PARTNERSHIP: BASICS

DEFINITIONS

Partnership	Partnership is the relationship between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all.
Partners	Persons who have entered into Partnership with one another are individually called Partners.
Firm	Persons who have entered into Partnership with one another are collectively called firm
Firm Name	The name under which their business is carried on is called the Firm Name

FEATURES OF PARTNERSHIP

Persons	It requires at least two persons to form a Partnership.
Agreement	An agreement is entered by all the persons concerned, setting out the terms and conditions under which the Partnership is based. When this agreement is set out in writing, it is called the ''Partnership Deed''.
Legal Business	A partnership can exist only in business. Thus, it is not the agreement alone which creates a partnership. A partnership comes into existence only when partners begin to carry on business in accordance with their agreement
Mutual Agency	The activities of the business will be carried on/managed by all or any one of them acting for all. This principle of **mutuality** is the essence of Partnership agreement
Sharing of Profit/loss	The Partners share the profits and losses of the business in the agreed ratio.

PARTNERSHIP DEED & CONTENTS

Meaning	Partnership Deed is the *written agreement* containing the terms and conditions under which the Partnership will sustain or exist.
Contents of Partnership Deed	❖ Name of the firm and the nature of the Partnership Business. ❖ Commencement and Tenure of the Business (e.g. Partnership at Will, etc.) ❖ Amount of Capital to be contributed by each Partner. ❖ Ratio for sharing the Profit/Loss of the Partnership business amongst Partners. ❖ Arrangement in respects of Drawings by Partners and limits thereon. ❖ Interest to be credited on the Capital Account of Partners. ❖ Interest to be charged on Drawings of Partners ❖ Remuneration to Partners and the basis of determining such remuneration e.g. Commission as a percentage of the Firm's Turnover, other conditions for eligibility of remuneration etc. ❖ Process of setting disputes that may arises among the Partners. ❖ Procedure for maintenance of Books of Accounts ❖ Audit of Books of Accounts ❖ Manner of valuation of Goodwill in case of admission of new partners, retirement of existing partners and death of a Partner. ❖ Procedure for settlement of Partners' claims in case of retirement/death ❖ Procedure for dissolution of Partnership
Notes	❖ When partnership deed is not registered a partnership firm is allowed to carry on business subject to certain disabilities. ❖ It is not mandatory to have a written agreement in all cases. Further, even in cases where there is a written Partnership Deed, it is not compulsory to have it registered.

DISTINCTION BETWEEN PARTNERSHIP & LIMITED LIABILITY PARTNERSHIP

BASIS	PARTNERSHIP	LIMITED LIABILITY PARTNERSHIP
Applicable Law	Indian Partnership Act 1932	The Limited Liability Partnerships Act, 2008
Registration	Optional	Compulsory
Creation	Created by an Agreement	Created by Law
Separate Legal Entity	No	Yes
Perpetual Succession	Partnerships do not have perpetual succession	It has perpetual succession and individual partners may come and go
Number of Partners	Minimum 2 and Maximum 50	Minimum 2 but no maximum limit
Ownership of Assets	Firm cannot own any assets. The partners own the assets of the firm	The LLP as an independent entity can own assets
Liability of Partners / Members	**Unlimited**: Partners are severally and jointly liable for actions of other partners and the firm and their liability extends to personal assets	Limited to the extent of their contribution towards LLP except in case of intentional fraud or wrongful act of omission or commission by a partner.

REMUNERATION, INTEREST ON CAPITAL, LOAN, DRAWINGS, PROFIT SHARING RATIO

1. **Governing Statute:** The law governing Partnership in India is the Partnership Act, 1932.
2. **Conditions not covered by Partnership Deed:** Where any situation or circumstance is not covered by the Partnership Deed or is not adequately provided for in the Partnership Deed, the Provision of the Partnership Act, 1932 will apply.

If the Deed is silent on-	Provisions of the Partnership Act
Partners' Remuneration/ Salary/ Commission	**No** Remuneration will be allowed to any Partner.
Interest on Partners' Capital	**No** IOC will be allowed to any Partner.
Interest on loan given by Partner to the Firm	**Maximum 6% p.a.** can be allowed on loan.
Interest on Partners' Drawings	**No** interest will be charged on Partners' Drawings
Profit Sharing Ratio	Profits and Losses will be shared **equally.**

PARTNER'S CAPITAL ACCOUNTS

1. **Methods of Accounting:** The transactions affecting the Partners' Capital Accounts may be accounted under any of the following methods**-**

Aspects	Fluctuating Capital Method	Fixed Capital Method
Ledger A/cs prepared	Partner's Capital Account.	1. Partner's Capital Account, and 2. Partner's Current Account.
Initial Capital contribution	Amount brought in or contribution is **credited to the Partner's Capital A/c**	Amount brought in or contributed is **credited to the Partners' Capital A/c**
Subsequent transactions	Subsequent transactions are accounted in Partner's **Capital Account**	Subsequent transactions are accounted in Partner's **Current Account**

FORMAT OF PARTNER'S CAPITAL ACCOUNT

Particulars	A	B	C	Particulars	A	B	C
To **Cash/Bank** (Withdrawal of capital, if any) To **Balance c/d**				By **Balance b/d** By **Cash/ Bank/ Assets** (Capital Contribution)			
Total				**Total**			

FORMAT OF PARTNER'S CURRENT ACCOUNT

Particulars	A	B	C	Particulars	A	B	C
To **Balance b/d** To **Drawings A/c** To **P&L A/c** - Share of Loss To **Profit & Loss Appropriation** -Interest on Drawings, if any To **Balance c/d**				By **Balance b/d** By **Profit & Loss Appropriation** -Remuneration/ Salary/Comm. -Interest on Capital -Share of Profit By **Balance c/d**			
Total				**Total**			

Note: If Capital Accounts are maintained on Fluctuating basis, all the above entries will be made in one single Capital Account only. There will not be any Current Account

PROFIT & LOSS APPROPRIATION ACCOUNT

1. **Purpose:** Profit and Loss A/c of firm will show the profit earned or loss suffered by the firm.
   To distribute the above Profit properly to the Partners, the **Profit and Loss Appropriation A/c** is used
2. **Features:**
   (a) It is **extension of P&L Account**.
   (b) It provides details of how the Net Profit for the period has been **distributed to the Partners**
   (c) The entries in P&L Appropriation A/c are **governed by the Partnership Deed**.

Note: Interest on Partners' Loan, Rent for use of Partners' premises, if any, etc. are debited to P&L A/c itself. Net Profit after charging and debiting these items, is only transferred to P&L Appropriation A/c

3. **Format:**

Dr. **Profit & Loss Appropriation A/c** **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Interest on partner's capital	XX	By P&L A/c balance (Profit)	XX
A ---		By Interest on partner's drawings	XX
B ---		A ---	
To Partner's Salary	XX	B ---	
A ---			
B ---			
To Partner's Commission/Bonus	XX		
A ---			
B ---			
To Reserves (Amount transferred)	XX		
To Profits transferred in PSR:	XX		
A ---			
B ---			
Total	**XXXX**	**Total**	**XXXX**

Interest on Partners' Capital

Type of Capital	Computation of Interest on Capital (IOC)
1. Opening Capital	IOC= Opening Capital x Rate of Interest
2. Additional Capital	IOC= Additional Capital x Rate of Interest x Period of use

Interest on Capital in case of Insufficient Profits or Loss

Interest on Capital

- Deed is silent or No Deed → No IOC
- Deed provides for IOC
  - In case of Loss → No IOC
  - In case of Profit
    - Sufficient Profits [Profits ≥ IOC] → Full IOC
    - Insufficient Profits [Profits < IOC] → Profits distributed in ratio of capital
- Deed provides for IOC & specifically states it to be charge against profit → Full IOC even if there is loss

Effective Capital

Partners may agree to share profits and losses in the capital ratio. The capitals for the purpose of ratio would be determined with reference to time on the basis of weighted average method.

Example:
A and B formed a partnership with a capital contribution of Rs.1,00,000 and Rs.80,000 respectively on 1st January 2021. Profits were to be shared in the Effective Capital ratio. Interest on Capital is 6% p.a.

Date	Capital Introduced		Capital Withdrawn	
	A	B	A	B
1st April	2,00,000			
1st July		40,000	1,00,000	

Calculate: (a) Profit-sharing ratio; (b) Interest on capital

Effective capital :

A

1/1 $100000 \times \frac{12}{12} = 100000$

1/4 $200000 \times \frac{9}{12} = 150000$

1/7 $(100000) \times 6/12 = (50000)$

200000

B

1/1 $80000 \times \frac{12}{12} = 80000$

1/7 $40000 \times \frac{6}{12} = 20000$

100000

Ratio (PSR) => 200000 : 100000 = 2 : 1

IOC : A = 2L × 6% = 12000   B = 1L × 6% = 6000

Interest on Partners' Drawings

- ❖ Drawings refers to amount withdrawn by Partners, in cash or in kind, for their personal use.
- ❖ Partners are supposed to pay interest on drawings only when provided by the agreement or agreed by the partners.
- ❖ Interest on drawings is gain for the business. It is recorded on credit side of P&L Appropriation A/c.
- ❖ Partner's Drawings A/c & interest on drawings is closed by transferring to debit side of Capital or Current A/c.

Interest on Drawings

- Dates of Drawings not given
  - P.a.
    - $IOD = Drawings \times \frac{Rate}{100} \times \frac{6}{12}$
  - ~~P.a.~~
    - $IOD = Drawings \times \frac{Rate}{100}$
- Dates of Drawings given
  - Amt. of each drawing same **and** Time interval b/w 2 drawings same
    - Direct Method
    - Product Method
    - Shortcut Method (Preferable)
  - Either amount not same **or** Time interval not same
    - Direct Method
    - Product Method (Preferable)
    - Shortcut Method (X)

Short cut Method :

$$IOD = Total\ Drawings \times \frac{Rate}{100} \times \frac{Average\ Time\ Period^*}{12}$$

TTP = Total Time Period

TI = Time Interval

* Average Time Period

	Beginning	Middle	End
	$\frac{TTP + TI}{2}$	$\frac{TTP}{2}$	$\frac{TTP - TI}{2}$
A) 12 Months Period			
a) Monthly	$\frac{12+1}{2} = 6.5$	$\frac{12}{2} = 6$	$\frac{12-1}{2} = 5.5$
b) Quarterly	$\frac{12+3}{2} = 7.5$	$\frac{12}{2} = 6$	$\frac{12-3}{2} = 4.5$
B) 6 Months Period			
a) Monthly	$\frac{6+1}{2} = 3.5$	$\frac{6}{2} = 3$	$\frac{6-1}{2} = 2.5$
b) Quarterly	$\frac{6+3}{2} = 4.5$	$\frac{6}{2} = 3$	$\frac{6-3}{2} = 1.5$

Calculation of Remuneration/ Salary/Commission to Partners

Remuneration/ Salary/ Commission to Partners, can be provided to Partners, only if the Partnership Deed so provides. The calculations are as under:-

Type of Capital	Computation
1. Remuneration/ Salary	Remuneration / Salary p.a. = Monthly Amount x No. of months
2. Commission as x % of Turnover	Commission p.a. = Sales Turnover of the Firm x Rate of Commission
3. Commission as x % of Net Profit (a) Before Commission (b) After Commission	 Net Profit before Commission x Rate of Commission /100 Net Profit before Commission x $\frac{\text{Rate of Commission}}{(100+\text{Rate of Commission})}$

Past Adjustments in capital accounts of partners

Sometimes a few errors and omissions in the recording of transactions or the preparation of financial statements are found after the final accounts have been prepared and the profits distributed among the partners.

These omissions and errors may be in respect of:

- Interest on capitals, Interest on drawings,
- Partner's salary, partner's commission or
- Outstanding expenses.
- There may also be some changes in the provisions of partnership deed or system of accounting having impact with retrospective effect.

All these acts of omission and commission need adjustments for correction.

Now instead of altering all the old accounts, necessary adjustments can be made either;

❖ Through Profit and Loss Adjustment Account, or

❖ Directly in the Capital Accounts of the concerned partners.

<u>Journal entry for adjustment is:</u>

Gaining partner capital/current A/c Dr.

To Sacrificing Partner capital/current A/c

TABLE

	A	B	TOTAL
Items to be Recorded			
IoC	✓	✓	✓
Salary, Commission, etc.	✓	✓	✓
Share of Profit	✓	✓	✓
IoD	(✓)	(✓)	(✓)
CR.	✓	✓	✓
Items to be Reversed			
IoC	✓	✓	✓
Salary, Commission, etc.	✓	✓	✓
Share of Profit	✓	✓	✓
IoD	(✓)	(✓)	(✓)
DR.	✓	✓	✓
Difference	✓	✓	

Guarantee of Minimum Profit to a Partner

1. **Meaning:** Sometimes, Partners may mutually agree that certain Partner (s) has the right to have **minimum amount** of profit. Such profit is called Guaranteed Profit or Guaranteed Minimum Profit.
   Example: Guarantee given to a partner 'X' by the other partners 'Y & Z' means in case of loss or insufficient profits 'X' will withdraw the minimum guaranteed amount.

2. **Treatment:**

Situation	Steps in Computation/ Treatment
(a) If Profit Share > Guaranteed Profit	Distribute the Total Available Profit in the agreed profit sharing ratio, in the usual manner.
(b) If Profit Share < Guaranteed Profit	• Distribute the Total Available Profit in the agreed profit sharing ratio, in the usual manner. • Compute the **shortfall** in Guaranteed Profit, and add that to the share of the Partner entitled to the same. • Deduct the shortfall from the Profit shares of the Other Partners, as described below

Burden of Shortfall:

Guarantee given by	Shortfall to be reduced from
(a) One of the remaining partners	That Remaining Partners Share of Profit.
(b) Remaining two or all Partners in an agreed ratio	Two or all Partners, in agreed ratio
(c) Remaining Partners in their mutual PSR	All remaining Partners in mutual PSR

Note: If the question is silent about the nature of guarantee, situation (c) given above is assumed

Example

A, B and C entered into partnership on 1.1.2021 to share profits and losses in the ratio of 5 : 3 : 2. A personally guaranteed that C's share of profit after charging interest on capitals at 5% p.a. would not be less than Rs. 30,000 in any year. Capitals of A, B and C were Rs. 3,20,000, Rs. 2,00,000 and Rs. 1,60,000 respectively. Profits for the year ending 31.12.2021 before providing for interest on partners capital was Rs. 1,59,000. You are required to prepare the Profit and Loss Appropriation Account

Profit and Loss Appropriation Account

Particulars	Amount	Particulars	Amount
To Interest on Capital A/c A 3,20,000*5% = 16,000 B 2,00,000*5% = 10,000 C 1,60,000*5% = 8,000	34,000	By Profit and Loss A/c (Net profit)	1,59,000
To Profit tfd to Capital A/c A 125,000*5/10 = 62,500 – 5,000 = 57,500 B 125,000*3/10 = 37,500 C 125,000*2/10 = 25,000 + 5,000 = 30,000	1,25,000		
	1,59,000		**1,59,000**

Question

Good, Better and Best are in partnership sharing profits and losses in the ratio 3:2:4. Their capital account balances as on 31st March, 2021 are as follows:

	Rs.
Good	1,70,000 (Cr)
Better	1,10,000 (Cr)
Best	1,22,000 (Cr)

Following further information provided:

(1) Rs. 22,240 is to be transferred to General Reserve.
(2) Good, Better and Best are paid monthly salary in cash amounting 2,400, 1,600 & 1,800 respectively.
(3) Partners are allowed interest on their closing capital balance @ 6% p.a. and are charged interest on drawings @ 8% p.a.
(4) Good and Best are entitled to commission @ 8% and 10% respectively of the net profit before making any appropriation.
(5) Better is entitled to commission @ 15% of the net profit before charging Interest on Drawings but after making all other appropriations.
(6) During the year Good withdraw Rs. 2,000 at the beginning of every month, Better Rs. 1,750 at the end of every month and Best Rs. 1,250 at the middle of every month.
(7) Firm's Accountant is entitled to a salary of Rs. 2,000 per month and a commission of 12% of net profit after charging such commission.

The Net Profit of the firm for the year ended on 31st March, 2021 before providing for any of the above adjustments was Rs. 2,76,000.

You are required to prepare Profit & Loss Appropriation A/c for the year ended on 31st March, 2021

Solution

Working Note:-

(1)

Profit = 276000

− Salary = (24000) (2000 x 12)

250000

− Commission = (27000) $\left[250000 \times \frac{12}{112}\right]$

Net Profit 225000

(2) Better Commission

Profit = 225000 − 22240 − 69600 − 24120 − 18000 − 22500

⇒ 68540

Commission ⇒ $68540 \times \frac{15}{100}$ ⇒ 10281

P&L Appropriation A/c

Particulars	Amount	Particulars	Amount
To General Reserve	22240	By Net Profit	225000
To Salary		By Interest on drawings	
Good = 2400 x 12 = 28800		Good	
Better = 1600 x 12 = 19200		$24000 \times \frac{8}{100} \times \frac{6.5}{12} \Rightarrow$ 1040	
Best = 1800 x 12 = 21600	69600	Better	
To Interest on capital		$21000 \times \frac{8}{100} \times \frac{5.5}{12} \Rightarrow$ 770	
Good = 170000 x 6% = 10200		Best	
Better = 110000 x 6% = 6600		$15000 \times \frac{8}{100} \times \frac{6}{12} \Rightarrow$ 600	2410
Best = 122000 x 6% = 7320	24120		
To Commission			
Good = 225000 x 8% = 18000			
Best = 225000 x 10% = 22500			
Better => 10281	50781		
To Profit trfd. (B.f.)			
Good = $60669 \times \frac{3}{9}$ = 20223			
Better = $60669 \times \frac{2}{9}$ = 13482			
Best = $60669 \times \frac{4}{9}$ = 26964	60669		

GOODWILL

1. 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 similar Firms in the same locality.
2. Goodwill is the benefits and advantage of the good name, reputation and connections of a business firm. It is the attractive force which brings in customers, and enhances the revenues of the firm

Types of Goodwill

A. Purchased Goodwill	B. Self-Generated Goodwill
1. **Purchased Goodwill** arises when a business is purchased, & the consideration paid therefore is more than the value of assets taken over. 2. Purchased Goodwill= Purchase Consideration **Less** Net Assets taken over 3. Purchased Goodwill is recorded in books of accounts and **is shown** in the **balance sheet.**	1. It refers to **internally generated goodwill,** that arises to the special advantages possessed by the Firm. 2. Internally Generated Goodwill is **not recorded** in the books of account, since Accounting Standard 26 issued by ICAI specifically provides so.

Situations which may involve valuation of Goodwill in case of Firms

- Change in Profit Sharing Ratio amongst the Partners,
- Admission, Retirement & Death of a Partner,
- Dissolution of the Partnership

Methods of Valuation of Goodwill

Method:1 Average Profits Method

Average Profits Method

Simple Average

$$\text{Average Profits} = \frac{\text{Profits of 'n' years}}{\text{No. of Years}}$$

G/W = Avg. Profits X No. of years of Purchase

Weighted Average

$$\text{Weighted Average Profits} = \frac{\text{Total Weighted Profits}}{\text{Total of Weights}}$$

G/W = Weighted AP X No. of years of Purchase

Computation of Adjusted Profits

Profits	xx
+ Abnormal loss	xx
− Abnormal Gain	(xx)
− Omission of Expense	(xx)
+ Omission of Income	xx
± Rectification of Errors	xx/(xx)
	xx

Method:2 Super Profits Method

G/w = Super Profits (SP) X No. of Years of Purchase

SP = Average Profits (AP) − Normal Profits (NP)

NP = Capital Employed (CE) X Rate of Return (r%)

CE = Total Assets − Outsider Liabilities
(excl. Fictitious Assets & Non Trade Investments)

Method:3 Annuity Method

G/w = Super Profits X Annuity Factor (A.F.)

$$A.F. = \sum PVF(r\%, n)$$

PVF : Present value Factor
r% : Rate of Return
n : No. of Years

Method:4 Capitalisation Method

Capitalisation Method

- Capitalisation of Average Profits

  G/w = Capitalised value of business (CVB) - Capital Employed

  $$CVB = \frac{\text{Avg. Profits}}{r\%}$$

- Capitalisation of Super Profits

  $$G/w = \frac{\text{Super Profits}}{r\%}$$

<u>Sometimes Question specifies to apply Average Capital Employed</u>

Average Capital Employed = $\frac{\text{Opening Capital Employed + Closing Capital Employed}}{2}$

Example 1

A and B are partners in a firm sharing profits and losses equally. On 31st March, 2021, total assets of the firm were 8,00,000 & outsider liabilities were 3,00,000. The profits of the firm for the last 3 years were 1,30,000, 1,50,000 & 1,28,000 The rate of normal profit is 20%. On 1st April, 2021 they agreed to admit C as a partner for 1/4th share. C will bring Rs. 1,00,000 as capital.

Compute value of the goodwill of firm on admission of C, if it is to be calculated on the basis of:

a) 3 years purchase of average profit.
b) 3 years purchase of super profit
b) 3 years purchase of super profit if discounting rate is 8%
d) Capitalization method

Solution

Average Profits = (1,30,000+1,50,000+1,28,000)/3 = 1,36,000
Capital Employed = 8,00,000 – 3,00,000 = 5,00,000

a) 3 years purchase of average profits

Goodwill = 3 × Average profit = 3 × Rs. 1,36,000 = Rs. 4,08,000

b) 3 years purchase of super profit

Average profit	1,36,000
Less : Normal profit @ 20% of 5,00,000	(1,00,000)
Super profit	36,000

Value of Goodwill = 3 ×Super profit = 3 × Rs. 36,000 = Rs. 1,08,000

c) Annuity Method:
Annuity Factor for 3 years at 8% = 0.926+0.857+0.794 = 2.577
Goodwill = 36,000*2.577 = 92,772

d) Capitalization of Average Profits method

$$\text{Normal value of business} = \frac{\text{Average profit}}{\text{Normal rate of profit}} = \frac{1,36,000}{20\%} = \text{Rs. } 6,80,000$$

Normal value of business	6,80,000
Less: Actual capital employed	(5,00,000)
Value of goodwill of the firm will be	**1,80,000**

Capitalization of Super Profits method

$$\text{Goodwill} = \frac{\text{Super profit}}{\text{Normal rate of profit}} = \frac{36,000}{20\%} = 1,80,000$$

Example 2

The profits and losses for the previous years are: 2018 Profit Rs. 10,000, 2019 Loss Rs. 17,000, 2020 Profit Rs. 50,000, 2021 Profit Rs. 81,000. The average Capital employed in the business is Rs. 2,00,000. Market Rate of interest on investment 9% & Rate of risk return on capital invested in business 1%

The remuneration from alternative employment of the proprietor is Rs. 6,000 p.a. Calculate the value of goodwill on the basis of 2 years' purchases of Super Profits based on the average of 3 years.

Solution

Total Profit for 3 years = (Rs. 17,000) + Rs. 50,000 + Rs. 81,000 = Rs. 1,14,000.
Average profits = Total Profits/No. of years = 1,14,000/3 = Rs. 38,000
Average Profits for Goodwill = Rs. 38,000 – Proprietor Remuneration
= Rs. 38,000 – Rs. 6,000
= Rs. 32,000
Normal Profit=Interest on Capital employed = Rs. 20,000 (i.e. Rs. 2,00,000 x10/100) = Rs. 20,000
Super Profit = Average Profit-Normal Profit = Rs. 32,000 – Rs. 20,000 = Rs. 12,000
Goodwill = Super Profit x 2 = Rs. 12,000 x 2 =Rs. 24,000

Treatment of Goodwill in case of change in PSR

Accounting Issue involved	Journal Entry
1. Writing off Goodwill existing in books	All Partner's Capital A/c (individually) Dr. (in **old ratio**) To Goodwill A/c
2. Adjusting Goodwill on change in PSR	Gaining Partner's Capital A/c Dr. (**Gain ratio**) To Sacrificing Partners' Capital A/c (**Sacrifice Ratio**)

Note: Only Purchased Goodwill should be shown in the books of accounts. Other Goodwill value, if any in the Balance sheet, should be written off from the books of accounts.

Sacrifice	Gain
Partners whose shares in Profit have decreased as a result of change in PSR, are known as **Sacrificing Partners.**	Partners whose shares in profits have increased as a result of change in PSR, are known as **Gaining Partners**
The ratio in which Partners have agreed to reduce their profits in favour of the other Partner(s) is called **Sacrifice Ratio or Sacrificing Ratio.**	The ratio in which Partners have agreed to gain their profits from the other Partner (s) is called **Gain Ratio or Gaining Ratio**
Sacrifice Ratio = Old Ratio **less** New Ratio	**Gain Ratio** = New Ratio **less** Old Ratio

Question

A, B & C are equal partners. They wanted to change the profit sharing ratio into 4:3:2. Goodwill of the firm is valued at ₹ 90,000. Pass necessary journal entry for goodwill adjustment.

Solution

Journal Entries

Date	Particulars	L.F.	Dr. Amount	Cr. Amount
	A's Capital A/c - Dr. To C's Capital A/c (Being the adjustment for goodwill through the Partners' Capital Accounts)		10,000	 10,000

Working Notes:

Particulars	A	B	C
Credit in Old Ratio (1:1:1)	30,000	30,000	30,000
Debit in New Ratio (4:3:2)	40,000	30,000	20,000
	10,000 Dr.	**-**	**10,000 Cr.**