

CH-10Unit-1Introduction to Partnership Accounts

Part + ownership

Governed by $\rightarrow$ Indian Partnership 1932

Basic Characteristics

Companies Act 2013

① No. of Partners $\rightarrow$ Min. = 2

Max. = 50 & LLP = Unlimited

② Agreement

 $\rightarrow$ Partnership Deed (can be oral or written)

Agree + arrangement

L In absence of Deed
provision of Partnership Act,
1932 shall apply ~~1932~~

③ Sharing of Profit

④ Mutual Agency $\rightarrow$ Act done by all or any of them acting
for all.⑤ Unlimited Liability $\rightarrow$ (except LLP)⑥ Decision Making $\rightarrow$ Regular Business $\rightarrow$ Major Decision $\rightarrow$ 100%⑦ Business Activity $\rightarrow$ i.e., no charitable work, aim Profit earning

Accounting Provisions (When Deed is absent or silent)

Dispute on —> Check with Deed

Some Matter

Ex. Salary to Partner

[If Deed is absent or silent]

Follow the provisions of Partnership Act 1932.

1. Profit Sharing Ratio —> Equal
2. Salary / Comm. / Brokerage —> Not allowed
3. Int. on Capital & Drawing —> Not allowed
4. Int. on Loan by Partner —> 6% p.a.

+ to Firm

[Liab. side wala]

Accounting Procedure

Charge
Vs
App.

Profit & Loss A/c $\xrightarrow{\text{Net Profit (N.P.)}}$ P & L App. A/c

↓

Charge against Profit

- # Int. on Loan by Partner
- # Rent to Partner

↓

Extension of P & L A/c

- # Profit Distribution to Partner

Capital A/c of Partners

Capital + Add. Capital
- Capital Reduction

Fixed Capital

(a) Capital A/c

(b) Current A/c

- Current Capital
- Reserve Distribution
- Revaluation, P&L
- Goodwill Adjustment

Fluctuating Capital

(a) Capital A/c

◦ a + b of Fixed Capital

Topics to be discussed

- ① Fundamentals → Calculation for SOC, DOD, Guarantee
- ② Goodwill Calculation → Avg. Profit
Weighted avg. Profit
Super Profit
Capitalisation
Annuity
- ③ Admission of Partner
- ④ Retirement of Partner
- ⑤ Death of Partner
- ⑥ Dissolution of Partnership Firm
 - Solvency
 - Insolvency
 - Piece Meal Distribution

FUNDAMENTALS

Cal. for IOD-2①

Drawings

Regular

Ex) Withdraw ₹ 20,000 at
end of every month

Random

Ex) 1 Jan. = 20,000

1 April = 10,000

30 Oct. = 50,000

$$\text{IOD} = \frac{\text{Total Drawing} \times \text{Rate}}{100} \times \frac{\text{Avg. Time}}{12}$$

$$\text{Avg Time} = \frac{\text{Time left after (1}^{\text{st}} \text{ Drawing + Last Drawing)}}{2}$$

Ex. 1 Mr. A withdraw ₹ 2,000 Per month at starting of every month. IOD @ 12% p.a.

Solve-

$$\text{IOD} = \frac{\text{Total Drawing} \times \text{Rate}}{100} \times \frac{\text{Avg. Time}}{12}$$

$$\text{IOD} = 24,000 \times \frac{12}{100} \times \frac{6.5}{12}$$

$$\text{IOD} = ₹ 1,560$$

$$\text{Avg. Time} = \frac{\text{Time left after (1}^{\text{st}} \text{ Drawing + Last Drawing)}}{2}$$

$$= \frac{12 + 1}{2} = 6.5$$

Ex. 2 Mr. B withdraw ₹ 10,000 per month at the end of every month. Calculate IOD @ 12% p.a.

Solve-
$$\text{IOD} = \text{Total Drawings} \times \frac{\text{Rate}}{100} \times \frac{\text{Avg. Time}}{12}$$

$$\text{IOD} = 1,20,000 \times \frac{12}{100} \times \frac{5.5}{12}$$

$$\boxed{\text{IOD} = 6,600}$$

$$\text{Avg. Time} = \frac{\text{Time left after (1st Drawing + Last Drawing)}}{2}$$

$$= \frac{11 + 0}{2} = 5.5$$

Ex. 3 Mr. Z withdraw ₹ 20,000 per Quarter at Beginning of every Quarter. Calculate IOD @ 12% p.a.

Solve-
$$\text{IOD} = \text{Total Drawings} \times \frac{\text{Rate}}{100} \times \frac{\text{Avg. Time}}{12}$$

$$\text{IOD} = 80,000 \times \frac{12}{100} \times \frac{7.5}{12}$$

$$\boxed{\text{IOD} = 6,000}$$

$$\text{Avg. Time} = \frac{\text{Time left after (1st Drawing + Last Drawing)}}{2}$$

$$= \frac{12 + 3}{2} = 7.5$$

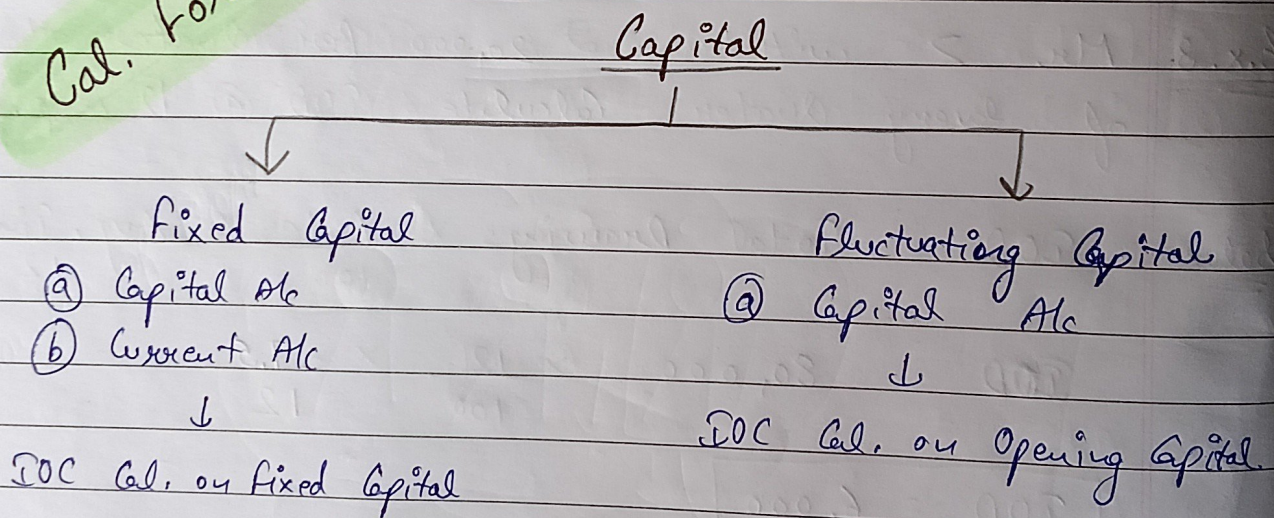
Random Drawing

$$\text{IOD} = \text{Drawing} \times \frac{\text{Rate}}{100} \times \frac{\text{Time of usage}}{12}$$

Ex 4-

1 Jan.	20,000	$\Rightarrow 20,000 \times \frac{12}{100} \times \frac{12}{12} = 2,400$
1 Feb.	15,000	$\Rightarrow 15,000 \times \frac{12}{100} \times \frac{11}{12} = 1,650$
30 April	50,000	$\Rightarrow 50,000 \times \frac{12}{100} \times \frac{8}{12} = 4,000$
Rate 12% p.a.		<u>8,050</u>
Jan. - Dec.		

Cal. for IOD



$$\text{Opening Cap.} = \text{Closing Capital}$$

(-) Reserves

(-) P & L

(+) Drawings

(-) Additional Drawings

$\neq$

Effective Capital Employed Method:

$$\text{EFC} \times \frac{\text{Rate}}{100} \times \frac{1}{12}$$

Partner ko cash main kuch nahi dete instead capital ↑ or ↓ kar dete hain

Capital = Liability
 ↑ Cr.
 ↓ Dr.

Capital Balance ↑

1. Additional Capital
2. I/O
3. Profit Distribution
4. Revaluation Profit
5. Goodwill share by New Partner
6. Salary / Commission

Capital Balance ↓

1. Drawings
2. I/O
3. Capital Withdrawal
4. Loss / Revaluation Distribution

Salary to Partner

M ₁	M ₂
Salary A/c I/Oc ...Dr.	P & L App. A/c ...Dr.
To PCA A/c	To PCA A/c
P & L App. A/c ...Dr.	
To Salary I/Oc A/c	

P&L APP. A/c

- ① Extension of P&L A/c
- ② Prepare to record appropriation or distribution among partners

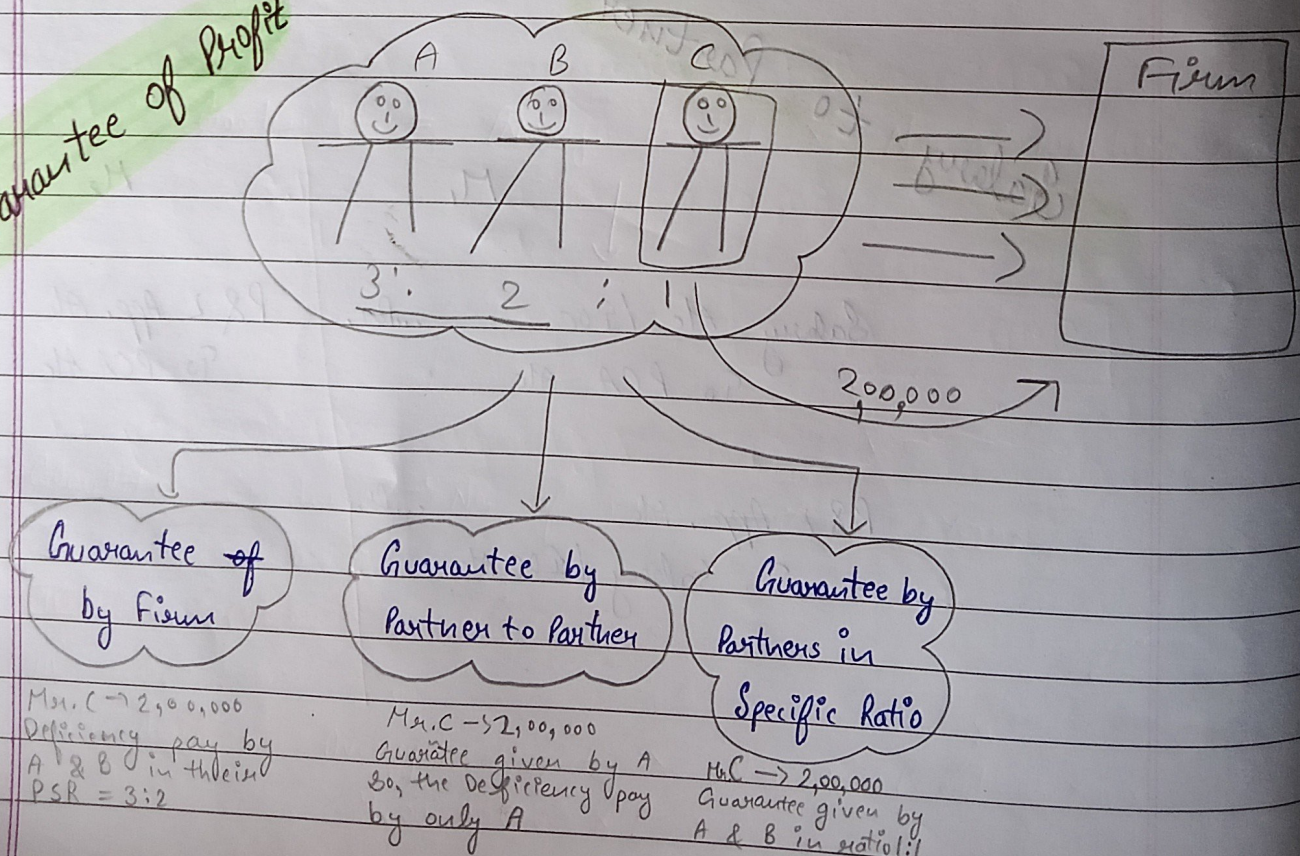
P&L APPROPRIATION A/c

Format

Dr.

Particulars	₹	Particulars	₹
To Salary A/c (Partner) (M ₁)		By Net Profit (P&L A/c)	
To PCA (Partner Salary) (M ₂)		By IOD	
To IOC		By P&L	
To Comm. BKR			
To General Reserve (Transfer)			
To PCA (Balance)			
old in Old			

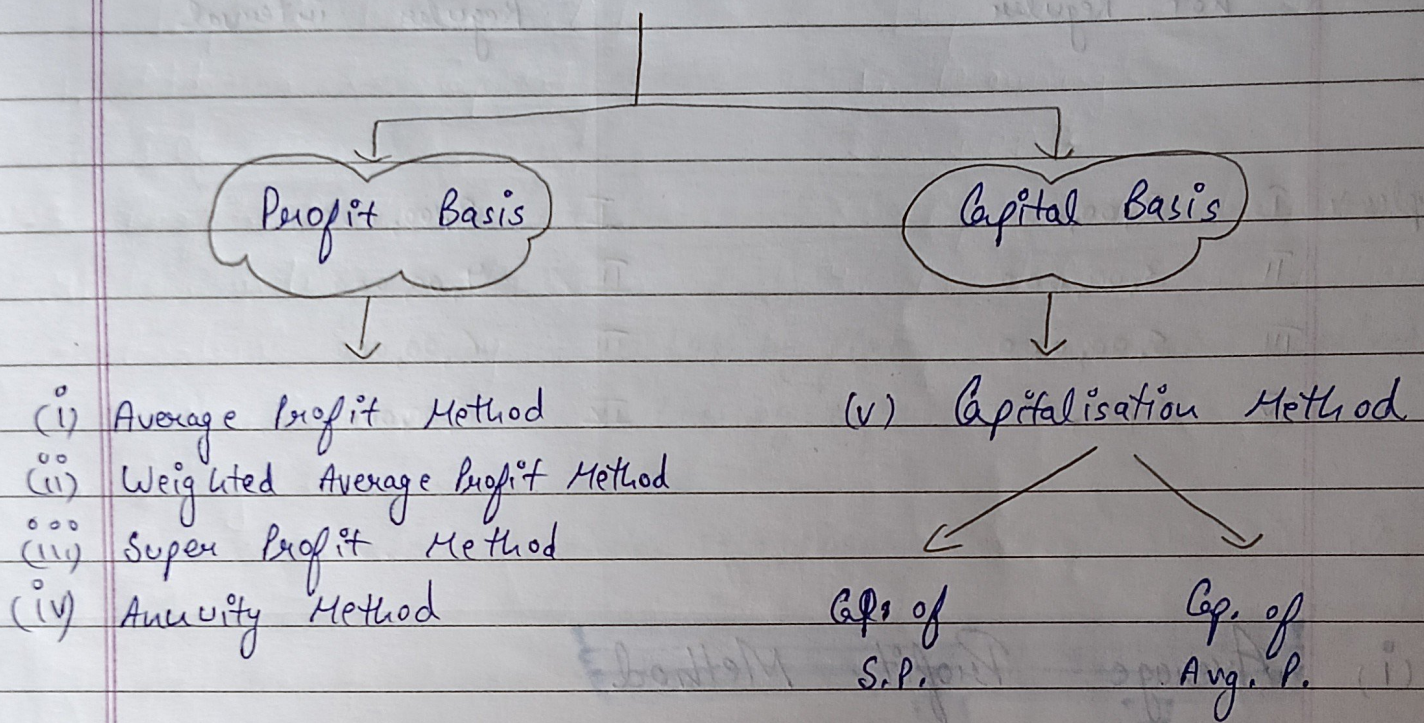
3★ Guarantee of Profit



Goodwill Calculation

Treatment

Goodwill Calculation



When to Calculate Goodwill ?

Any change in Partnership Structure i.e.

1. Change in PSR
2. Admission
3. Retirement
4. Death

How to Calculate Goodwill ? — Basis will be given in Q.

Average Profit and Weighted Average Profit

↓
When Profits is
not Regular

↓
When Profits is ↑ in
Regular interval

Examples - 1

I	2,00,000
II	3,00,000
III	5,00,000
IV	8,00,000

I	2,00,000
II	4,00,000
III	6,00,000
IV	8,00,000

(i) Average Profit Method

$$\text{Goodwill} = \text{Average Profit} \times \text{No. of Purchase Year}$$

↓

$$\frac{\text{Total Profit}}{\text{No. of Years}}$$

↓
(Given in Q. OR year)

Q1 Calculate Goodwill - No. of Purchase Years = 2 Years

$$I = 3,00,000$$

$$II = 6,00,000$$

$$III = 3,00,000$$

Solve -

$$\begin{aligned} \text{Goodwill} &= \text{Average Profit} \times \text{No. of Purchase Years} \\ &= 4,00,000 \times 2 \\ &= ₹ 8,00,000 \end{aligned}$$

$$\text{Average Profit} = \frac{\text{Total Profit}}{\text{No. of Years}} = \frac{3,00,000 + 6,00,000 + 3,00,000}{3} = ₹ 4,00,000$$

Q.2- Same as ques 1 but the adjustment is

I = Abnormal loss of 50,000

II = Abnormal gain of 50,000

Solve- Profit = Profit + Abnormal Loss - Abnormal Gain

↓

Loss by fire
Loss by theft

↓

Claim Received

$$\text{I} = 3,00,000 + 50,000 = 3,50,000$$

$$\text{II} = 6,00,000 - 50,000 = 5,50,000$$

$$\text{III} = 3,00,000$$

$$\text{Average Profit} = \frac{12,00,000}{3,00,000} = ₹ 4,00,000$$

$$\text{Goodwill of Firm} = 4,00,000 \times 2 = ₹ 8,00,000$$

(ii) Weighted Average Profit Method

$$\text{Goodwill} = \text{Weighted Average Profit} \times \text{No. of Purchase Years}$$

$$\downarrow$$

$$\frac{\sum \text{Weighted Profit}}{\sum \text{Weights}}$$

(iii)

Super Profit

$$\text{Goodwill} = \text{Super Profit} \times \text{No. of Purchase Years}$$

$$\begin{array}{c} \downarrow \\ \text{Actual Profit} \\ \text{OR} \\ \text{Average} \\ \downarrow \\ \text{[Given in Q.]} \end{array} \quad \begin{array}{c} \downarrow \\ \text{Actual - Normal Profit} \\ \downarrow \\ \text{Part. Cap.} \\ (+ \text{ Reserves} \\ + \text{ Non Current Liab.}) \\ \downarrow \\ \text{Capital Employed} \times \text{NRR} \\ \downarrow \\ \text{[Given in Q.]} \end{array} \quad \begin{array}{c} \downarrow \\ \text{[Given in Q.]} \end{array}$$

Total Assets
(- Current Liab.)

Q.1 Calculate goodwill through S.P. Method. No. of purchase year = 5 years

Capital of Partner A = 3,00,000

Capital of Partner B = 2,00,000

NRR = 10%

Profit of last 3 years = 3,00,000 ; 6,00,000 ; 9,00,000

Solve- Average Profit = $\frac{3,00,000 + 6,00,000 + 9,00,000}{3} = \frac{18,00,000}{3} = ₹ 6,00,000$

Normal Profit = $\frac{[3,00,000 + 2,00,000] \times 10}{100} = ₹ 50,000$

Super Profit = $6,00,000 - 50,000$
= ₹ 5,50,000

Goodwill of firm = $5,50,000 \times 5$
= ₹ 27,50,000

(iv) Annuity Method

$$\text{Goodwill} = \text{Super Profit} \times \text{Annuity Value}$$

Actual

$$\text{Annuity Value} \rightarrow PV [1 + \text{Int. rate}]^n = FV$$

- ① Int. Rate, Value $\Rightarrow 12\%$
- ② No. of Purchase Year $\Rightarrow 3$ Years
- ③ A.V. $= \frac{1}{1.12} = = = GT$

If 15%
& 5 years
↓

$$\frac{1}{1.15} = = = GT$$

Stock

Rectification (sahi karna kr)
Effect on P&L

Overvalued C/S	↑	↓
Undervalued C/S	↓	↑
Overvalued O/S	↑	↑
Undervalued O/S	↓	↓

(v) Capitalisation Method

Method ①

$$\text{Goodwill} = \text{SP} \times \frac{100}{\text{NRR}}$$

Method ②

$$\text{Goodwill} = \text{CAP} - \text{Capital employed}$$

$$\text{Capitalised value of Average Profit} = \frac{\text{Average Profit} \times 100}{\text{NRR}}$$

Admission of Partner

Ratio ka khel

Case I (Standard Case)

A : B C $\leftarrow$ $\frac{1}{4}$ th share (No info.)
3 : 2

Sacrificing Ratio = Old Ratio
= 3 : 2

Calculation for New Ratio

Total Share = 1

Remaining Share = 1 - New Partner's Share

Remaining Partner ~~Share~~ Remaining Share $\times$ Old Ratio of Partners

Q.1- A : B : C
2 : 3 : 5

D $\leftarrow$ $\frac{1}{5}$ share

Cal. Sac. Ratio and
New Ratio

Remaining Share = $1 - \frac{1}{5} = \frac{4}{5}$

$$A = \frac{2}{5} \times \frac{4}{5} = \frac{8}{25}$$

$$B = \frac{3}{5} \times \frac{4}{5} = \frac{12}{25}$$

$$C = \frac{5}{5} \times \frac{4}{5} = \frac{20}{25}$$

$$D = \frac{1}{5} \times \frac{4}{5} = \frac{4}{25}$$

New Ratio = 8 : 12 : 20 : 4 & Sacrificing Ratio = 2 : 3 : 5

Case II (Conditional Admission)

Type (a) New Partner Ratio is Given $\rightarrow$

A:B

3:2

C $\frac{1}{5}$ th Share which he takes equally

from A & B

New Ratio

$$A = \frac{3}{5} - \left[\frac{1 \times 1}{5 \times 2} \right] = \frac{3}{5} - \frac{1}{10} = \frac{5}{10}$$

$$B = \frac{2}{5} - \left[\frac{1 \times 1}{5 \times 2} \right] = \frac{2}{5} - \frac{1}{10} = \frac{3}{10}$$

$$C = \frac{1}{5} \times \frac{2}{2} = \frac{2}{10}$$

$$A:B:C = 5:3:2$$

$$\text{Sacrificing Ratio} = \text{Equally} \\ = 1:1$$

$$\text{New Ratio} = \text{Old Ratio} - \text{Sacrificing Ratio}$$

$$\text{Sacrificing Ratio} = \text{Old Ratio} - \text{New Ratio}$$

Required $\Rightarrow$ (1) Goodwill Adjustments

(2) Profit / Reserve not want to distribute

A:B $\rightarrow$ 3:2 C in such a way that the ratio b/w B & C will be same as it was b/w A & B. Answer: 1:1

$$A : B : C$$

3 2
↓
3 2

9 : 6 : 4

BY $\rightarrow$ री
TO $\rightarrow$ तक

Revaluation A/c

- > Also known as P&L Adjustment A/c
- > Record the change in the value of Asset and Liability of firm.
- > Prepare at time of Reconstitution of partnership.
- > Balance distributed in Partners Capital A/c old in old.

formate

REVALUATION A/c		P&L ADJUSTMENT A/c	
Particulars	₹	Particulars	₹
Liability ↑ Asset ↓		Asset ↑ Liability ↓	
Unrecorded Liability		Unrecorded Asset	

Balance Sheet

Balance Transfer to PCA Old in Old

 $A \uparrow = Dr$, $A \downarrow = Cr$ $L \uparrow = Cr$, $L \downarrow = Dr$ Basic Journal Entries

①	↑ in value of Assets / Unrecorded Ass.	①	↑ in value of Liability / Unrecorded Lia.
	Asset A/c		Revaluation A/c
	To Revaluation A/c		To Liability A/c
②	↓ in value of Asset	②	↓ in value of Liability
	Revaluation A/c		Liability A/c
	To Asset A/c		To Revaluation A/c

Balance Sheet of Firm

→ Adj. for change in val. of Asset/Liability

In New B/S want to Record Changes

↓
Revaluation A/c

In new B/S do not want to record changes

↓
Option I → Memorandum Revaluation A/c

Option II → Adjustment

entries

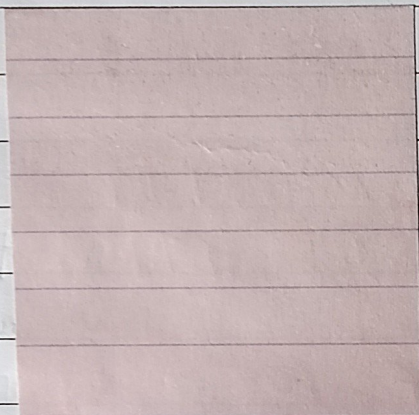
Old Ratio $\longrightarrow$ New Ratio
 $A:B$
 $3:2$ $1:1$

① PSR $\longrightarrow$

② Admission $A:B$
 $3:2$ $\longrightarrow$ $A:B:C$
 $2:2:1$

★★ Partners do not want to change B's Values

Option F



Memorandum Revaluation

Tina

3:2

Jassi

Pinku

New PSR = 5:3:2

	BV	MV	Gain
Machine	1,00,000	1,20,000	20,000
Furniture	40,000	50,000	10,000
Stock	20,000	20,000	—
Creditors	10,000	8,000	2,000
			<u>32,000</u>

$\longrightarrow$ NOT TO RECORD Revised Value of Assets & Liab.

Op. II Adj. Entry

Dr.	
Gainig Par.	
To Sac. Par.	

Op. I

Memorandum Revaluation A/c

Dr.

To Assets [↓]
 To Liab. [↑]
 To Gain on Revaluation
 [Old Par. - Old Ratio]

To Assets [↑]
 To Liab. [↓]

By Assets [↑]

By Liab. [↓]

By Assets [↓]

By Liab. [↑]

By Loss on Revaluation
 [New Ratio - All par.]

Journal

1. Memo. Rev. A/c

To Asset [↓]

To Liab. [↑]

2. Asset [↑]

Liab. [↓]

To Memo. Rev. A/c

3. Memorandum Rev. A/c

To Old Par. Cap.
 [Old Ratio]

4. Asset [↓]

Liab. [↑]

To Memo. Rev. Alc

5. Memo. Rev. Alc

To Asset [↑]

To Liab. [↓]

6. All partner Cap. Alc — (New Ratio)

To Memo. Rev. Alc

→ HIDDEN GOODWILL

	A : B	C
	3 : 2	$\frac{1}{5}$ th share
	1,00,000	2,00,000
		1,00,000

Step. 1 Total Capital on basis of New Partner

$$\Rightarrow 1,00,000 \times 5 \left[\begin{array}{l} \text{Reciprocal} \\ \text{of C's} \\ \text{Share} \end{array} \right]$$

$$= 5,00,000$$

Step. 2 Actual Capital of Firm

$$= \begin{array}{rcl} A & - & 1,00,000 \\ B & - & 2,00,000 \\ C & - & \underline{1,00,000} \\ & & 4,00,000 \end{array}$$

$$\text{Goodwill of Firm} = 5,00,000 - 4,00,000$$

$$= ₹ 1,00,000$$

$$\text{C's share of Gw} = \frac{1}{5} \times 1,00,000$$

$$= ₹ 20,000$$

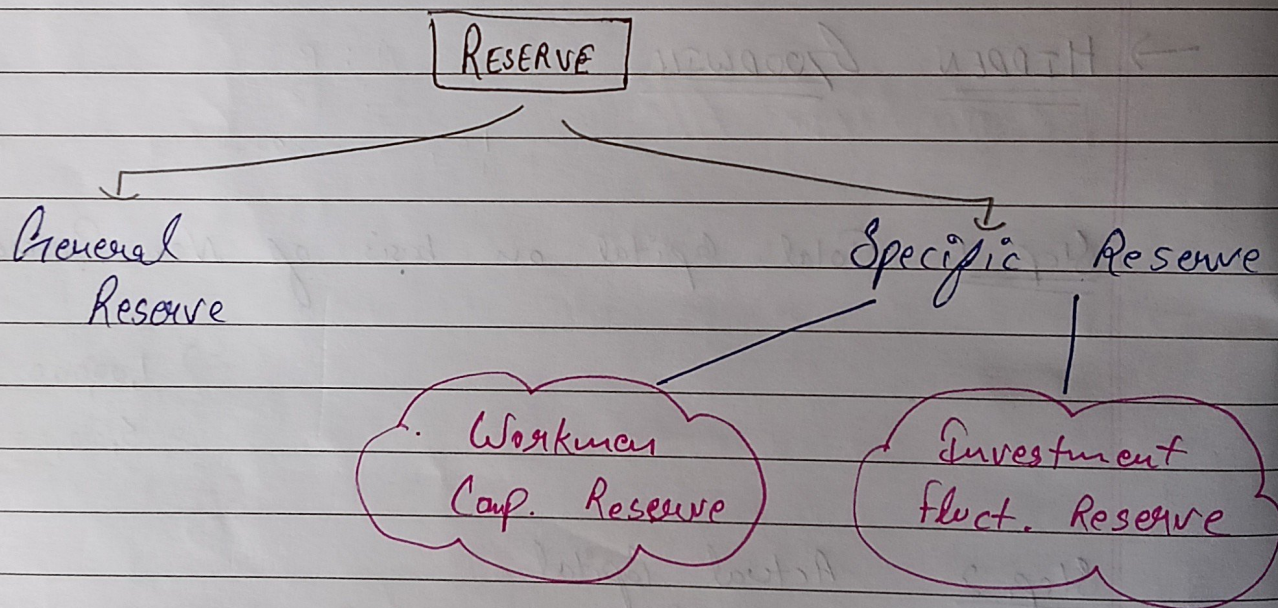
→ Reserves

Reserve
↓

Distributed b/w old partners
in old Ratio

Journal

Reserves A/c Dr.
To Old Partners



1. Workmen Compensation Reserve

a. WCR = ₹ 20,000

NO Impo.

WCR

To Old Partners
[in old Ratio]

20,000

20,000

b. WCR = ₹ 20,000
 Workmen Compensation Claim = ₹ 12,000

Can combine the entry

→ WCR Dr.	12,000
To WCC	12,000
→ WCR Dr.	8,000
To Old Part.	8,000

c. WCR - ₹ 100,000
 WCC - ₹ 20,000

→ WCR Dr.	20,000
To WCC	20,000

d. WCR - 20,000
 WCC - 25,000

→ Revaluation

WCR	Dr 20,000	Loss shared b/w old Part.
To WCC		25,000

→ Adjustment of Capital

When old partners capital are to be adjusted on the basis of New

Partners

When New Partner will bring Proportionate Capital

Step 1: Take New Partner Cap.

Step 2: Take New Partner Share

Step 3: Calculate Total Capital

$$= \text{New Par. Cap.} \times \text{Reciprocal of New Par. Share}$$

Step 4: Distribute this capital in New Ratio

Step 1: Let Total Share = 1

Step 2: Remaining Share = 1 - NP Share

Step 3: Calculate Total Capital

$$= \text{Capital of Partners [After Adjustment]} \times \text{Reciprocal of Remaining Share}$$

Step 4: Distribute or take out New Partners' Capital

If Par. brings
add Cap.

Bank A/c	Dr
to Par. Cap.	

If Par. Withdraws
Cap.

Par. Cap.	Dr
to Bank A/c	