memorandum Revaluation A/c Dr.
   To Assets A/c (Individually) (Amount of increase in value)
   To Liabilities A/c (Individually) (Amount of reduction in value)
3. All Partners' Capital A/c Dr. (Individually in New Ratio)
   To Memorandum Revaluation A/c (Balancing Figure)
   OR
   Memorandum Revaluation A/c Dr. (Balancing Figure)
   To All Partners' Capital A/c (Individually in New Profit ratio)

Note: Thus, if there is a profit in the first part there will be a loss of the same amount in the second part. The only point to be remembered is that the result of the first part of Memorandum Revaluation Account is shared by old partners in the old profit-sharing ratio, while the result of the second part is shared by all partners including the new one in the new profit-sharing ratio.

Table 1.2 Proforma of Memorandum Revaluation Account

Particulars	Amount	Particulars	Amount
Decrease in Assets Increase in Liabilities Unrecorded Liabilities Profit (BF) transferred to old partners' capital Accounts	XXX ---------------	Increase in Assets Decrease in Liabilities Unrecorded Assets Loss (BF) Transferred to old partners' capital accounts	XXX ------------------
Increase in Assets Decrease in Liabilities Unrecorded Assets Profit transferred to all partners' capital accounts including new partner		Decrease in Assets Increase in Liabilities Unrecorded Liabilities Loss transferred to all partners' capital accounts including new partner	

Illustration 13

Following was the balance sheet A, B and C who were the equal partners as at 31st march, 2020

Liabilities	Amount	Assets	Amount
Bills payable	3,300	Cash	600
Creditors	6,000	Debtors	10,800
Capital A/Cs		Stock	11,400
A	16,800	Furniture	2,400
B	12,600	Building	19,500
C	6,000		
Total	44,700	Total	44,700

D is admitted as new partner from 1st April, 2020 for 1/4th share in the profits on the following terms:

(i) D should bring in Rs. 9,000 for goodwill and Rs. 15,000 for capital.
(ii) Stock and Furniture be depreciated by 10%.
(iii) A liability for 1,080 be created against bills discounted.
(iv) Provision for Bad debts be created at5%
(v) Building is undervalued by 8,500
(vi) The value of assets and liabilities other than cash are not to be altered

Prepare memorandum revaluation accounts, capital accounts and new balance sheet

Solution:

Step-1

Calculation of new profit-sharing ratio

Old profit-sharing ratio between A, B and C = 1:1:1 (Given)

Let the profit be 1

D's share = 1/4th of 1= ¼= 3/12

Remaining profit =1- ¼= ¾

¾ will be shared between A, B and C equally

A's new share= 1/3 x 3/4= 3/12

B's new share=1/3 x 3/4= 3/12

C's new share= 1/3 x 3/4= 3/12

New profit sharing ratio between A, B, C and D = 3/12 : 3/12 : 3/12 : 3/12 =1:1:1:1

Step-2

Calculation of sacrificing ratio

Particulars	Old ratio 1:1:1	New ratio 1:1:1:1	Sacrificing ratio= Old- New=1:1:1
A	1/3	1/4	1/3-1/4=1/12
B	1/3	1/4	1/3-1/4=1/12
C	1/3	1/4	1/3-1/4=1/12
D	-	1/4	

Step-3

Entry for capital brought in by new partner

Cash A/C Dr 15,000

To D's Capital A/C 15,000

(Being capital brought in by D)

Cash A/c Dr 9,000

To A's capital 3,000

To B's capital 3,000

To C's capital 3,000

(Being goodwill brought in cash by new partner transferred to old partners' capital accounts in their sacrificing ratio)

Step-4

Memorandum Revaluation Account

Particulars	Amount	Particulars	Amount
Stock Furniture Provision for bad debts Liability for bills discounted Capital accounts A B C	1,140 240 540 1,080 1,833 1,833 1,834	Building	8,500
	8,500		8,500
Building	8,500	Stock Furniture Provision for bad debts Liability for bills discounted capital accounts A B C D	1,140 240 540 1,080 1,375 1,375 1,375 1,375
Total	8,500	Total	8,500

Step -5

Preparation of capital accounts of partners

Particulars	A	B	C	D	Particulars	A	B	C	D
To memorandum revaluation	1,375	1,375	1,375	1,375	By Balance b/d	16,800	12,600	6,000	
To balance c/d	20,258	16,058	9,459	13,625	By cash	3,000	- 3,000	- 3,000	15,000
					By memorandum Revaluation	1,833	1,833	1,834	
	21,633	17,433	10,834	15,000		21,633	17,433	10,834	15,000

Step -6

Preparation of cash Account

Particulars	Amount	Particulars	Amount
To Balance b/d To D's Capital To old partners' capital	600 15,000 9,000	By Balance c/d	24,600
Total	24,600	Total	24,600

Step-7

Preparation of new balance sheet

Liabilities	Amount	Assets	Amount
Bills payable	3,300	Cash	24,600
Creditors	6,000	Debtors	10,800
Capital A/Cs		Stock	11,400
A	20258	Furniture	2,400
B	16,058	Building	19,500
C	9,459		
D	13,625		
Total	68,700	Total	68,700

Difference between Revaluation Account and Memorandum Revaluation Account

1. Revaluation account is prepared to find out the profit or loss on revaluation of assets and liabilities which appear in the new balance sheet at the new or revalued figures. Memorandum revaluation account is also prepared to record the effect of revaluation of assets and liabilities which of course are recorded at their old figures in the new balance sheet.

2. Revaluation account is not divided into two parts. But the memorandum revaluation account has two parts: first part for old partners and second part for all partners including the new partner.

3. The net result of revaluation of assets and liabilities in the revaluation account is transferred to old partners' capital accounts in the old profit-sharing ratio. In the case of memorandum revaluation account the first part is used to record the changes in the values of assets and liabilities due to revaluation and in the second part the effect of the first part is cancelled. The balance of the first part is transferred to old partner's capital accounts in the old profit-sharing ratio while the balance of the second part is transferred to all partners including the new partner in the new profit-sharing ratio.

1.5.5 Adjustment of Partner's Capital in New Profit-Sharing Ratio

Sometimes, it is possible that the partners decide to adjust their capital so as to be proportionate to their profit-sharing ratio. If the capital of the new partner is given, the same can be used as a base for calculating the new capitals of the old partners. After making the necessary adjustments the partners can compare their new capital with the old capital and the partner whose capital falls short, will bring in the necessary amount and the partner who has a surplus, will withdraw excess amount of capital.

The partners can decide to maintain their new capital on the following basis:

- On the basis of new Partner's Capital and his profit-sharing ratio
- On the basis of the existing partner's capital account balances

On the Basis of new Partner's Capital and his Profit-Sharing Ratio

If the capital of the new partner is given, the entire capital of the new firm will be determined on the basis of the new partner's capital and his profit-sharing ratio. Therefore, the capital of other partners is ascertained by dividing the total capital as per his profit-sharing ratio.

If the existing capital of the partner after adjustment is in excess of his new capital, the excess amount is withdrawn by partner or transferred to the credit of his current account. If the existing capital of the partner is less than his new capital, the partner brings the short amount or makes transfer to the debit of his current account.

The journal entries are made as under:

(i) When excess amount is withdrawn by the partner or transferred to current account.

Existing Partner's Capital A/c Dr.

To Bank A/c or Partner Current A/c

(Excess amount is withdrawn by the partner or transferred to current account)

(ii) For bringing in the Deficit amount or Balance transferred to current account.

Bank A/c or Partner Current A/c Dr

To Existing Partner's Capital A/c

(Bringing the Deficit amount or Balance transferred to current account)

Illustration 14

A and B are partners sharing profit in the ratio of 5:3 with capital of Rs.80,000 and Rs.70,000 respectively. They admit a new partner C. The new profit-sharing ratio of A, B and C is 5:3:2 respectively. C brings Rs.40,000 as capital. The profit on revaluation of assets and reassessment of liabilities is Rs.6,400. It is agreed that capitals of the partner's should be in the new profit-sharing ratio. Calculate new capital of each partner.

Solution:

Actual Capital of A and B

	A (Rs)	B (Rs)
Balance in Capital A/c	80,000	70,000
Add Profit on Revaluation (5 : 3)	4,000	2,400
Capital after Adjustment	84,000	72,400

Calculation of new capital of the firm and existing partner's capital

C's Share in the firm = 2/10

C's brings 40,000 for 2/10 Share

Total capital of the new firm in terms of C's capital

= 40,000 × 10/2= Rs. 2, 00,000

A's share in New Capital = 2,00,000 × 5/10 = Rs1,00,000

B's share in New Capital = 2,00,000 × 3/10 = Rs.60,000

On comparing A's adjusted capital with the new capital, we find that the A brings Rs.16,000 [1, 00,000 – 84,000] or the amount may be debited to his current account.

On comparing the B's adjusted capital with the new capital, we find that the B is to withdraw Rs12,400 [72,400 – 60,000] or the amount may be credited to his current account.

On the Basis of the Existing Partner's Capital Account Balances

Sometimes the capital of the new partner is calculated on the basis of existing partners. The partner is required to bring an amount proportionate to his/her share of profit. In such a case, new partner's capital will be calculated on the basis of adjusted capital of the existing partners.

Illustration 15

The capital account of X and Y show the balance after all adjustments and revaluation are 100,000 and 50,000, respectively.

They admit Z as a new partner for 1/4 share in the profits. Z's capital is calculated as follows:

Total share = 1

Z's share in the profit = 1/4

Remaining share = 1 – 1/4 = 3/4

3/4 share of profit combined capital of X and Y = 100,000 + 50,000 = Rs.1,50,000

Total Capital of the firm = 1,50,000 × 4/3 = Rs.2,00,000

Z's capital for 1/4 share of profits = 2,00,000 × 1/4 = Rs50,000

Z brings in Rs.50,000 as his Capital

1.6 ACCOUNTING FOR RETIREMENT/DEATH OF A PARTNER

Retirement/death of a partner means a partner ceases to be a partner of the partnership firm. According to Section 32 of partnership Act, 1932 contemplates three ways in which a partner may retire from the firm. They are:

(i) If there is agreement about the retirement.

(ii) If all partners agree to his/her retirement

(iii) If the partnership is at will, by giving a written notice to the remaining partners of his decision to retire.

On retirement of a partner old partnership firm comes to an end and a new partnership among the remaining partners comes into force. However, the firm continues. The partner who has retired from a firm is called an outgoing partner. The firm is reconstituted by the remaining partners.

1.7 LIABILITY OF RETIRING PARTNER/OUTGOING PARTNER

A retiring partner remains liable for all the acts of the firm up to the date of retirement. On retirement the outgoing partner has to give a public notice of his retirement from the firm otherwise he remains liable to third parties for any acts of the firm even after his/her retirement.

1.8 ADJUSTMENTS REQUIRED ON RETIREMENT OF A PARTNER

(i) Computation of new profit-sharing ratio and gaining ratio

(ii) Treatment of goodwill

(iii) Revaluation of assets and reassessment of liabilities

(iv) Distribution of reserves and accumulated profits/losses

(v) Settlement of the Accounts due to Retired partner/outgoing partner

1.8.1 Computation of new profit-sharing ratio and gaining ratio

Retirement or death of a partner leads to change in profit sharing ratio among the remaining partners as they acquire share of retiring or deceased partner. New profit-sharing ratio of the continuing or remaining partners and their gaining ratio are calculated. The ratio in which remaining or continuing partners share the profits or losses of the firm is called new profit-sharing ratio.

Gaining ratio: It is the ratio in which the continuing partners have acquired the share from the outgoing partner. Gaining Ratio = New Ratio - Old Ratio

Illustration 16

A, B and C are partners sharing profits in the ratio of 5:3:2. Due to some personal reasons A retires from the partnership. Calculate the new profit-sharing ratio and gaining ratio of remaining partners.

Solution:

1. Calculation of new profit-sharing ratio: In order to calculate new ratio of B and C, it is assumed that A's share of 5/10 will be taken up by B and C in their old profit-sharing ratio

B's new share = 3/10 + (5/10 ×3/5) = 3/10 + 15/50 = 30/50

Raj's new share = 2/10 + (5/10 × 2/5) = 2/10 + 10/50 = 20/50

Therefore, the new profit-sharing ration is30/50: 20/50 or 3:2

2. Calculation of gaining ratio: Gaining ratio = New share – Old share

(i) B's gain =3/5 – 3/10 = 3/10

(ii) C's gain =2/5 – 2/10 = 2/10

Gaining ratio of B and C is 3/10 :2/10 or 3:2

1.8.2 Treatment of Goodwill

At the time of retirement or death of a partner the retiring partner/representative of deceased partner is entitled to his share of goodwill because the goodwill has been earned by the firm with the efforts of all the existing partners. The valuation of goodwill will be done as per the agreement among the partners. It is possible that company will earn some profit in near future because of the existing goodwill of the company. Therefore, the retiring/deceased partner should be compensated for the same by the continuing partners in their gaining ratio. For this purpose, the retiring/deceased partner's capital will be credited.

1. When old goodwill appears in the books then first of all this is written off in the old ratio.

 All Partners' capital A/c Dr (Old ratio)

 To Goodwill A/c

2. After written off of goodwill adjustment of retiring partner's share of goodwill will be made through the following journal entry.

 Remaining Partner's Capital A/c Dr. (in gaining ratio)

 To Retiring/Deceased Partner's Capital A/c (share of goodwill of retiring partner)

Illustration 17

A, B and C are partners sharing profits in the ratio 5:3:2. A retires and goodwill is valued at 54,000. New profit-sharing ratio of continuing partners will be equal. Pass the necessary journal entry.

Solution:

Journal

B's Capital a/c	Dr 10,800	
C' Capital a/c	Dr 16,200	
To A's Capital a/c		27,000

(Being A's share of Goodwill raised debited remaining partners' capital a/c in gaining ratio)

Working Notes:

Total Goodwill= 54,000

A's share= 1/2 of 54,000= 27,000

New profit-sharing ratio of B and C= 1:1 (Given)

Calculation of Gaining Ratios

Gain of partner = New share – Old share

B's Old share =3/10

B's new share = ½

B's gain =1/2– 3/10 = 2/10

C's Old share =2/10

C's new share =1/2

C's gain =1/2– 2/10 = 3/10

Therefore, gaining ratio is 2: 3

1.8.3 Revaluation of Assets and Reassessment of Liabilities

In case of retirement or death of a partner the assets and liabilities of the firm should be revalued in the same way as at the time of admission of a partner. At the time of retirement/death some of the assets or liabilities may not have been shown at their current values. To ascertain the net profit and loss on revaluation of assets and liabilities Revaluation A/c is prepared.

The following journal entries are passed for the revaluation of assets and liabilities:

(i) For increase in the value of Assets

Asset A/c Dr.

To Revaluation A/c

(Increase in the value of assets)

(ii) For decrease in the value of Asset

Revaluation A/c Dr.

To Asset A/c

(Decrease in the value of assets)

(iii) For increase in the value of Liabilities

Revaluation A/c Dr.

To Liabilities A/c

(Increase in the value of Liabilities)

(iv) For decrease in the value of Liabilities

Liabilities A/c Dr.

To Revaluation A/c

(Decrease in the value of Liabilities)

(v) For unrecorded Assets

Asset A/c [unrecorded] Dr.

To Revaluation A/c

(Unrecorded asset recorded at actual value)

(vi) For unrecorded Liability

Revaluation A/c Dr.

To Liability A/c [unrecorded]

(Unrecorded Liability recorded at actual value)

(vii) For transfer of gain on revaluation:

Revaluation A/c Dr.

To All Partner's Capital A/c (Old ratio)

(Profit on revaluation transferred to capital account in old profit-sharing ratio)

(viii) For transfer of loss on revaluation:

All Partner's Capital Dr.

To Revaluation A/c

(Loss on revaluation transferred to capital account in existing ratio)

Illustration 18

X, Y and Z are partners sharing profit in the ratio 1:2:3. X retires from the partnership. In order to settle his claim, the following revaluation of assets and liabilities 29as agreed upon:

(i) The value of Machinery is increased by 15,000.

(ii) The value of Investment is increased by 2,000.

(iii) A provision for outstanding bill standing in the books at 1,000 is now not required.

(iv) The value of Land and Building is decreased by 12,000.

Give journal entries and prepare Revaluation account.

Solution:

Journal Entries

1. Machinery a/c Dr 15,000

   Investment a/c Dr 2,000

   Provision for Outstanding Bill Dr 1,000

   To Revaluation a/c 18,000

   (Being increase in assets and decrease in liability)

2. Revaluation a/c Dr 12,000

   To land and Building a/c 12,000

   (Being decrease in assets)

3. Revaluation a/c Dr 6,000

To X's capital a/c 1,000

To Y's capital a/c 2,000

To Z's capital a/c 3,000

(Being profit on revaluation)

Revaluation A/C

Particulars	Amount	Particulars	Amount
To Land and Building	12,000	By Machine	15,000
To profit on revaluation		By Investment	1,000
X	1,000	By provision for Bill	2,000
Y	2,000		
Z	3,000		
Total	18,000	Total	18,000

1.8.4 Accounting Treatment of Reserves and Undistributed Profits or Losses

At the time of retirement or death of a partner the amount of reserves and undistributed profits (losses), as shown in the Balance Sheet of the firm belongs to all the partners and is transferred to their capital accounts in old profit-sharing ratio.

For the purpose, the following journal entries are recorded:

(i) For distribution of undistributed profit and reserve.

Reserves A/c Dr

Profit and loss A/c (Profits i.e., credit balance) Dr

To All partners' capital A/c (individually)

(Reserves and undistributed profit transferred to partner's capital A/c in old profit sharing ratio)

(ii) For distributing losses among all partners in the old ratio

All Partners' Capital A/c Dr

To P&L A/c (accumulated losses, i.e., debit balance)

To Deferred Revenue Expenditure A/c

The surplus available on some specific funds like workmen's compensation fund or investment fluctuation fund to meet certain obligations in future will be transferred to capital accounts of all the partners in their old ratio. For the purpose, the following journal entries are recorded:

Workman's Compensation Fund A/c Dr.

Investment Fluctuation fund A/c Dr.

To All Partners' capital A/c

(Surplus available on workmen's compensation fund and investment fluctuation fund transferred to partner's capital A/c in old profit-sharing ratio)

1.8.5 Settlement of the Accounts due to Retired partner

When a partner retires from business, his claim against the firm is determined by preparing his capital account incorporating therein all the adjustments in respect of his share of goodwill, accumulated profits or losses, profit/loss on revaluation of assets and liabilities, etc. Now the settlement of the claim depends on the provisions of the partnership deed. If nothing is given in the problem to be solved in respect of settlement of claim, the amount of claim is usually transferred to the Retiring partner's Loan Account for which the following entry is passed:

Retiring Partner's Capital A/c Dr

To Retiring Partner's Loan A/c

Note: Retiring partner's loan a/c is shown as liability in the new balance sheet. If retiring partner's loan is paid immediately then, it is no more shown as liability.

Mode of Payment

The outgoing partner's account is settled as per terms of partnership deed, i.e., in lump sum immediately or in various installments with/without interest as agreed or partly cash immediately and partly in installments at the agreed intervals.

- **Payment in Lump Sum**

If the full amount of claim is payable to the retiring partner on the date of retirement as per agreement, the amount will not be transferred to Loan Account but will be paid in cash or by cheque.

The following journal entry is made for disposal of-the amount payable to the retiring partner:

Retiring Partner's Capital A/c Dr.

To Cash/Bank A/c

(Amount paid to the retiring partner)

- ***Payment in Installments***

In this case the amount due to retiring partner is paid in installments. In the absence of any agreement, section 37 of the Indian Partnership Act, 1932 is applicable.

*Note: As per the Sec 37 of Indian Partnership Act, 1932, outgoing partner is at liberty to receive either interest @ 6% p.a. till the date of payment or the share of profits which has been earned with his money.

An instalment consists of two parts:

(i) Principal Amount of instalment due to retiring partner

(ii) Interest at an agreed rate.

Interest due on loan amount is credited to retiring partners' loan account. Instalment inclusive of interest then is paid to the retiring partner as per schedule agreed upon.

(i) On part payment in cash and balance transferred to his/her loan account.

Retiring Partner's Capital A/c Dr.

To Cash/Bank A/c

To Retiring Partner's Loan A/c

(Part payment made and balance transferred to loan A/c)

(ii) Total amount due transferred to loan A/c

Retiring Partner's Capital A/c Dr.

To Retiring Partner's Loan A/c

(Total amount due transferred to loan A/c)

(iii) For interest due

Interest on loan A/c Dr

To Retiring Partners' Loan A/c

(Interest due on loan)

(iv) For payment of instalment

Retiring Partners' Loan A/c Dr

To Cash/Bank A/c

(Instalment inclusive of interest paid)

DEATH OF PARTNER

1.9 ACCOUNTING TREATMENT ON DEATH OF A PARTNER

The key difference between the retirement and death of partner is that normally the retirement takes place at the end of an accounting period whereas death can occur at any time. Hence, in the case of death of a partner his claim shall include:

- share in the profits of the firm up to the date of death
- interest on his capital up to the date of death
- share in the proceeds of joint life policy (if any) in addition to his share in the accumulated profits
- share of goodwill,
- profit or loss on revaluation of assets and liabilities

On the death of a partner, the accounting treatment regarding goodwill, revaluation of assets and reassessment of liabilities, accumulated reserves and undistributed profit are similar to that of the retirement of a partner.

1.10 ASCERTAINMENT OF SHARE OF PROFIT UP TO THE DEATH OF PARTNER

If the death of a partner occurs during the year, the representatives of the deceased partner are entitled to his/her share of profits earned till the date of his/her death. Such profit is ascertained by any of the following methods:

- Time Basis
- Turnover or Sales Basis

On the Basis of Time

There are two methods used in ascertainment of profit on the basis of time:

1. On the basis of average profit of certain years: Under this method the calculation of profit is based on the average annual profit for the past few years say, 3 to 5 years. Then, the profit for the proportionate period is found out.

Illustration 19

X, Y and Z are partners sharing profits equally. Z dies on April 30, 2004. The accounts of the firm are closed on Dec. 31. The profits for the past 3 years are: 2018 - 35,000; 2019 - 40,000 and 2020 - 60,000. Calculate the Z's share of profit from 1st April to 30th April2021.

Solution:

The average profit for the past three years:

(35,000 + 40,000 + 60,000)/3 = Rs. 45,000

Profit for 4 months up to April 30, 2004 = 4/12 × 45,000 = Rs. 15,000

Z's share of Profit = 15,000 × 1/3 = Rs. 5,000

2. On the basis of last year's profit: Calculation of profit is based on the last year's profit.

Illustration 20

The total profit of previous year is 3,60,000 and a partner dies three months after the close of previous year, the profit of four months= 3,60,000 ×4/12 = Rs.1,20,000

If the deceased partner took 2/10 share of profit, his/her share of profit till the date of death is1,20,000 × 2/10 = Rs 24,000.

On the Basis of Turnover

Under this method, the share of profit is calculated on the basis of the profit and the total sales of the last year. Thereafter, the profit up to the date of death is estimated on the basis of the sale of the last year. Profit is assumed to be earned uniformly at the same rate.

Illustration 21

A, B and C are partners sharing profits and losses in the ratio of 2:1:1. B dies on March 1, 2021. Sales for the year 2021 amount to Rs 80,000, out of which Rs 25,000 are for a period from January 1, 2021 to March 1, 2021. The profit for the year is Rs. 40,000. Calculate the B's share of profit.

Solution:

The Profit up to the date of B's death= (25,000/80,000) × 40,000= Rs.12,500

B's share = 12,500 × 1/4 = Rs. 3,125

Journal Entry for share of profit of deceased partner up to date of death is:

P/L suspense a/c Dr

To deceased partner's capital a/c

Note: P/L suspense a/c is shown as asset in the balance sheet till actual profit for the year of death of deceased partner is calculated.

1.11 SETTLEMENT OF EXECUTOR'S ACCOUNT

After the death of a partner the total amount due to him is transferred to his, executor's account and paid off as per the provisions of the partnership deed immediately or in instalments together with interest on the unpaid balance. As explained earlier the amount due to the deceased partner should include the amount standing to the credit of his Capital Account, a share in the accumulated profits, goodwill, joint life policy (if any), profit on revaluation of assets/liabilities.

The following entries should be passed for disposal of amount due to the deceased partner:

(a) The amount standing to the credit of deceased partner's capital is transferred to his executor's account, by recording the following entry:

Deceased partner's capital A/c Dr

To Deceased partner's executor's A/c

Deceased partner's executor's account will be settled as per the agreement between the firm and executors of the deceased partner. Unless otherwise mentioned Executor's account is shown as liability in new balance sheet.

(b) When the full amount is paid in cash, following entry is recorded:

Executor's A/c Dr

To Cash/Bank A/c

(c) When the settlement is made in installments, the following entries are made:

(i) For interest due:

Interest on executor's A/c Dr

To Executor's A/c

(ii) For payment of instalment on loan account

Executor's A/c Dr

To Cash/Bank A/c

Illustration 22

Balance sheet as at 31st march 2020 of A, B and C partners in a firm sharing profits and losses in the ratio of 5:3:2 is as follows:

Liabilities	Amount	Assets	Amount
Capital A/Cs		Furniture	10,000
A	10,000	Machinery	40,000
B	15,000	Stock	15,000
C	20,000	Debtors	15,000
Creditors	30,000	Cash in hand	5,000
Profit and Loss	10,000		
Total	85,000	Total	85,000

B died on 31st May, 2020 and A and C decided to share future profits and losses in the ratio of 3:2. Average profit earned by the firm is 12,000. Following adjustments are agreed

(a) Maintain provision for bad and doubtful debts Rs. 1,000
(b) Stock is to be valued at Rs. 10,000
(c) Machinery be reduced by 10%
(d) Amount of Rs. 12,000 included in creditors no longer payable
(e) The goodwill of the firm was valued at Rs. 25,000 on B's death.

The amount payable to B was transferred to his executor's account. You are required to prepare revaluation account, partners' capital account and balance sheet of A and C.

Solution:

Step-1

Old profit-sharing Ratio between A, B and C= 5:3:2

New profit-sharing ratio between A and C= 3:2

Step-2

Calculation of gaining ratio

Particulars	Old ratio=5:3:2	New ratio=3:2	Gaining ratio=New-old=1:2
A	5/10	3/5	3/5 – 5/10= 1/10
B	3/10	-	
C	2/10	2/5	2/5 – 2/10 =2/10

Step-3

Treatment of Goodwill

Goodwill valued at Rs 25,000

Deceased partner's (B) share goodwill has been raised

His share in goodwill = 3/10 x 25,000= 7,500

A's capital a/c Dr 2,500

C's Capital a/c Dr 5,000

To Deceased partner's capital a/c (B's Capital a/c) 7,500

(Being B's share of goodwill raised and transferred to existing partners' capital a/cs in their gaining ratio)

Step- 4

Calculation of share of profit of B (Deceased partner) till the date of death

Closing date = 31st march

Date of death = 31st may

Average profit earned per annum =12,000

Estimated profit for 2 months i.e., 31st March to 31st May 2020

= 2/12 x 12,000 = 2,000

B's share of such profit= 3/10 x 2,000= 600

Profit and Loss suspense a/c Dr 600

To B's capital a/c 600

(Being share of estimated profit transferred to B's capital a/c)

Step-5

Distribution of Accumulated profits

Profit and Loss a/c Dr 10,000

To A's capital a/c 5,000

To B's capital a/c 3,000

To C's capital a/c 2,000

(Being accumulated profits distributed among all the partners in their old profit-sharing ratio)

Step-6

Preparation of Revaluation A/C

Revaluation Account

Particulars	Amount	Particulars	Amount
To provision for bad and doubtful debts To stock To machinery To capital accounts A B C	1,000 5,000 4,000 1,000 600 400	By creditors	12,000
Total	12,000	Total	12,000

Step -7

Preparation of capital accounts

Capital Accounts

Particulars	A	B	C	Particulars	A	B	C
To Goodwill	2,500	-	5,000	By Balance b/d	10,000	15,000	20,000
To B's executor a/c		26,700		By Goodwill		7,500	
To Balance c/d				By Revaluation	1,000	600	400
A C	13,500		17,400	By profit and Loss	5,000	3,000	2,000
				By P/L suspense		600	
	16,000	26,700	22,400		16,000	26,700	22,400

Step- 8

Preparation of new balance Sheet

Balance sheet after Death of B

Liabilities	Amount	Assets	Amount
Capital A/Cs		Furniture	10,000
A	13,500	Machinery	36,000
C	17,400	Stock	10,000
B's Executor a/c	26,700	Debtors	14,000
Creditors	18,000	Cash in hand	5,000
		P/L Suspense a/c	600
Total	75,600	Total	75,600

1.12 SOME USEFUL BOOKS

- Robert N Anthony, David Hawkins, Kenneth A. Merchant, *Accounting: Text and Cases*. McGraw-Hill Education, 13th Ed. 2013.
- Charles T. Horngren and Donna Philbrick, *Introduction to Financial Accounting,* Pearson Education.
- J.R. Monga, *Financial Accounting: Concepts and Applications*. Mayur Paper Backs, New Delhi.

- M. C. Shukla, T.S. Grewal and S. C. Gupta. *Advanced Accounts. Vol.-I. S.* Chand & Co., New Delhi.
- S.N. Maheshwari, and. S. K. Maheshwari. *Financial Accounting*. Vikas Publishing House, New Delhi.
- Deepak Sehgal. *Financial Accounting.* Vikas Publishing H House, New Delhi.
- Bhushan Kumar Goyal and HN Tiwari, *Financial Accounting,* International Book House
- Goldwin, Alderman and Sanyal, *Financial Accounting,* Cengage Learning.
- Tulsian, P.C. *Financial Accounting,* Pearson Education.
- *Compendium of Statements and Standards of Accounting*. The Institute of Chartered Accountants of India, New Delhi

1.13 QUESTIONS/EXCERSISES

Questions

Admission

1. What do you understand by admission of a partner? How is new partner admitted to the firm?

2. What is new profit-sharing ratio? How is it calculated in different cases?

3. What is sacrificing ratio? How is it calculated? Explain the significance of sacrificing ratio for admission of a partner.

4. Discuss the methods of valuation of goodwill on admission of a partner.

5. Explain the accounting treatment of goodwill in the books of firm on admission of a partner.

6. What is revaluation account? Why is revaluation account opened on admission of a partner? Give its accounting treatment in the books of firm.

7. Give accounting treatment of accumulated profits and losses and reserves appearing in the books of a firm on admission of a partner.

8. X and Y are partners sharing profits and losses in the ratio of 3:1. Calculate new profit-sharing ratio and sacrificing ratio in each of the following cases:

Case 1. Z is admitted with 1/8th of the profits

Case 2. Z is admitted with conditions that Z acquires 1/12 from X and 1/6 from Y

Case 3. Z is admitted on the conditions that X surrenders 1/3rd of his share in favour of Z whereas Y surrenders 2/3rd of his share in favour of Z.

Case 4. Z is admitted into partnership on the conditions that Z acquires 1/4th of his share from X and 3/4th of his share from Y

(Answer: Case 1: New profit-sharing ratio- 21:7:4, Sacrificing ratio: 3:1

Case 2: New profit-sharing ratio- 8:1:3, Sacrificing ratio: 1:2

Case 3: New profit-sharing ratio- 6:1:5, Sacrificing ratio: 3:2

Case 4: New profit-sharing ratio- 9:1:6, Sacrificing ratio: 1:1)

9. Profits for last four years of a partnership firm ending 31st march are:

2020-Rs. 12,000, 2019- Rs.18,000, 2018- Rs. 16,000 and 2017- Rs. 14,000

Capital employed is 1,00,000

Normal rate of profit is 10%

A and B were partners sharing profits and losses equally and they admit C as new partner into the firm.

Make a valuation of Goodwill by following the methods given below:

(a) Average profit method taking 3 years' purchase
(b) Super profit method taking two years' purchase
(c) Capitalization method

(Answer: (a): Rs. 45,000, (b): Rs:10,000, (c): Rs. 50,000)

10. Pass journal entries to record the following transactions on admission of new partner Z with partners X and Y who share profits and losses in the ratio of 3:2. Prepare revaluation a/c.

(a) The value of furniture is to be increased by Rs. 10,000

(b) Stock is undervalued by 10% whose book value is Rs. 18,000

(c) Machinery is overvalued by Rs. 20,000

(d) Bills Payable is shown in the balance sheet in excess by Rs.3,000

(e) Creditors is to be increased by Rs.6,000

(f) Other fixed assets of Rs.40,000 will be appreciated by 20%

(g) Provision for bad debts is to be maintained by 5% (Debtors Rs45,000)

(h) Outstanding expenses of Rs.4,000 was not disclosed in the balance sheet.

(i) Investment of Rs.12,000 not recorded in the balance sheet.

(Answer: Profit on revaluation: Rs. 2,550)

11. X and Y are partners in a firm sharing profits and losses in the ratio of 3:2. They admit Z as new partner with $1/8^{th}$ share in the future profits of the firm, when their balance sheet stood as:

Balance Sheet

Liabilities	Amount	Assets	Amount
Creditors	20,000	Cash in hand	2,000
Bills Payable	12,000	Cash at bank	23,000
X's Capital	40,000	Inventory	10,000
Y's Capital	30,000	Debtors	25,000

		Plant and Machinery	42,000
Total	1.02,000	Total	1,02,000

Additional Information

(i) Goodwill is valued at 2 years purchase of the average profits of last three years which are Rs. 21,000, Rs24,000 and Rs. 27,000.
(ii) Z is to bring in cash his share of Goodwill
(iii) Z is to bring in cash Rs. 20,000 as his capital
Pass necessary journal entries recording the transactions and prepare the balance sheet of the firm after admission of Z. Also calculate the new profit-sharing ratio and sacrificing ratio.

(Answer: New profit-sharing ratio: 21:14:5, Sacrificing ratio: 3:2, Goodwill Rs. 48,000 Balance Sheet total: Rs. 1,28,000, Capitals: X- Rs. 43,600, Y-Rs. 32,400, Z-Rs. 20,000)

12. Following is the balance sheet of A and B who are sharing profits in the ratio of 1:1 as at 31st march 2021.

Liabilities	Amount	Assets	Amount
Capital A/Cs		Land and Buildings	25,000
A	15,000	Plant and Machinery	12,500
B	10,000	Stock	10,000
Bills payable	32,950	Debtors	4,850
		Cash in hand and cash at bank	5600
Total	57,950	Total	57,950

They agree to admit C into the partnership on the following conditions:

(i) C is to bring in Rs.8,000 as his capital and Rs. 4,000 as goodwill for 1/4th share in the firm.
(ii) Value of stock and plant machinery are to be reduced by 5%
(iii) A provision for doubtful debts is to be created for debtors
(iv) Land and building is to be appreciated by 10%

Prepare revaluation a/c, capital accounts of partners and balance sheet of the new firm. Pass necessary journal entries to record the above arrangements.

(Answer: New profit-sharing ratio: 3:3:2, Sacrificing ratio: 1:1, Profit on revaluation: Rs. 890, Balance Sheet total: Rs. 70,840, Capitals: A- Rs. 17,445, B-Rs. 12,445, C-Rs. 18,000)

13. A and B are partners sharing profits and losses in the ratio of 2:1. The balance sheet of the firm as on 31st march 2021 is as follows:

Liabilities	Amount	Assets	Amount
Sundry Creditors	25,000	Cash /Bank	5,000
General Reserve	18,000	Debtors	15,000
Capital A/Cs		Stock	10,000
A	75,000	Machinery	50,000
B	62,000	Building	1,00,000
Total	1,80,000	Total	1,80,000

They admit C into partnership on the same date on the following terms:

(a) C brings in Rs. 40,000 as his capital and he is given 1/4th share in profits
(b) C brings in Rs. 15,000 for goodwill
(c) Machinery is depreciated by 5% and Building is appreciated by 10%
(d) Creditors of Rs. 5,000 remains unrecorded
(e) Capitals of A and B are to be proportionate to that of C on their profit-sharing basis.

Pass journal entries, prepares and revaluation a/c, capital accounts and new balance sheet of the firm.

(Answer: New profit-sharing ratio: 2:1:1, Sacrificing ratio: 2:1, Profit on revaluation: Rs. 2500, Balance Sheet total: Rs. 1,90,000, Capitals: A- Rs. 80,000, B-Rs. 40,000, C-Rs. 40,000, Surplus Cash paid to A – Rs, 18,667, B- Rs. 33,833)

14. A and B are partners in a firm sharing profits and losses in the ratio of 3:1. They admit C as a new partner for 1/4th share in future profits of the firm. C is to bring Rs. 50,000 for his capital. The balance sheet of A and B as at 31st march 2020, the date on which C was admitted is:

Liabilities	Amount	Assets	Amount
Sundry Creditors	70,000	Cash /Bank	10,000
General Reserve	10,000	Debtors	34,000
Capital A/Cs		Stock	30,000
A	50,000	Investments	26,000
B	80,000	Plant and machinery	70,000
		Land and Building	40,000
Total	2,10,000	Total	2,10,000

Other terms agreed upon are:

(a) Goodwill is valued at 24,000
(b) Land and building are valued at Rs 60,000 and plant machinery is at Rs.65,000
(c) Provision for doubtful debts is to be maintained by 10%
(d) The capital of partners is to be adjusted on the basis of C's capital to the firm

(e) Excess or shortfall, if any be transferred to current accounts

Prepare revaluation account, partners' capital accounts and balance sheet of the new firm.

(Answer: New profit-sharing ratio: 9:3:4, Sacrificing ratio: 3:1, Profit on revaluation: Rs. 11,600, Balance Sheet total: Rs. 3,13,400, Capitals: A- Rs. 1,12,500, B-Rs. 37,500, C-Rs. 44,000, current account of A(Dr): Rs. 41,800, Current account of B(Cr) – Rs. 49,400)

15. P and Q are partners in a firm sharing profits and losses in the ratio of 2:1. They admit R as a new partner for 1/5h share in future profits of the firm. R is to bring Rs. 60,000 for his capital. The balance sheet of P and Q as at 31st march 2021, the date on which C was admitted is:

Liabilities	Amount	Assets	Amount
Creditors	50,000	Cash /Bank	10,000
Bills Payable	90,000	Debtors	25,000
General Reserve	10,000	Stock	30,000
Profit & Loss	20,000	Investments	55,000
Capital A/Cs		Plant and machinery	1,00,000
P	60,000	Land and Building	90,000
Q	80,000		
Total	3,10,000	Total	3,10,000

Other terms agreed upon are:

(a) R is to bring in Rs. 4,000 for goodwill
(b) Land and building are valued at Rs 75,000 and plant machinery is at Rs.1,05,000
(c) Provision for doubtful debts is to be maintained by 10%
(d) Equipment worth Rs.10,000 was unrecorded.
(e) Outstanding expenses Rs. 2,000 is to be recognized.

Prepare revaluation account, partners' capital accounts and balance sheet of the new firm.

(Answer: New profit-sharing ratio: 8:4:3, Sacrificing ratio: 2:1, Loss on revaluation: Rs. 4,500, Balance Sheet total: Rs. 3,71,500, Capitals: P- Rs. 79,667, Q-Rs. 89,833, R-Rs. 60,000)

16. Following is the balance sheet of A, B and C who are equal partners as at 31st march 2020.

Liabilities	Amount	Assets	Amount
Bills Payable	3,300	Cash /Bank	10,600
Sundry Creditors	6,000	Debtors	10,800
General Reserve	10,000	Stock	11,400
Capital A/Cs		Furniture	2,400
A	16,800	Land and Building	19,500
B	12,600		

C	6,000		
Total	54,700	Total	54,700

Other terms agreed upon are:

(a) D is admitted as a new partner for 1/4th share in profits of the firm and brings in Rs. 15,000 as capital and Rs. 9,000 as his share of goodwill
(b) Stock and furniture are depreciated by 10%
(c) A liability of Rs. 1,000 be created against bills discounted
(d) The value of building is undervalued by Rs.8,000
(e) The value of assets and liabilities is not be changed in new balance sheet except cash

Prepare revaluation account, Memorandum revaluation a/c, partners' capital accounts and balance sheet of the new firm. Pass necessary journal entries.

(Answer: New profit-sharing ratio: 1:1:1:1, Sacrificing ratio: 1:1:1, Memorandum revaluation A/c Balance: Rs. 5,620, Balance Sheet total: Rs. 78,700, Capitals: A- Rs. 23,601, B-Rs. 19,401, C-Rs. 12,803, D- Rs. 13,595)

Retirement& Death

17. Distinguish between sacrificing and gaining ratio.

18. Explain the procedure of calculating gaining ratio with an example.

19. Explain the accounting treatment of goodwill on retirement/death of a partner.

20. Why are assets and liabilities revalued on retirement /death of a partner? Pass necessary journal entries to that effect.

21. What problems arise when a partner die? How would you deal with them as an Accountant?

22. Explain the procedure of estimation of profits up to the date of death on the basis of time and turnover/sales.

23. Calculate new profit-sharing ratio and gaining ratio in the following cases:

(a) A, B and C were partners, sharing profits and losses in the ratio of 5:4:1. A retires/dies. Calculate new profit-sharing ratio between B and C. Also calculate gaining ratio between B and C.

(b) A, B and C were partners sharing profits and losses in the ratio of 5: 3:2. B retires/dies. His share is taken by A and c in the ratio of 2:1. Calculate new profit-sharing ratio as well as gaining ratio between A and C.

(c) A, B and C were partners sharing profits and losses in the ratio of 2:2:1. C retires/dies. His share is taken by B. calculate new profit-sharing ratio and gaining ratio.

(d) A, b and C were partners sharing profit and loss in the ratio of 5:3:2. A retire/dies. B and C decide to share future profits and losses in the ratio of 3:2. Calculate new profit-sharing ratio and gaining ratio

(e) X, Y and Z were partners sharing profits and losses in the ratio of 4:3:2. Z retires and surrenders 1/9th of his share to X and the remaining to Y. Calculate new profit-sharing ratio and gaining ratio.

(Answer: (a) New profit-sharing ratio- 4:1, Gaining ratio: B only gains

(b) New profit-sharing ratio- 7:3, Gaining ratio: 2:1

(c) New profit-sharing ratio- 3:2, Gaining ratio: A only gains

(d) New profit-sharing ratio- 3:2, Gaining ratio: 3:2)

(e) New profit-sharing ratio- 38:43, Gaining ratio: 1:8)

24. Make necessary journal entries for adjustment of goodwill in the books of account of firm after retirement or death of a partner.

(a) A, B, C and D are partners sharing profits and losses in the ratio of 2:1:2:1. On retirement/death of C, goodwill was valued at Rs. 72,000. A, B and D decided to share future profits equally. Calculate gaining ratio and Make adjustment entries for goodwill without opening the goodwill account.

(b) X, Y and Z are partners sharing profits and losses in the ratio of 3:2:1. Z retires/ dies on which date goodwill was valued at Rs. 1,20,000. Calculate new profit-sharing ratio and gaining ratio and pass the necessary journal entries giving effect to goodwill account.

(c) A, B and C were partners sharing profits and losses in the ratio of 3:2:1. C retired from the firm on that date goodwill was valued at Rs. 1,20,000. Pass the necessary journal entries raising goodwill for retiring partner’s share. Also calculate new profit sharing and gaining ratio.

(d) X, Y and Z are partners sharing profits and losses in the ratio of 2:3:5. Goodwill is appearing in their books at a value of Rs. 50,000 and on that date X retires. Goodwill is valued at Rs. 45,000. Y and Z decided to share the future profits equally. Pass necessary journal entries for goodwill.

(e) A, B and C are partners sharing profits and losses in the ratio of 1: 2:3. C retires and his capital after making all adjustments for accumulated profits and reserves and profit / loss on revaluation Rs. 2,20,000. A and B agreed to pay him Rs. 2,50,000 in full settlement of his claim. Record necessary journal entry for the treatment of goodwill if the new profit-sharing ratio is 1:3.

(Answer: (a) New profit-sharing ratio- 2:1:1, Gaining ratio: 2:1:1

(b) New profit-sharing ratio- 3:2, Gaining ratio: 3:2

(c) New profit-sharing ratio- 3:2, Gaining ratio: 3:2

(d) New profit-sharing ratio- 1:1, Gaining ratio: Y gains only)

(e) New profit-sharing ratio- 1:3, Gaining ratio: 1:5)

25. Balance sheet of A, B and C partners sharing profits and losses in the ratio of 5:3:2 as at 31st March 2020 was:

Liabilities	Amount	Assets	Amount
Sundry creditors	15,000	Cash at Bank	27,000
Capital A/Cs		Debtors	15,200
A	46,000	Stock	12,800
B	34,000	Plant and machinery	35,000
C	25,000	Land and Building	30,000
Total	1,20,000	Total	1,20,000

B retires / dies on 1st April, 2020. A and c decided to share future profits and losses in the ratio of 3:1. Following adjustments are agreed:

(a) An amount of Rs. 1,200 included in debtors be written off as bad debts.
(b) Stock to be written down by Rs. 1,500
(c) Land and Building is written up by Rs. 11,000
(d) Plant and Machinery be reduced to Rs. 34,000
(e) Amount of Rs. 700 included in creditors no longer payable
(f) Firm had to pay Rs. 5,000 to an employee injured in an accident.

You are required to pass journal entries and also prepare revaluation account.

(Answer: New profit-sharing ratio: 3:1, Gaining ratio: 5:1, Profit on revaluation: Rs. 3,000, Retiring partners loan account (Partner B) -Rs. 34,900, Balance Sheet total: Rs. 1,27,300, Capitals: A- Rs. 47,500, C-Rs. 25,600)

26. Balance sheet of A, B and C partners in a firm sharing profits and losses in the ratio of 5:3:2 is as follows:

Liabilities	Amount	Assets	Amount
Capital A/Cs		Land and Building	60,000

A	92,000	Plant and Machinery	70,000
B	68,000	Stock	25600
C	50,000	Debtors	30,400
Sundry creditor	25,000	Cash in hand	5,500
Expense Payable	5,000	Cash at bank	48,500
Total	2,40,000	Total	2,40,000

On that date B retires from the firm and A and C decided to share future profits and losses in the ratio of 3:2. Following adjustments are agreed

(a) An amount of Rs. 1,000 included in debtors be written off as bad debts.
(b) Stock to be written down by Rs. 1,200
(c) Land and Building is written up by Rs. 11,000
(d) Plant and Machinery be reduced to Rs. 64,000
(e) Amount of Rs. 1,000 included in creditors no longer payable
(f) Firm had to pay Rs. 6,000 to an employee injured in an accident.
A and C decided that assets and liabilities shall continue to be shown at existing values other than cash and bank balance. Prepare Memorandum revaluation account.

(Answer: New profit-sharing ratio: 3:2, Gaining ratio: 1:2, Profit on revaluation: Rs. 2,200, Retiring partners loan account (Partner B) -Rs. 67,340, Balance Sheet total: Rs. 2,40,000, Capitals: A- Rs. 92,220, C-Rs. 50,440)

27. A, B and C are partners sharing profits and losses in the ratio of 3:2:1. C retires/dies. On the date of retirement, the following balances appear in the books of the firm:

General reserves Rs. 90,000

Profit and Loss account (Dr) Rs. 15,000

Employees' provident fund Rs 1,20,000

Workmen compensation fund Rs 12,000 which is no more required.

Pass journal entries for adjustment of these items on C's retirement.

(Answer: New profit-sharing ratio: 3:2, Gaining ratio: 3:2)

28. A, B and C are partners sharing profits and losses of a firm in the ratio of 3:2:1. Their balance sheet is at 31st March 2010 was:

Liabilities	Amount	Assets	Amount
Capital A/Cs		Land and Building	14,000
A	10,000	Plant and Machinery	6,000
B	10,000	Stock	7,000

C	10,000	Debtors	9,000
Sundry creditor	1,600	Cash in hand	600
General Reserve	6,000	Cash at bank	1,000
Total	37,600	Total	37,600

C retires from the business on 1st April. It was agreed that the amount due to him will be treated as loan. It was also agreed to adjust the value of assets as follows:

(a) Provision for bad debts be maintained on debtors by 10%.
(b) Stock is undervalued by Rs. 1,200
(c) Land and Building is written up by Rs. 10,000
(d) Plant and Machinery be increased to Rs. 12,000
(e) Goodwill of the firm is valued at Rs 15,000
(f) A and B will continue to carry on the business and shall share profits and losses equally in future.

Prepare Revaluation account, partners' capital accounts and balance sheet of new firm after retirement.

(Answer: New profit-sharing ratio: 1:1, Gaining ratio: B only gains, Profit on revaluation: Rs. 16,300, Retiring partners loan account (Partner C) -Rs. 16,217, Balance Sheet total: Rs. 53,900, Capitals: A- Rs. 21,150, B-Rs. 14,933)

29. A, B and C are partners sharing profits and losses of a firm in the ratio of 3:2:1. Their balance sheet is at 31st March 2010 was:

Liabilities	Amount	Assets	Amount
Capital A/Cs		Land and Building	14,000
A	10,000	Plant and Machinery	6,000
B	10,000	Stock	7,000
C	10,000	Debtors	9,000
Sundry creditor	3,000	Cash in hand	1, 600
General Reserve	7,000	Cash at bank	2,400
Total	40,000	Total	40,000

C retires from the business on 30th June, 2010. It was agreed that the amount due to him will be treated as loan. It was also agreed to adjust the value of assets as follows:

(a) Provision for bad debts be maintained on debtors by 5%.
(b) Stock is undervalued by Rs. 1,500
(c) Land and Building is written up by Rs. 10,200
(d) Plant and Machinery be increased to Rs. 12,600
(e) Goodwill of the firm is valued at two years' purchase of average profit. Average profit is Rs. 30,000
(f) C' share of profit up to the date of retirement be calculated on the basis of average profit

(g) A and B will continue to carry on the business and shall share profits and losses equally in future.

Prepare Revaluation account, partners' capital accounts, partner's loan account and balance sheet of new firm after retirement.

(Answer: New profit-sharing ratio: 3:2, Gaining ratio: 3:2, Profit on revaluation: Rs. 17,850, Retiring partners loan account (Partner C) -Rs. 25,392, Balance Sheet total: Rs. 59,100, Capitals: A- Rs. 16,425, B-Rs. 14,283)

30. Balance sheet as at 31st march 2020 of A, B and C partners in a firm sharing profits and losses in the ratio of 5:3:2 is as follows:

Liabilities	Amount	Assets	Amount
Capital A/Cs		Furniture	6,000
A	12,000	Machinery	35,000
B	16,000	Stock	15,000
C	12,000	Debtors	15,000
Sundry creditor	22,000	Cash in hand	3,000
General reserve	12,000		
Total	74,000	Total	74,000

B died on 31st March, 2020 and A and C decided to share future profits and losses in the ratio of 3:2. Following adjustments are agreed

(f) An amount of Rs. 1,000 included in debtors be written off as bad debts.
(g) Stock to be written down by Rs. 1,200
(h) Machinery be reduced by 10%
(i) Amount of Rs. 1,000 included in creditors no longer payable
(j) The goodwill of the firm was valued at Rs. 25,000 on B's death.

The amount payable to B was transferred to his executor's account. You are required to prepare revaluation account, partners' capital account and balance sheet of A and C.

(Answer: New profit-sharing ratio: 3:2, Gaining ratio: 1:2, Loss on revaluation: Rs. 4,700, B's executor's A/C -Rs. 25,690, Balance Sheet total: Rs. 68,300, Capitals: A- Rs. 13,150, C-Rs. 8,460)

31. Balance sheet as at 31st march 2020 of A, B and C partners in a firm sharing profits and losses in the ratio of 3:2:1 is as follows:

Liabilities	Amount	Assets	Amount
Capital A/Cs		Investments	1,41,000
A	1,80,000	Machinery	1,80,000

B	1,50,000	Stock	1,32,000
C	1,20,000	Debtors	30,000
Bills Payable	30,000	Cash in hand	48,000
Loan	36,000		
General reserve	15,000		
Total	5,31,000	Total	5,31,000

C died on 31st May, 2020 and A and B decided to share future profits and losses equally. Following adjustments are agreed

(a) Stock to be written down by Rs. 10,000
(b) Machinery be reduced by 10%
(c) Amount of Rs. 1,000 included in Bills payable no longer to be paid
(d) The goodwill of the firm was to be valued at two years' purchase of average profits of last three years which were Rs. 1,20,000
(e) C's share of profit till the date of death was to be calculated on the basis of last year's profit. Last year profit was Rs. 3,00,000.

Prepare partners' capital account, revaluation account and new balance sheet. C's capital account balance is to be transferred to his executor's account.

(Answer: New profit-sharing ratio: 1:1, Gaining ratio: B only gains, Loss on revaluation: Rs. 27,000, C's executor's A/C -Rs. 1,66,333, Balance Sheet total: Rs. 5,11,333, Capitals: A-Rs. 1,74,000, B-Rs. 1,06,000)

About the Authors:

1. **Dr. Rabindra Kumar Swain** is a senior faculty of P. G. Department of Commerce, Utkal University, Bhubaneswar having 30 years of teaching and research experience in Accounting, Corporate Reporting, Financial Management and Entrepreneurship. He has completed his M. Com, M. Phil, and Ph.D. from the P.G. Department of Commerce, Utkal University. He has also done his MBA from Utkal University. He qualified UGC-JRF in 1994. He has been honored with several national and international awards for best research papers. He has published about 58 research papers in various Peer Reviewed, UGC CARE and Scopus Indexed journals. He has also published eight books and many chapters to his credit. He has attended more than 100 national and international seminars and conferences and has also presented nearly 60 research papers in national seminars and about 36 research papers in international seminars. He has actively attended many refresher courses, Orientation Programmes, Training programmes and workshops. He has also organized various State, National and International level seminars, and conferences. He has successfully mentored 7 Ph.D. and 12 M.Phil. Scholars.

2. **Dr. Chandrika Prasad Das** is working as Assistant Professor at P.G. Department of Commerce, Berhampur University, Berhampur. He has published more than 27 research papers in various international and national repute journals. He has 3 research books to his credit in international repute and edited two books to date. His research interest is corporate finance, accounting, corporate governance, international business, international finance. He is having 7 years of teaching and research experience. He has been awarded the best research paper awards not only in India but across the world. He has presented more than 55 papers at national and international conferences.

3. **Dr. Suman Bindu** is currently working as Assistant Professor at Department of Commerce, S.B.R. Govt. (Auto) Women's College, Berhampur. Her research interest is corporate finance, international business, and corporate governance. She is having 4 years and 9 months of teaching and research experience. She has presented more than 20 papers at national and international conferences. She has 2 research books to her credit in international repute.