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Retirement / Death of a Partner

1. Introduction

Retirement of a partner means retiring as a partner from a firm. As per Indian Partneship Act; 1932, when a partner retires from a firm for any reason or a partner dies, the partnership ends but the firm is not dissolved. Remaining partners can continue the firm and its business. For this purpose necessary accounting treatments of retirement are required to be given in the books of the firm. In this situation a partnership is reconstituted (reconstructed).

2. Circumstances of Retirement of a Partner

The circumstances of retirement of a partner can be divided into two parts :

(A) As per Indian Partnership Act

(B) Voluntary retirement of a partner due to his personal reasons

(A) As per Indian Partnership Act : As per Indian Partnership Act, partner can retire from the firm due to any of following reasons :

(1) Unanimously : Any partner can retire by unanimous consent of all the partners.

(2) By notice : A partner has right to retire from the firm by giving notice to other partners in writing indicating his intention of retirement from the firm.

(3) By contract : Any partner can retire as per the conditions of the partnership deed.

(4) Insolvency of a partner : A partnership of any partner ends from the date from which he is declared insolvent.

(5) Death of a partner : Partnership ends automatically due to the death of a partner.

(6) Expulsion by other partners : Subject to provision in partnership deed, a partner can be expelled by other partners.

(B) Voluntary retirement of a partner due to his personal reasons : A partner can decide to retire from the partnership due to his personal reasons. An active partner is required to give public notice regarding his retirement; otherwise he is responsible for the liabilities towards third parties arising from the activities after his retirement.

3. Important Accounting Aspects and Accounting Treatments

Following accounting aspects and accounting treatments are required to be taken into consideration when on the date of retirement a partner retires or dies and remaining partners decide to continue the business of the firm.

(1) Calculation of new profit-loss sharing ratio and calculation of gaining share of continuing partners.

(2) Valuation of goodwill and its accounting treatment.

(3) Revaluation of assets and liabilities.

(4) Distribution of accumulated reserves and balances of undistributed profits and losses.

(5) Determination of amount payable to the retiring or deceased partner.

(6) Payment of amount due to the retiring or deceased partner.

4. Calculation of New Profit and Loss Sharing Ratio and Gaining Ratio

When a partner retires or dies and the remaining partners continue the business of the firm, the new ratio of continuing partners is decided. The same way, the profit share of the retiring partner is distributed between the continuing partners. Consequently the gaining share of the continuing partners comes into existence. Now let us understand how the new profit sharing ratio and the gaining ratio is calculated.

Calculation of new profit-loss sharing ratio : Due to the retirement of a partner his profit share is distributed among the remaining continuing partners and therefore they are benefited in terms of profit share. Hence it becomes necessary to calculate the new profit-loss sharing ratio of the remaining partners. New share of continuing partners is obtained by adding their gain to their old share.

$\therefore$ New share = Old share + Gain and

Gain = New share − Old share

New profit-loss sharing ratio can be calculated as per the following circumstances :

(1) When gaining ratio or gain is not given, means old ratio is continued

(2) When gaining share of continuing partners is given

(3) When gaining ratio of continuing partners is given

(4) When old and new profit and loss sharing ratios are given

Now let us discuss the calculation of new profit sharing ratio in detail :

(1) **When gaining ratio or gain is not given, means old ratio is continued :** When the ratio in which the retiring partners' share is to be distributed among the continuing partners is not given, it is assumed that the continuing partners will continue to share the profit or loss in their respective old profit and loss sharing ratio. It means their old ratio will become the new ratio. In this situation new ratio of continuing partners becomes their old ratio by eleminating retiring partner's share.

Illustration 1 : M, N and O are the partners sharing profit and loss in the ratio of 4:3:2. Calculate new profit-loss sharing ratio under the following circumstances,

if (i) M retires

(ii) N retires

(iii) O retires

Ans. : Old ratio of M, N and O is 4:3:2.

(i) If M retires new profit and loss sharing ratio between N and O will be 3:2.

(ii) If N retires then new profit and loss sharing ratio of M and O will be 4:2 that is 2:1.

(iii) If O retires then new profit and loss sharing ratio of M and N will be 4:3.

Here the gaining ratio will be the old ratio of partners.

Gain = New share − Old share

When M retires :

	M		N		O
Old ratio :	4	:	3	:	2
New ratio :	Retired	:	3	:	2

N's gain $= \frac{3}{5} - \frac{3}{9} = \frac{27-15}{45} = \frac{12}{45}$

O's gain $= \frac{2}{5} - \frac{2}{9} = \frac{18-10}{45} = \frac{8}{45}$

∴ Gaining ratio of N and O = 12:8 i.e. 3:2.

Similarly when N retire the gaining ratio of M and O will be 2:1 and when O retires the gaining ratio of M and N will be 4:3.

Illustration 2 : M, N and O are the partners sharing profit and loss in the ratio of $\frac{4}{9}$, $\frac{1}{3}$ and $\frac{2}{9}$. Find out the new profit and loss sharing ratio under the following cases :

if (i) M retires

(ii) N retires

(iii) O retires

Ans. : Old profit and loss sharing ratio of M, N and O is $\frac{4}{9} : \frac{1}{3} : \frac{2}{9}$. Taking LCM, the ratio $= \frac{4}{9} : \frac{3}{9} : \frac{2}{9}$ i.e. 4:3:2. The new profit and loss sharing ratio in given circumstances will be as follows (Calculation will be the same as it is in illustration 1).

(i) If M retires then new profit and loss sharing ratio of N and O = 3:2.

(ii) If N retires then new profit and loss sharing ratio of M and O = 4:2 means 2:1.

(iii) If O retires then new profit and loss sharing ratio of M and N = 4:3.

Explanation : In the above illustrations if we calculate gaining ratio of the continuing partners,

Gain = New share − Old share

Under circumstances (i) if M retires,

	M		N		O
Old ratio	4	:	3	:	2
∴ Old share	$\frac{4}{9}$	:	$\frac{3}{9}$	:	$\frac{2}{9}$

On retirement of M, new ratio of N and O = 3:2

∴ New share of N and O $= \frac{3}{5} : \frac{2}{5}$

$\therefore$ Gain = New share − Old share

N's Gain = $\frac{3}{5} - \frac{3}{9} = \frac{27-15}{45} = \frac{12}{45}$

O's Gain = $\frac{2}{5} - \frac{2}{9} = \frac{18-10}{45} = \frac{8}{45}$

$\therefore$ Gaining ratio of N and O is $\frac{12}{45} : \frac{8}{45}$ means 12:8 or 3:2.

Thus, old ratio of N and O becomes their gaining ratio. Therefore,

Under circumstances (ii), if N retires, gaining ratio of M and O will be their old ratio 4:2 i.e. 2:1.

Under circumstances (iii), if O retires, gaining ratio of M and N will be their old ratio 4:3.

Note : Thus, by observing the above illustration we can say that when old profit and loss sharing ratio of remaining partners is continued even after the retirement of a partner, their gaining ratio also will be the same as old ratio. (Similar situation arises on the admission of a partner. Here gaining ratio is obtained while sacrificing ratio is obtained on admission. See illustration 1, chapter 4.)

(2) **When gaining share of the continuing partners is given :** When gaining share of continuing partners is given out of the retiring partners' share, new profit and loss sharing ratio will be calculated as under :

New share = Old share + Gain

Illustration 3 : X, Y and Z are the partners sharing profit and loss in the ratio of 3:2:1. Y retires as a partner. X gain $\frac{1}{9}$th share and Z gains $\frac{2}{9}$th share from the profit and loss share of Y. Calculate the new profit and loss sharing ratio of X and Z.

Ans. : Old ratio of X, Y and Z = 3:2:1

X gains $\frac{1}{9}$th share and Z gains $\frac{2}{9}$th share from $\frac{2}{6}$ share of Y.

$\therefore$ Gain of X = $\frac{1}{9}$ and Gain of Z = $\frac{2}{9}$. $\therefore$ Gaining ratio is 1:2.

New share = Old share + Gain

$\therefore$ X's new share = $\frac{3}{6} + \frac{1}{9} = \frac{9}{18} + \frac{2}{18} = \frac{11}{18}$

Z's new share = $\frac{1}{6} + \frac{2}{9} = \frac{3}{18} + \frac{4}{18} = \frac{7}{18}$

$\therefore$ New profit and loss sharing ratio of X and Z = 11:7

(3) **When gaining ratio of the continuing partners is given :** When the gaining ratio of continuing partners is given to distribute profit and loss share of the retiring partner, new profit and loss sharing ratio can be calculated as under :

First of all calculate gaining share of continuing partners by distributing retiring partners' share.

Gaining share of continuing partner = Share of the retiring partner × gaining share given to the respective partners

e.g. A, B and C are the partners sharing profit and losses in the ratio of 3:2:1. 'A' retires and his share is distributed between B and C in the ratio of 1:4.

A's share = $\frac{3}{6}$

A's $\frac{3}{6}$ share will be distributed by B and C in the ratio of 1:4.

So, B's gain $= \frac{3}{6} \times \frac{1}{5} = \frac{3}{30}$

C' gain $= \frac{3}{6} \times \frac{4}{5} = \frac{12}{30}$

So, gaining ratio of B and C = 1:4

Thereafter new profit and loss sharing ratio of B and C will be calculated as under :

New share = Old share + gain

$\therefore$ B's new share $= \frac{2}{6} + \frac{3}{30} = \frac{10}{30} + \frac{3}{30} = \frac{13}{30}$

C's new share $= \frac{1}{6} + \frac{12}{30} = \frac{5}{30} + \frac{12}{30} = \frac{17}{30}$

$\therefore$ New profit and loss sharing ratio of B and C = 13:17

Illustration 4 : O, B and C are the partners sharing profit and loss in the ratio of 4:5:1. O retires and his share is gained by B and C in the ratio of 1:4. Calculate new profit and loss ratio of B and C.

Ans. : Old ratio of O, B and C = 4:5:1

O's share is $\frac{4}{10}$ which is gained by B and C in the ratio of 1:4.

Gain = Retiring partners' share $\times$ Share of gaining ratio

B's Gain $= \frac{4}{10} \times \frac{1}{5} = \frac{4}{50}$

C's Gain $= \frac{4}{10} \times \frac{4}{5} = \frac{16}{50}$ So, gaining ratio of B and C = 1:4

New share = Old share + Gain

B's new share $= \frac{5}{10} + \frac{4}{50} = \frac{25}{50} + \frac{4}{50} = \frac{29}{50}$

C's new share $= \frac{1}{10} + \frac{16}{50} = \frac{5}{50} + \frac{16}{50} = \frac{21}{50}$

$\therefore$ New profit and loss sharing ratio of B and C = 29:21

Explanation : In the same illustration if B's gain $\frac{4}{50}$ and C's gain $\frac{16}{50}$ is given instead of gaining ratio 1:4, there is no need to calculate the gaining share of the continuing partners and new profit and loss sharing ratio can be calculated directly as under.

New share = Old share + Gain

$\therefore$ B's new share $= \frac{5}{10} + \frac{4}{50} = \frac{25}{50} + \frac{4}{50} = \frac{29}{50}$

C's new share $= \frac{1}{10} + \frac{16}{50} = \frac{5}{50} + \frac{16}{50} = \frac{21}{50}$

$\therefore$ New profit and loss sharing ratio of B and C = 29:21.

Note : Thus observing above, it can be seen that the gaining ratio and the gaining share are two different things. When gaining ratio is given, it is necessary to calculate first gaining share and new share can be calculated thereafter only. While new profit and loss sharing ratio can be directly calculated when the gaining share is given.

Illustration 5 : P, Q and R are the partners sharing profit and loss in the ratio of $\frac{1}{4}$, $\frac{1}{3}$ and $\frac{5}{12}$. Q retires. P and R decided to distribute Q's share in the ratio of 2:1. Calculate profit-loss sharing ratio of P and R.

Ans. : Old ratio of P, Q and R $= \frac{1}{4} : \frac{1}{3} : \frac{5}{12}$

Making LCM equal, the ratio is $\frac{3}{12} : \frac{4}{12} : \frac{5}{12}$.

Q retires and his share $\frac{4}{12}$ is gained by P and R in the ratio of 2:1.

$\therefore$ P's gain $= \frac{4}{12} \times \frac{2}{3} = \frac{8}{36}$

$\therefore$ R's gain $= \frac{4}{12} \times \frac{1}{3} = \frac{4}{36}$

Now, New share = Old share + Gain

$\therefore$ P's new share $= \frac{3}{12} + \frac{8}{36} = \frac{9}{36} + \frac{8}{36} = \frac{17}{36}$

R's new share $= \frac{5}{12} + \frac{4}{36} = \frac{15}{36} + \frac{4}{36} = \frac{19}{36}$

$\therefore$ New profit and loss sharing ratio of P and R = 17:19

Illustration 6 : R, B and I are the partners sharing profit and loss in the ratio of 5:4:3. B retires and $\frac{1}{4}$th share of B is acquired by R and remaining share is acquired by I. Find out new profit and loss sharing ratio of R and I.

Ans. : Old ratio of R, B and I $= \frac{5}{12} : \frac{4}{12} : \frac{3}{12}$

B retires and $\frac{1}{4}$ of his share $\frac{4}{12}$ is acquired by R.

$\therefore$ R's gaining share $= \frac{4}{12} \times \frac{1}{4} = \frac{4}{48} = \frac{1}{12}$

B's $\frac{1}{4}$th share is obtained by R, therefore $\frac{3}{4} \left(1 - \frac{1}{4}\right)$ share will be obtained by I.

$\therefore$ I's gain $= \frac{4}{12} \times \frac{3}{4} = \frac{12}{48} = \frac{3}{12}$

$\therefore$ Gain of R and I $= \frac{1}{12}$ and $\frac{3}{12}$

$\therefore$ Gaining ratio is 1:3.

New share = Old share + Gain

$\therefore$ R's new share $= \frac{5}{12} + \frac{1}{12} = \frac{6}{12}$

I's new share $= \frac{3}{12} + \frac{3}{12} = \frac{6}{12}$

$\therefore$ New profit and loss sharing ratio of R and I $= \frac{6}{12} : \frac{6}{12} = 1:1$

Illustration 7 : M, N and C are the partners sharing profit and loss in the ratio of $\frac{1}{3}$, $\frac{1}{2}$ and $\frac{1}{6}$. C retires and his share is taken up by M. Calculate the new ratio of profit and loss sharing of M and N.

Ans. : Old sharing ratio of M, N and C $= \frac{1}{3} : \frac{1}{2} : \frac{1}{6}$

$= \frac{2}{6} : \frac{3}{6} : \frac{1}{6}$

C retires and his $\frac{1}{6}$ share is taken by M.

$\therefore$ M's Gain $= \frac{1}{6}$ and N's Gain = zero

New share = Old share + Gain

$\therefore$ M's new share $= \frac{2}{6} + \frac{1}{6} = \frac{3}{6}$

N's new share $= \frac{3}{6} + 0 = \frac{3}{6}$

$\therefore$ New profit and loss sharing ratio of M and N = 3:3 means 1:1

Illustration 8 : S, E, B and I are the partners sharing profits in the ratio of 4:3:2:1. B and I retires. B's share is acquired by S and I's share is acquired by E. Find out the new profit and loss sharing of S and E.

Ans. : Old ratio of S, E, B and I $= \frac{4}{10} : \frac{3}{10} : \frac{2}{10} : \frac{1}{10}$

B's share $\frac{2}{10}$ is acquired by S. So, S's gain $= \frac{2}{10}$

I's share $\frac{1}{10}$ is acquired by E. So, E's gain $= \frac{1}{10}$ $\therefore$ Gaining ratio is 2:1.

New share = Old share + Gain

$\therefore$ S's new share $= \frac{4}{10} + \frac{2}{10} = \frac{6}{10}$

E's new share $= \frac{3}{10} + \frac{1}{10} = \frac{4}{10}$

$\therefore$ New share of profit and loss sharing ratio $= \frac{6}{10} : \frac{4}{10}$

= 6:4 means 3:2

(4) When old and new profit and loss sharing ratios are given :

Gain = New share − Old share

Illustration 9 : U, P and A are the partners sharing profits and losses in the ratio of 4:3:2. U retires and P and A decide to share the future profit and loss in the ratio of 2:1. Calculate the gaining ratio of P and A.

Ans. : Old sharing ratio of U, P and A = 4:3:2

U retires.

New sharing ratio of P and A = 2:1

Gain = New share − Old share

$\therefore$ P's new share $= \frac{2}{3} - \frac{3}{9} = \frac{6-3}{9} = \frac{3}{9}$

A's new share $= \frac{1}{3} - \frac{2}{9} = \frac{3-2}{9} = \frac{1}{9}$

$\therefore$ Gaining ratio of P and A = 3:1

5. Accounting Treatment of Goodwill

On the death or retirement of a partner the continuing partners receive profit and loss share of the retiring or deceased partner. To compensate this gain in profit, continuing partners give the retiring partner, his share in firm's goodwill. Deceased or retiring partner is also entitled to receive his share in the firm's goodwill because the goodwill was earned by the firm when he was a partner.

As per the Accounting Standard-26, only that goodwill for which consideration is paid, can be recorded in the books of accounts. Internally generated goodwill can not be recorded in the books of accounts. At the time of the retirement of a partner also the goodwill of the firm is valued by internal assessment only, therefore no goodwill can be shown in the balance sheet of the firm as an asset. Therefore retiring or deceased partner will be given his share in the firm's goodwill by the continuing partners in their gaining ratio by making necessary adjustments only in capital accounts of the partners. Old goodwill (if any) appearing in the old balance sheet should be written off by debiting all the partners' capital accounts in their old profit sharing ratio, because the old partnership is dissolved.

Considering above, the accounting treatment of goodwill on death or retirement of a partner will be given as under :

(1) Old goodwill if any, appearing in the balance sheet of the old firm, it will be written off in old profit-loss sharing ratio among all the partners including the deceased or retiring partner. For which following journal entry is passeed.

All partners' capital/current A/c ...Dr

To goodwill A/c

(Being old goodwill written off among all the partners in their old profit-loss sharing ratio.)

(2) Retiring or deceased partner is given his share in goodwill in their gaining ratio :

Continuing partners' capital/current A/c ...Dr

To retiring/deceased partners' capital A/c

(Being goodwill given by the continuing partners to the retiring/deceased partner in their gaining ratio.)

Illustration 10 : I, C, W and A are the partners sharing profit and loss in the ratio of 4:3:2:1. I retired from 1-4-2016. Balance sheet of the firm shows goodwill at ₹ 20,000 at the time of the retirement of I. New profit-loss sharing ratio of C, W and A was decided at 2:2:1. Goodwill of the firm valued at ₹ 60,000 at the time of retirement of I. Write journal entry for goodwill.

Ans. :

Journal Entries

Date	Particulars		L.F.	Debit (₹)	Credit (₹)
1-4-2016	I's capital A/c	Dr		8000	
	C's capital A/c	Dr		6000	
	W's capital A/c	Dr		4000	
	A's capital A/c	Dr		2000	
	To Goodwill A/c				20,000
	[Being existing goodwill written off in old ratio.]				
1-4-2016	C's capital A/c	Dr		6000	
	W's capital A/c	Dr		12,000	
	A's capital A/c	Dr		6000	
	To I's capital A/c				24,000
	[Being I's share of goodwill adjusted to C's, W's and A's capital account in their gaining ratio.]				

Explanation (1) : Gaining ratio :

Old profit and loss sharing ratio of I, C, W and A = 4:3:2:1

New profit and loss sharing ratio of C, W and A = 2:2:1

Gain = New share − Old share

C's gain = $\frac{2}{5} - \frac{3}{10} = \frac{1}{10}$

W's gain = $\frac{2}{5} - \frac{2}{10} = \frac{2}{10}$

A's gain = $\frac{1}{5} - \frac{1}{10} = \frac{1}{10}$

∴ Gaining ratio of C, W and A = 1:2:1

(2) : I's share in goodwill = $60{,}000 \times \frac{4}{10}$ = ₹ 24,000

I's share of goodwill will be given by C, W and A in their gaining ratio, 1:2:1.

Goodwill given by C = ₹ 24,000 × $\frac{1}{4}$ = ₹ 6000

Goodwill given by W = ₹ 24,000 × $\frac{2}{4}$ = ₹ 12,000

Goodwill given by A = ₹ 24,000 × $\frac{1}{4}$ = ₹ 6000

Illustration 11 : A, M, T and S are the partners of the firm sharing profit and loss in the ratio of 5:4:3:2. M retires as partner. At the time of the retirement of M, his share in firm's goodwill is ₹ 35,000. After retirement of M, partner A, T and S decided to share the future profit and loss in the ratio of 2:3:2. Pass the journal entry of goodwill.

Ans. :

Journal Entries

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
	T's capital A/c Dr		26,250	
	S's capital A/c Dr		17,500	
	To A's capital A/c			8750
	To M's capital A/c			35,000
	[Being A's and M's share of goodwill debited to T's and S's capital account in their gaining ratio.]			

Calculation 1 : Gaining ratio :

Old profit and loss sharing ratio of A, M, T and S = 5:4:3:2

New profit and loss sharing ratio of A, T and S = 2:3:2

Gain = New share − Old share

A's gain = $\frac{2}{7} - \frac{5}{14} = -\frac{1}{14}$ (Sacrifice)

T's gain = $\frac{3}{7} - \frac{3}{14} = \frac{6-3}{14} = \frac{3}{14}$

S's gain = $\frac{2}{7} - \frac{2}{14} = \frac{2}{14}$

Retiring partner M's share of goodwill = ₹ 35,000

A sacrifice his $\frac{1}{14}$ share out of his profit, therefore A will receive goodwill by the amount of his sacrifice.

Goodwill receivable by A :

Goodwill receivable by M for $\frac{4}{14}$th share = ₹ 35,000

Goodwill receivable by M for $\frac{1}{14}$th share = (?)

₹ $35,000 \times \frac{1}{14} \times \frac{14}{4}$ = ₹ 8750

Goodwill receivable by M and A ₹ 35,000 and ₹ 8750 respectively. Total amount = ₹ 43,750.

T and S will give in their gaining ratio

T's gain = $\frac{3}{14}$

S's gain = $\frac{2}{14}$

∴ Gaining ratio of T and S = 3:2

Goodwill payable by T = ₹ $43,750 \times \frac{3}{5}$ = ₹ 26,250

Goodwill payable by S = ₹ $43,750 \times \frac{2}{5}$ = ₹ 17,500

Illustration 12 : B, R and T are the partners sharing profit and loss in ther ratio of 3:2:1. B retires. B's capital after distributing profit of revaluation account and accumulated reserves and profit-loss is ₹ 1,20,000. R and T decided to pay ₹ 1,50,000 as final settlement including goodwill to B. R and T will distribute future profit and loss in the ratio of 3:2. Write necessary journal entries for goodwill.

Ans. :

Journal Entries

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
–	R's capital A/c Dr		16,000	
	T's capital A/c Dr		14,000	
	To B's capital A/c			30,000
	[Being goodwill given to B by his share in goodwill by R and T in their gaining ratio.]			

Explanation (1) : Total amount payable to B in final settlement of his account = ₹ 1,50,000

Less : Capital of B except goodwill = ₹ 1,20,000

Goodwill payable to B = ₹ 30,000

(2) : Gaining ratio :

Old ratio of B, R and T = 3:2:1

New ratio of R and T = 3:2

Gain = New share – Old share

R's Gain = $\frac{3}{5} - \frac{2}{6} = \frac{18-10}{30} = \frac{8}{30}$

T's Gain = $\frac{2}{5} - \frac{1}{6} = \frac{12-5}{30} = \frac{7}{30}$

∴ Gaining ratio of R and T = 8:7

6. **Revaluation of Assets and Liabilities**

Fixed assets are not shown at their market value in the books of the firm. Therefore there is difference between their book value and the market value. Some assets, liabilities and necessary provisions may not have been shown in the books. All profits and losses of the firm till the date of the retirement or death of a partner must be distributed among all the partners in their old profit-loss sharing ratio so that any partner may not get undue advantage or loss. Therefore, assets and liabilities are revalued at the time of the retirement or death of a partner and net increase or decrease in them is transferred to the revaluation account. Net profit or net loss of revaluation account is distributed among all the partners in their old profit-loss sharing ratio. Revaluation account is prepared in the same manner as it is prepared in the earlier chapter no. 5, in which

- Increase in assets and decrease in liabilities and provisions is credited to the revaluation account.
- Decrease in assets and increase in liabilities and provisions is debited to the revaluation account.
- Net profit or loss of revaluation account is distributed among all the partners in their old profit sharing ratio in their capital/current A/c.
- Assets and liabilities will be shown in the new balance sheet at their new values.

Memorandum Revaluation Account : Partners may also decide to show all the assets and liabilities at the same value in the new balance sheet after retirement. Memorandum revaluation account is prepared in such case. Memorandum revaluation account is prepared in the same manner as it is prepared in the previous chapter no. 5. Net increase or decrease in assets and liabilities are recorded in the first part of memorandum revaluation account in the same manner as they are shown in the revaluation account and net profit or net loss is distributed among all the partners in their old profit-loss sharing ratio. In the second part of the memorandum revaluation account all entries of the first part are reversed and therefore net profit of first part will become net loss and net loss of first part will become net profit of the second part which is distributed among the continuing partners except the retiring partners in their new profit-loss sharing ratio. All assets except cash and all liabilities will be shown in new balance sheet at their old values when memorandum revaluation account is prepared. **(Not expected in examination.)**

7. **Distribution of Reserves and Accumulated Profit-Losses**

Balances of reserves, undistributed profit or loss and balances of deferred revenue expenditure on the date of retirement or death are distributed among all the partners including retiring or deceased partners in their old profit-loss sharing ratio. Same journal entries in this respect as shown in previous chapter no. 5 "Admission of a Partner" are recorded at the time of the retirement or death of a partner.

8. **Determination of Amount Payable to the Retiring Partner**

Amount payable to the retiring partner is decided by preparing his capital account :

(1) Following amounts are credited to the retiring partners' capital account :

(i) Opening balance of capital account and credit balance of current account on the date of retirement.

(ii) Share in profit of revaluation account

(iii) Share in reserves and undistributed profit

(iv) Share in new value of goodwill

(v) Share in profit of the firm from the date of last balance sheet to the date of retirement.

(vi) Salary, commission, interest on capital, interest on loan given to the firm from the date of last balance sheet to the date of retirement. (If rate of interest on the partners' loan is not given; interest is payable on the partner's loan at the rate of 6 % p.a. till the date of retirement.)

(2) Following balances reduce capital, therefore they are debited to his capital account :

(i) Debit balance of current account

(ii) Drawings

(iii) Interest on drawings till the date of retirement

(iv) Share in undistributed loss and defferred revenue expenditure (fictitious assets)

(v) Share in old goodwill appearing in the books of the firm

(vi) Share in loss of revaluation account

(vii) Loan given by the firm to the retiring partner

The balance obtained by closing the retiring partners' capital account is the amount payable to the retiring partner. The amount payable to the retiring partner is paid in cash fully or partly and balance of the unpaid amount is transferred to his loan account, for which of the following entry is passed.

Retiring partners' capital A/c...Dr

To cash A/c

To retiring partners' loan A/c

Interest payable to retiring partners' loan account : Unpaid amount out of the total amount payable to the retiring partner is transferred to his loan account. If the rate of interest payable on such loan is not mentioned in the partnership deed, the interest is payable at the rate of 6 % per annum as per Indian Partnership Act, 1932.

Illustration 13 : The balance sheet of X, Y and Z is given below as on 31-3-2016.

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Goodwill		40,000
X	2,00,000		Land-Building		1,99,000
Y	1,20,000		Machinery		1,80,000
Z	1,00,000	4,20,000	Stock		50,000
General reserve		40,000	Debtors	70,000	
Partners' loan :			− Bad debt reserve	5000	65,000
Y	20,000		Bank balance		30,000
Z	30,000	50,000	Advertisement campaign expenditure		16,000
Creditors		80,000	Profit-loss A/c		20,000
Workmen compensation reserve		10,000			
		6,00,000			**6,00,000**

X, Y and Z are the partners of the firm sharing profit and loss in the ratio of 3:3:2. Y retires on 1-4-2016 on the following terms :

(1) Land and Building is to be valued at ₹ 2,20,000.

(2) Value of machinery is to be reduced by ₹ 30,000.

(3) The provision for doubtful debts is to be kept at 10 %.

(4) Liability for workmen compensation is accepted at ₹ 15,000.

(5) Goodwill of the firm is valued at ₹ 1,60,000. Y's share in goodwill is to be adjusted through the capital acccount of X and Z.

(6) The new ratio of profit and loss sharing of X and Z is decided at 1:1. From the above information pass necessary journal entries and prepare revaluation account, partners' capital account and balance sheet after the retirement of Y.

Ans. :

Journal Entries

No.	Particulars	L.F.	Debit (₹)	Credit (₹)
1.	General reserve A/c Dr		40,000	
	To X's capital A/c			15,000
	To Y's capital A/c			15,000
	To Z's capital A/c			10,000
	[Being balance of general reserve is distributed to all partners' capital accounts in their old profit sharing ratio.]			
2.	Revaluation A/c Dr		5000	
	Workmen compensation reserve A/c Dr		10,000	
	To Workmen compensation claim A/c			15,000
	[Being amount of workmen compensation reserve and access of claim over the reserve debited to the revaluation account.]			
3.	X's capital A/c Dr		15,000	
	Y's capital A/c Dr		15,000	
	Z's capital A/c Dr		10,000	
	To Goodwill A/c			40,000
	[Being old goodwill written off in old profit-loss sharing ratio.]			
	Total carry forward		95,000	95,000

No.	Particulars	L.F.	Debit (₹)	Credit (₹)
	Total bring forward		95,000	95,000
4.	X's capital A/c Dr Y's capital A/c Dr Z's capital A/c Dr To Advertisement campaign expenditure A/c [Being balance of advertisement campaign expenditure is distributed to all partners' capital account in their old profit sharing ratio.]		6000 6000 4000	 16,000
5.	X's capital A/c Dr Y's capital A/c Dr Z's capital A/c Dr To Profit and loss A/c [Being debit balance of profit and loss account distributed to all partners' capital account in their old ratio.]		7500 7500 5000	 20,000
6.	Revaluation A/c Dr To Machinery A/c To Bad debt reserve A/c [Being decrease in machinery and increase in bad debt reserve transferred to revaluation A/c.]		32,000	 30,000 2000
7.	Land-Building A/c Dr To Revaluation A/c [Being increase in land and building transferred to revaluation A/c.]		21,000	 21,000
8.	X's capital A/c Dr Y's capital A/c Dr Z's capital A/c Dr To Revaluation A/c [Being loss of revaluation A/c distributed to all partners' capital accounts in their old profit sharing ratio.]		6000 6000 4000	 16,000
9.	X's capital A/c Dr Z's capital A/c Dr To Y's capital A/c [Being Y's share in goodwill adjusted through capital accounts of X and Z in their gaining ratio.]		20,000 40,000	 60,000
10.	Y's loan A/c Dr To Y's capital A/c [Being Y's loan transferred to his capital A/c.]		20,000	 20,000
	Total carry forward		2,80,000	2,80,000

No.	Particulars	L.F.	Debit (₹)	Credit (₹)
	Total bring forward		2,80,000	2,80,000
11.	Y's capital A/c Dr		1,80,500	
	To Y's loan A/c			1,80,500
	[Being amount due to Y transferred to his loan account.]			
	Total		**4,60,500**	**4,60,500**

Revaluation Account

Dr Cr

Particulars	Amt. (₹)	Particulars		Amt. (₹)
To Machinery A/c	30,000	By Land-Building A/c		21,000
To Bad debt reserve A/c	2000	By Partners' capital A/c : loss		
(New ₹ 7000 – Old ₹ 5000)		X	6000	
To Workmen compensation claim A/c	5000	Y	6000	
		Z	4000	16,000
	37,000			**37,000**

Partners' Capital Accounts

Dr Cr

Particulars	X (₹)	Y (₹)	Z (₹)	Particulars	X (₹)	Y (₹)	Z (₹)
To Adv. campaign expenditure A/c	6000	6000	4000	By Balance b/d	2,00,000	1,20,000	1,00,000
To Profit-loss A/c	7500	7500	5000	By General reserve A/c	15,000	15,000	10,000
To Goodwill A/c (old)	15,000	15,000	10,000	By Y's loan A/c	–	20,000	–
To Y's capital A/c (New goodwill)	20,000	–	40,000	By X's capital A/c (New goodwill)	–	20,000	–
To Revaluation A/c	6000	6000	4000	By Z's capital A/c (New goodwill)	–	40,000	–
To Y's loan A/c	–	1,80,500	–				
To Balance c/d	1,60,500	–	47,000				
	2,15,000	**2,15,000**	**1,10,000**		**2,15,000**	**2,15,000**	**1,10,000**

Balance Sheet as on 1-4-2016 After Retirement

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Land-Building		2,20,000
X	1,60,500		Machinery		1,50,000
Y	47,000	2,07,500	Stock		50,000
Partner Z's loan		30,000	Debtors	70,000	
Partner Y's loan		1,80,500	− Bad debt reserve	7000	63,000
Provision for workmen compensation claim		15,000	Bank balance		30,000
Creditors		80,000			
		5,13,000			**5,13,000**

Explanation : (1) Gaining ratio of continuing ratio

Old profit-loss sharing ratio of X, Y and Z = 3:3:2

New profit-loss sharing ratio of X and Z = 1:1

Gain = New share − Old share

$$\text{X's Gain} = \frac{1}{2} - \frac{3}{8} = \frac{4-3}{8} = \frac{1}{8}$$

$$\text{Z's Gain} = \frac{1}{2} - \frac{2}{8} = \frac{4-2}{8} = \frac{2}{8}$$

∴ Gaining ratio of X and Z = 1:2

(2) Share of goodwill of Y which is contributed by X and Z in their gaining ratio of 1:2

Y's share of goodwill = ₹ 1,60,000 $\times \frac{3}{8}$ = ₹ 60,000

X and Z will give ₹ 60,000 for goodwill to Y in their gaining ratio 1:2.

Goodwill payable by X = ₹ 60,000 $\times \frac{1}{3}$ = ₹ 20,000

Goodwill payable by Y = ₹ 60,000 $\times \frac{2}{3}$ = ₹ 40,000

Journal Entry

No.	Particulars	L.F.	Debit (₹)	Credit (₹)
–	X's Capital A/c Dr		20,000	
	Z's Capital A/c Dr		40,000	
	To Y's Capital A/c			60,000

Note : (1) Old goodwill ₹ 40,000 is written off by debiting capital accounts of X, Y and Z in their old profit and loss sharing ratio. (2) The balance of workmen compensation reserve is ₹ 10,000. But accepted claim of workmen compensation is ₹ 15,000. Therefore, additional ₹ 5000 is debited to revaluation account as provision for workmen compensation claim.

Workmen compensation reserve A/c Dr... 10,000

Revaluation A/c Dr... 5000

To Workmen compensation claim A/c 15,000

(3) Amount paid to Y is not mentioned in the question, hence the total amount payable to Y is transferred to Y's loan account.

Illustration 14 : Ajay, Alpa and Amay are the partners of the firm sharing profit and loss in the ratio of 50 %, 30 % and 20 % respectively. The balance sheet of the firm as on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Goodwill		50,000
Ajay	60,000		Other fixed assets		1,00,000
Alpa	50,000		Investments		60,000
Amay	80,000	1,90,000	Debtors	70,000	
Investment fluctuation fund		20,000	− Bad debt reserve	6000	64,000
Workmen compensation reserve		30,000	Stock		20,000
Creditors		40,000	Cash		16,000
Provident fund		60,000	Profit-loss A/c		30,000
		3,40,000			**3,40,000**

Ajay retires on 1-4-2017 on the following terms :

(1) The claim of workmen compensation is accepted at ₹ 20,000.

(2) The market value of investment is ₹ 45,000.

(3) Bad debts on debtors ₹ 2000 is to be written off and the provision for doubtful debts is to be kept at 5 %

(4) Fixed assets to be appreciated by 20 %.

(5) The book value of stock is over valued by ₹ 600 compared to its cost. The cost of stock is to be recorded.

(6) The value of goodwill of the firm is ₹ 1,00,000.

(7) Ajay is to be paid ₹ 10,000 in cash.

(8) The new profit and loss sharing ratio of Alpa and Amay is 1:4.

Prepare revaluation account, capital accounts of partners and the balance sheet after the retirement of Ajay.

Ans. :

Revaluation Account

Dr | Cr

Particulars		Amt. (₹)	Particulars	Amt. (₹)
To Stock A/c		600	By Bad debt reserve A/c	
To Partners' capital A/c (Profit)			(₹ 6000 − Bad debts ₹ 2000 −	
Ajay	10,000		New bad debt reserve ₹ 3400)	600
Alpa	6000		By Fixed assets A/c	20,000
Amay	4000	20,000		
		20,600		**20,600**

Partners' Capital Accounts

Dr | | | | | | | Cr

Particulars	Ajay (₹)	Alpa (₹)	Amay(₹)	Particulars	Ajay (₹)	Alpa (₹)	Amay(₹)
To Goodwill A/c	25,000	15,000	10,000	By Balance b/d	60,000	50,000	80,000
To Profit-loss A/c	15,000	9000	6000	By Workmen comp. reserve A/c	5000	3000	2000
To Ajay's capital A/c (goodwill)	–	–	50,000	By Investment fluctuation fund A/c	2500	1500	1000
To Alpa's capital A/c (goodwill)	–	–	10,000	By Amay's capital A/c (goodwill)	50,000	10,000	–
To Cash A/c	10,000	–	–	By Revaluation A/c	10,000	6000	4000
To Ajay's loan A/c	77,500	–	–				
To Balance c/d	–	46,500	11,000				
	1,27,500	**70,500**	**87,000**		**1,27,500**	**70,500**	**87,000**

Balance Sheet as on 1-4-2017 After Retirement

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Fixed assets		1,20,000
Alpa	46,500		Investments		45,000
Amay	11,000	57,500	Debtors	70,000	
Ajay's loan		77,500	– Bad debt	2000	
Workmen compensation claim		20,000		68,000	
Creditors		40,000	– Bad debt reserve (5 %)	3400	64,600
Provident fund		60,000	Stock		19,400
			Cash (₹ 16,000 - ₹ 10,000 payment to Ajay)		6000
		2,55,000			**2,55,000**

Explanation (1) : Gaining ratio :

Old profit and loss sharing ratio of Ajay, Alpa and Amay = 5:3:2

New profit and loss sharing ratio of Alpa and Amay = 1:4

Gain = New share – Old share

Alpa's gain $= \frac{1}{5} - \frac{3}{10} = \frac{2-3}{10} = -\frac{1}{10}$ (Sacrifice)

Amay's gain $= \frac{4}{5} - \frac{2}{10} = \frac{8-2}{10} = \frac{6}{10}$

(2) : Calculation of goodwill :

Ajay is retiring, so goodwill receivable by him $= \frac{5}{10} \times 1,00,000 = 50,000$

Alpa's sacrifice $\frac{1}{10}$ share, therefore amount of goodwill receivable by her $= \frac{1}{10} \times 1,00,000 =$ ₹ 10,000

Amay is gaining, so goodwill contributed by him $= \frac{6}{10} \times 1,00,000 =$ ₹ 60,000

Journal Entries

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
–	Amay's capital A/c Dr		60,000	
	To Ajay's capital A/c			50,000
	To Alpa's capital A/c			10,000

Explanation : Retiring partner Ajay as well as Alpa from the continuing partners sacrifice their profit share and therefore they receive goodwill by their sacrifice while Amay gains, therefore he will give goodwill by his gain.

Note : (1) Decrease in the value of investment is ₹ 15,000 while there is investment fluctuation fund against it and it is ₹ 20,000. Therefore the balance of investment fluctuation fund after writting off the decrease in investments ₹ 15,000 is ₹ 5000, which is credited to all the partners' capital accounts in their old profit and loss sharing ratio. For this following journal entry is passed :

Investment fluctuation fund A/c Dr...	20,000	
To Investments A/c		15,000
To Ajay's capital A/c		2500
To Alpa's capital A/c		1500
To Amay's capital A/c		1000

(2) Claim of workmen compensation accepted is ₹ 20,000 against the workmen compensation reserve of ₹ 30,000 and balance of reserve ₹ 10,000 is distributed among all the partners in their old profit and loss sharing ratio.

Workmen compensation reserve A/c Dr...	30,000	
To workmen compensation claim A/c		20,000
To Ajay's capital A/c		5000
To Alpa's capital A/c		3000
To Amay's capital A/c		2000

Illustration 15 : Gopi, Krishna and Ram are the partners of a firm sharing profit-loss in the ratio of $\frac{1}{2}$, $\frac{1}{3}$ and $\frac{1}{6}$. The balance sheet of the firm as on 31-3-2017 is as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Goodwill	1500
Gopi	30,000		Trademark	18,000
Krishna	20,000		Machinery	60,000
Ram	30,000	80,000	Investments (Market value ₹ 15,000)	40,000
Current Accounts :			Stock	12,000
Gopi	8,000		Debtors	26,000
Ram	10,000	18,000	Cash in bank	3000
Contingency reserve		12,000	Current account of Krishna	4500
Workmen compensation fund		9000		
Investment fluctuation fund		15,000		
Creditors		23,000		
Bad debt reserve		8000		
		1,65,000		**1,65,000**

Ram retires on 1-4-2017 on the following terms :

(1) The value of machinery is to be increased by 10 %.

(2) The value of trademark is to be reduced upto 40 %.

(3) Bad debt reserve on debtors is to be kept at 15 %.

(4) Discounted bills receivable of ₹ 1300 which is dishonoured on due date, 31-3-2017. No amount is received from the debtors.

(5) Goodwill of the firm is valued at ₹ 60,000.

(6) The new profit-loss sharing ratio of Gopi and Krishna is 2:1.

Prepare revaluation account, partners' current account, capital account and balance sheet after the retirement of Ram.

Ans. :

Dr **Revaluation Account** Cr

Particulars	Amt. (₹)	Particulars		Amt. (₹)
To Investments A/c	10,000	By Machinery A/c		6000
To Trademark	10,800	By Bad debt reserve A/c		
To Bank A/c	1300	(₹ 8000 – ₹ 3900)		4100
(Dishonoured bills receivable)		By Partners' current A/c (Loss) :		
		Gopi	6000	
		Krishn	4000	
		Ram	2000	12,000
	22,100			**22,100**

Current Accounts of Partners

Dr Cr

Particulars	Gopi (₹)	Krishna(₹)	Ram (₹)	Particulars	Gopi (₹)	Krishna(₹)	Ram (₹)
To Balance b/d	–	4500	–	By Balance b/d	8000	–	10,000
To Goodwill	750	500	250	By Contingency reserve A/c	6000	4000	2000
To Ram's A/c (goodwill)	10,000	–	–	By Workmen compenstion fund	4500	3000	1500
To Revaluation A/c	6000	4000	2000	By Gopi's A/c (goodwill)	–	–	10,000
To Ram's capital A/c	–	–	21,250				
To Balance c/f	1750	–	–	By Balance c/f	–	2000	–
	18,500	**9000**	**23,500**		**18,500**	**9000**	**23,500**

Dr **Capital Accounts of Partners** Cr

Particulars	Gopi (₹)	Krishna(₹)	Ram (₹)	Particulars	Gopi (₹)	Krishna(₹)	Ram (₹)
To Ram's loan A/c	–	–	51,250	By Balance b/d	30,000	20,000	30,000
To Balance c/f	30,000	20,000	–	By Ram's current A/c	–	–	21,250
	30,000	**20,000**	**51,250**		**30,000**	**20,000**	**51,250**

Balance Sheet as on 1-4-2017 After Retirement

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Trademark (18,000 – 10,800)		7200
Gopi	30,000		Machinery		66,000
Krishna	20,000	50,000	Debtors	26,000	
Current account of Gopi		1750	– Bad debt reserve	3900	22,100
Ram's loan A/c		51,250	Investments		15,000
Creditors		23,000	(40,000 – (15,000 + 10,000))		
			Stock		12,000
			Cash in bank (₹ 3000 – ₹ 1300)		1700
			Current account of Krishna		2000
		1,26,000			**1,26,000**

Explanation (1) : Gaining ratio :

Old profit-loss sharing ratio of Gopi, Krishna and Ram = $\frac{1}{2} : \frac{1}{3} : \frac{1}{6} = \frac{3}{6} : \frac{2}{6} : \frac{1}{6} = 3:2:1$

New profit-loss sharing ratio of Gopi and Krishna = 2:1

Gain = New share – Old share

Gopi's gain = $\frac{2}{3} - \frac{3}{6} = \frac{4-3}{6} = \frac{1}{6}$; Krishna's gain = $\frac{1}{3} - \frac{2}{6} = \frac{2-2}{6} = 0$

(2) : Calculation of goodwill and its effect :

Goodwill receivable by Ram = $\frac{1}{6} \times 60,000$ = ₹ 10,000

Krishna's gain is zero therefore goodwill of Ram is given by Gopi only.

Journal Entry

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
–	Gopi's current A/c Dr To Ram's current A/c		10,000	 10,000

Note : (1) Loss of investments is ₹ 25,000. While balance of investment fluctuation reserve is ₹ 15,000. Therefore additional loss of ₹ 10,000 is debited at revaluation account.

Investment fluctuation reserve A/c Dr...	15,000	
Revaluation A/c Dr...	10,000	
To Investments A/c		25,000

(2) Dishonored bills receivable :

(i) Bill receivables A/c Dr...	1300	
To Bank A/c		1300
(ii) Debtors A/c Dr...	1300	
To Bills receivables A/c		1300
(iii) Revaluation A/c Dr...	1300	
To Debtors A/c		1300
or		
Revaluation A/c Dr...	1300	
To Bank A/c		1300

(3) Trademark is to be reduced upto 40 % means, from 100 % ·············· to 40 %

Complete amount means, reduce upto 60 %.

9800 ·············· 10,800 ·············· 7200

∴ 18,000's 60 % = ₹ 10,800 is to be reduced.

Illustration 16 : A, B and C are the partners of the firm sharing profit and loss in equal proportion. A retires as on 1-4-2014 after adjustment of goodwill, revaluation profit and reserves, balance of A's capital is ₹ 90,000. Amount due to A is to be paid in three equal annual instalments together with interest at 10 % p.a. Prepare A's loan account till it is finally paid. Financial year ends on 31st March.

Ans. :

A's Loan Account

Dr | Cr

Date	Particulars	Amt. (₹)	Date	Particulars	Amt. (₹)
31-3-15	To Bank A/c(30,000 + 9000)	39,000	1-4-14	By A's capital A/c	90,000
”	To Balance c/f	60,000	31-3-15	By Interest A/c	9000
		99,000			**99,000**
31-3-16	To Bank A/c(30,000 + 6000)	36,000	1-4-15	By Balance b/d	60,000
”	To Balance c/f	30,000	31-3-16	By Interest A/c	6000
		66,000			**66,000**
31-3-17	To Bank A/c(30,000 + 3000)	33,000	1-4-16	By Balance b/d	30,000
			31-3-17	By Interest A/c	3000
		33,000			**33,000**

- **Adjustment of capitals (i) When the total capital of the new firm is given**

Illustration 17 : P, V and R are the partners of the firm sharing profit and loss in the ratio of 5:3:2. R retires after the adjustment of profit of revaluation, reserves and goodwill, partners capital stood ₹ 50,000, ₹ 70,000 and ₹ 80,000 respectively. The entire capital of the firm as newly constituted is fixed ₹ 1,40,000 between P and V in their new profit-loss sharing ratio 3:2. Calculate the actual cash to be paid or to be brought in by the continuing partners. Pass the necessary journal entries with working notes and also prepare capital accounts of partners.

Ans. : Explanation (1) : Total new capital of P and V = ₹ 1,40,000, in proportion of 3:2,

P's new capital $= ₹\ 1,40,000 \times \frac{3}{5}$

$= ₹\ 84,000$

V's new capital $= ₹\ 1,40,000 \times \frac{2}{5}$

$= ₹\ 56,000$

(2) Calculation of the amount of cash to be paid or to be brought in :

	P (₹)	V (₹)
New capital	84,000	56,000
Less : Actual capital after adjustment	50,000	70,000
Capital to be brought in (paid off)	34,000	(14,000)
	Capital brought	Capital paid

₹ 34,000 cash to be brought by P. ₹ 14,000 additional cash withdrawn by V as capital.

Journal Entries

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
–	Cash A/c Dr		34,000	
	To P's capital A/c			34,000
	[Being necessary capital brought by P.]			
–	V's capital A/c Dr		14,000	
	To Cash A/c			14,000
	[Being additional capital withdrawn by V.]			

Capital Accounts of Partners

Dr Cr

Particulars	P (₹)	V (₹)	R (₹)	Particulars	P (₹)	V (₹)	R (₹)
To R's loan A/c	–	–	80,000	By Balance b/d	50,000	70,000	80,000
To Cash A/c	–	14,000	–	By Cash A/c	34,000	–	–
To Balance c/f	84,000	56,000	–				
	84,000	**70,000**	**80,000**		**84,000**	**70,000**	**80,000**

(ii) When the total capital of the new firm is not given and the amount paid to the retiring partner is to be brought in by the remaining partners :

Illustration 18 : A, B and C are the partners sharing profit and loss in the ratio of 4:3:2 respectively. 'A' retired on 1-4-2017. The capital of A, B and C after all the adjustment of the revaluation of profit, reserves and goodwill were at ₹ 30,000, ₹ 80,000 and ₹ 90,000 respectively. All partners decide that A is to be paid amount due to him in cash which is to be brought in by B and C in such a way as to make their capitals proportionate to their new profit-loss sharing ratio. All necessary adjustments are to be made in cash. Give journal entries and prepare partners' capital account.

Ans. : Explanation (1) : Capital of new firm :

Old profit-loss sharing ratio of A, B and C = 4:3:2

After retirement of A, the new ratio of B and C = 3:2

Total capital of new firm :	B's capital	= ₹ 80,000
	C's capital	= ₹ 90,000
	Additional capital (Payable to A)	= ₹ 30,000
	Total capital of new firm	= ₹ 2,00,000

B's share in total capital of new firm = 2,00,000 × $\frac{3}{5}$ = ₹ 1,20,000 (New ratio)

C's share in total capital of new firm = ₹ 2,00,000 × $\frac{2}{5}$ = ₹ 80,000 (New ratio)

(2) Calculation of cash to be paid or brought in

	B (₹)	C (₹)
Capital required after adjustments	1,20,000	80,000
Less : Actual capital after adjustment	80,000	90,000
Cash to be brought in (paid off)	40,000	(10,000)
	Capital brought	Capital returned

Journal Entries

Date	Particulars		L.F.	Debit (₹)	Credit (₹)
–	A's capital A/c	Dr		30,000	
	To cash A/c				30,000
	[Being amount due to A paid off.]				
–	Cash A/c	Dr		40,000	
	To B's capital A/c				40,000
	[Being additional capital brought by B.]				
–	C's capital A/c	Dr		10,000	
	To cash A/c				10,000
	[Being additional capital of C paid off.]				

Dr **Capital Accounts of Partners** Cr

Particulars	A (₹)	B (₹)	C (₹)	Particulars	A (₹)	B (₹)	C (₹)
To Cash A/c	30,000	–	–	By Balance b/d	30,000	80,000	90,000
To Cash A/c	–	–	10,000	By Cash A/c	–	40,000	–
To Balance c/f	–	1,20,000	80,000				
	30,000	**1,20,000**	**90,000**		**30,000**	**1,20,000**	**90,000**

(iii) The retiring partner is to be paid in cash and an amount brought in by the remaining partner in cash in such a way that minimum cash is to be maintained :

Illustration 19 : A, B and C are the partners sharing profit and loss in the ratio of 5:3:1. 'A' retires on 1-4-2017. The capital of A, B and C after all adjustments regarding loss of revaluation account, reserves and goodwill stood at ₹ 60,000, ₹ 50,000 and ₹ 70,000 respectively. On that day balance of cash was ₹ 30,000. Partners decided as under :

(A) Amount due to A is to be paid in cash.

(B) The amount of cash to be paid or to be brought in by the remaining partners in such a way so as to make their capitals proportionate to their new profit-loss sharing ratio and minimum cash balance ₹ 20,000 is to be maintained.

Give journal entries with necessary calculation and prepare partners' capital account and cash account :

Ans. : Explanation (1) : Capital of B and C in new firm

Old profit and loss sharing ratio of A, B and C = 5:3:1

After the retirement of A, new profit and loss sharing ratio of B and C = 3:1

Share of cash to be brought in by B and C :

To make payment to A	=	₹ 60,000
Less : Available cash for payment to A	=	₹ 10,000
(₹ 30,000 – ₹ 20,000 cash to be maintained)		
Cash brought in by B and C		₹ 50,000

Total capital of new firm of B and C :

B's capital =	₹	50,000
+ C's capital =	₹	70,000
+ Additional capital =	₹	50,000
Total capital of B and C =	₹	1,70,000

(Necessary cash balance to maintain minimum cash balance and to pay dhes of 'A')

B's capital in new profit and loss sharing ratio = ₹ 1,70,000 × $\frac{3}{4}$ = ₹ 1,27,500 (As per new ratio)

C's capital in new profit and loss sharing ratio = ₹ 1,70,000 × $\frac{1}{4}$ = ₹ 42,500 (As per new ratio)

(2) : Cash to be brought in or paid off to B and C :

	B (₹)	**C (₹)**
New capital	1,27,500	42,500
Less : Capital after adjustment	50,000	70,000
Cash to be brought in as capital (or paid off)	77,500	(27,500)
	Capital brought	Capital paid

Journal Entries

Date/No.	**Particulars**	**L.F.**	**Debit (₹)**	**Credit (₹)**
1	A's capital A/c Dr To Cash A/c [Being the due amount paid to A.]		60,000	 60,000
2	Cash A/c Dr To B's capital A/c [Being required cash brought in by B as his capital.]		77,500	 77,500
3	C's capital A/c Dr To Cash A/c [Being additional capital paid off to C.]		27,500	 27,500

Capital Accounts of Partners

Dr | Cr

Particulars	A (₹)	B (₹)	C (₹)	Particulars	A (₹)	B (₹)	C (₹)
To Cash A/c	60,000	–	–	By Balance b/d	60,000	50,000	70,000
To Cash A/c	–	–	27,500	By Cash A/c	–	77,500	–
To Balance c/f	–	1,27,500	42,500				
	60,000	**1,27,500**	**70,000**		**60,000**	**1,27,500**	**70,000**

Cash Account

Dr | Cr

Date	Particulars	Amt. (₹)	Date	Particulars	Amt. (₹)
1-4-17	To Balance b/d	30,000	1-4-17	By A's capital A/c	60,000
1-4-17	To B's capital A/c	77,500	1-4-17	By C's capital A/c	27,500
			1-4-17	By Balance c/f	20,000
		1,07,500			**1,07,500**

Illustration 20 : Karan, Fenil and Farshid are partners in a firm sharing profit and loss in the ratio of their capitals. Balance sheet of the firm as on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Creditors		16,000	Goodwill		40,000
Workmen compensation reserve		12,000	Land-Building		2,00,000
Employee's profit sharing fund		30,000	Patents		60,000
Provident fund		45,000	Machinery		80,000
Capital Accounts :			Debtors	35,000	
Karan	2,00,000		– Bad debt reserve	5000	30,000
Fenil	1,20,000		Stock		53,000
Farshid	80,000	4,00,000	Bank		40,000
		5,03,000			**5,03,000**

Farshid retires on the above date. Partners decided the following terms of retirement :

(1) The new profit-loss sharing ratio of Karan and Fenil is to be kept at 2:3.

(2) Goodwill of the firm is to be valued at ₹ 80,000.

(3) Paid ₹ 60,000 for patents during current year which is for total 4 years.

(4) Machinery is to be depreciated by 10 %.

(5) Bad debt on debtors is to be written off ₹ 3000.

(6) ₹ 20,000 is to be paid to Farshid.

(7) Market value of stock is ₹ 54,000.

(8) New firm's total capital will be equal to total capital of old firm. The entire capital of the new firm is to be kept in new profit and loss sharing ratio of Karan and Fenil. All necessary adjustments are to be made through bank.

Prepare (i) Revaluation account (ii) Capital accounts of partners (iii) Bank account (iv) Balance Sheet after retirement of Farshid.

Ans. :

Revaluation Account

Dr | Cr

Particulars	Amt. (₹)	Particulars		Amt. (₹)
To Patent A/c	15,000	By Bad debt reserve A/c		2000
To Machinery A/c	8000	(₹ 5000 – ₹ 3000 bad debt)		
		By Stock A/c		1000
		By Partners' capital A/c (Loss) :		
		Karan	10,000	
		Fenil	6000	
		Farshid	4000	20,000
	23,000			**23,000**

Capital Accounts of Partners

Dr | Cr

Particulars	Karan (₹)	Fenil (₹)	Farshid (₹)	Particulars	Karan (₹)	Fenil (₹)	Farshid (₹)
To Goodwill A/c	20,000	12,000	8000	By Balance b/d	2,00,000	1,20,000	80,000
To Karan's capital A/c	–	8000	–	By Workmen compensation fund	6000	3600	2400
To Farshid's capital A/c (goodwill)	–	16,000	–	By Fenil's capital A/c (goodwill)	8000	–	16,000
To Bank A/c	–	–	20,000	By Bank A/c	–	1,58,400	–
To Revaluation A/c	10,000	6000	4000				
To Farshid's loan A/c	–	–	66,400				
To Bank A/c	24,000	–	–				
To Balance c/f	1,60,000	2,40,000	–				
	2,14,000	**2,82,000**	**98,400**		**2,14,000**	**2,82,000**	**98,400**

Bank Account

Dr | Cr

Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	40,000	By Farshid A/c	20,000
To Fenil's capital A/c	1,58,400	By Karan A/c	24,000
		By balance c/f	1,54,400
	1,98,400		**1,98,400**

Balance Sheet as on 1-4-2017 After Retirement

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Creditors		16,000	Patents	45,000
Employee's profit sharing fund		30,000	Machinery	72,000
Provident fund		45,000	Debtors	32,000
Farshid's loan A/c		66,400	Stock	54,000
Capital Accounts :			Bank	1,54,400
Karan	1,60,000		Land-Building	2,00,000
Fenil	2,40,000	4,00,000		
		5,57,400		**5,57,400**

Explanation : (1) Distribution of goodwill

Old ratio of Karan, Fenil and Farshid = 5:3:2; New ratio of Karan and Fenil = 2:3

Gain = New share − Old share

Karan's gain = $\frac{2}{5} - \frac{5}{10} = -\frac{1}{10}$ (Sacrifice)

Fenil's gain = $\frac{3}{5} - \frac{3}{10} = \frac{3}{10}$

∴ Goodwill payable by Fenil = ₹ 80,000 × $\frac{3}{10}$ = ₹ 24,000

Karan also sacrifices his share, so he will also receive goodwill which is given by Fenil.

Goodwill receivable by Karan = $\frac{1}{10}$ × 80,000 = ₹ 8000

Goodwill receivable by Farshid = $\frac{2}{10}$ × 80,000 = ₹ 16,000

Journal Entries : Fenil's capital A/c...Dr		24,000	
	To Karan's capital A/c		8000
	To Farshid's capital A/c		16,000

(2) Distribution of capital of new firm

New firm's total capital of ₹ 4,00,000 is same as old firm's total capital which is distributed between Karan and Fenil in their new profit and loss sharing ratio, 2:3.

∴ New capital of Karan = 4,00,000 × $\frac{2}{5}$ = 1,60,000; New capital of Fenil = 4,00,000 × $\frac{3}{5}$ = 2,40,000

Illustration 21 : L, M and N are partners of a firm. They share their profit and loss 40 %, 30 % and 30 % respectively. Balance sheet of the firm as on 31 March, 2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Creditors		60,000	Cash	13,000
Investment fluctuation reserve		15,000	Stock	32,000
Bad debt reserve		10,000	Debtors	80,000
Capital Accounts :			Investments	60,000
L	1,80,000		Building	2,20,000
M	1,00,000		Furniture	30,000
N	90,000	3,70,000	Advertisement campaign expenditure	20,000
		4,55,000		**4,55,000**

M retires on 1-4-2016. Terms of retirement were as under :

(1) M's share is to be distributed between L and N in the ratio of 3:2.

(2) Bad debt of ₹ 8000 is to be written off and provision for bad debt is to be kept at 10 % and provision for discount reserve is to be kept at 5 % on debtors.

(3) Market value of investment is ₹ 50,000.

(4) Market value of building is ₹ 2,50,000.

(5) Write off ₹ 1560 from furniture.

(6) The capital of L and N is to be kept in their new profit and loss sharing ratio and all necessary adjustments to be made through their current account.

(7) The value of goodwill of the firm is ₹ 50,000.

(8) N accepts creditors of ₹ 5500 to pay.

Prepare necessary accounts and prepare balance sheet after retirement also :

Ans. :

Revaluation Account

Dr | Cr

Particulars		Amt. (₹)	Particulars	Amt. (₹)
To Bad debt reserve A/c		5200	By Building A/c	30,000
(₹ 10,000 – bad debt ₹ 8000 –				
New bad debt reserve ₹ 7200)				
To Discount reserve on debtors A/c		3240		
To Furniture A/c		1560		
To Partners' capital A/c (Profit) :				
L	8000			
M	6000			
N	6000	20,000		
		30,000		**30,000**

Capital Accounts of Partners

Dr | Cr

Particulars	L (₹)	M (₹)	N (₹)	Particulars	L (₹)	M (₹)	N (₹)
To Advertisement campaign exp.	8000	6000	6000	By Balance b/d	1,80,000	1,00,000	90,000
To M's capital A/c (goodwill)	9000	–	6000	By Investment fluctuation reserve A/c	2000	1500	1500
To M's loan A/c	–	1,16,500	–	By Revaluation A/c	8000	6000	6000
To Current A/c	19,880	–	–	By L's capital A/c (goodwill)	–	9000	–
To Balance c/f	1,53,120	–	1,10,880	By N's capital A/c (goodwill)	–	6000	–
				By Creditors A/c	–	–	5500
				By Current A/c	–	–	19,880
	1,90,000	**1,22,500**	**1,22,880**		**1,90,000**	**1,22,500**	**1,22,880**

Balance Sheet as on 1-4-2016 After Retirement

Liabilities		Amt. (₹)	Assets		Amt. (₹)
M's loan		1,16,500	N's current A/c		19,880
L's current A/c		19,880	Debtors	80,000	
Capital Accounts :			– Bad debt	8000	
L	1,53,120			72,000	
N	1,10,880	2,64,000	– Bad debt reserve	7200	
Creditors (₹ 60,000 – ₹ 5500)		54,500		64,800	
			– Discount reserve	3240	61,560
			Stock		32,000
			Investments		50,000
			Building		2,50,000
			Furniture		28,440
			Cash		13,000
		4,54,880			**4,54,880**

Explanation : (1) Distribution of goodwill

Old ratio of L, M and N = 4:3:3

Share of M to be distributed between L and N in ratio of 3:2.

∴ Gaining ratio of L and N = 3:2

M's share of goodwill = $50,000 \times \frac{3}{10}$ = ₹ 15,000

M's goodwill ₹ 15,000 is to be given by L and N in their gaining ratio 3:2.

Journal Entries :

L's capital A/c...Dr	9000	
N's capital A/c...Dr	6000	
To M's capital A/c...Dr		15,000

(2) New profit and loss sharing ratio of L and N

Old profit and loss sharing ratio of L, M and N = 4:3:3

Share of M $\frac{3}{10}$, which is gained by L and N in the ratio of 3:2.

∴ L's gain = $\frac{3}{10} \times \frac{3}{5} = \frac{9}{50}$

N's gain = $\frac{3}{10} \times \frac{2}{5} = \frac{6}{50}$

New share = Old share + Gain

∴ Share of L = $\frac{4}{10} + \frac{9}{50} = \frac{20+9}{50} = \frac{29}{50}$

Share of N = $\frac{3}{10} + \frac{6}{50} = \frac{15+6}{50} = \frac{21}{50}$

∴ New ratio = 29:21

(3) **Adjustment of total capital of new firm according to new profit sharing ratio of L and N**

Capital of L (₹ 1,90,000 − ₹ 17,000)	= ₹		1,73,000
Capital of N (₹ 1,03,000 − ₹ 12,000)	= ₹		91,000
Total capital of new firm	= ₹		2,64,000

Total capital to be distributed in the new profit-loss sharing ratio = 29:21

∴ New capital of L = 2,64,000 × $\frac{29}{50}$ = ₹ 1,53,120

New capital of N = 2,64,000 × $\frac{21}{50}$ = ₹ 1,10,880

Illustration 22 : P, Q and R are partners in a firm sharing profit and loss equally. Balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Trademark		5400
P	9000		Land-Building		10,000
Q	6000		X Ltd.'s share		1500
R	6000	21,000	Stock		3000
General reserve		1200	Debtors	3000	
Investment fluctuation fund		360	− Bad debt reserve	240	2760
Creditors		4600	Cash-Bank		1500
			Profit-loss A/c		3000
		27,160			**27,160**

R retired on 31 March 2016, following terms were decided at the time of retirement :

(1) Goodwill is to be valued at 3 times the average profit of last five years.

(2) Value of land and building is ₹ 15,000.

(3) Market value of X Ltd.'s share is ₹ 1200.

(4) All debtors are good.

(5) A provision of ₹ 2000 for outstanding salary is to be made.

(6) Last four years profit of the firm was as under :

2011-12 ₹ 6000

2012-13 ₹ 2000

2013-14 ₹ 3000

2014-15 ₹ 2000

(7) Share of R will be gained by P.

(8) Amount due to R is to be paid in cash which is brought in by P and Q in such a way as to make their capitals in proportionate to their new profit and loss sharing ratio.

Prepare necessary accounts and new balance sheet.

Ans. :

Revaluation Account

Dr | Cr

Particulars		Amt. (₹)	Particulars	Amt. (₹)
To Outstanding salary A/c		2000	By Bad debt reserve A/c	240
To Partners' capital A/c (Profit) :			By Land-building A/c	5000
P	1080			
Q	1080			
R	1080	3240		
		5240		**5240**

Capital Accounts of Partners

Dr | Cr

Particulars	P (₹)	Q (₹)	R (₹)	Particulars	P (₹)	Q (₹)	R (₹)
To Profit and loss A/c	1000	1000	1000	By Balance b/d	9000	6000	6000
To R's capital A/c	2000	–	–	By General reserve A/c	400	400	400
To Cash-bank A/c	–	–	8500	By Investment fluctuation fund	20	20	20
To Balance b/d	15,000	7500	–	By P's Capital A/c (goodwill)	–	–	2000
				By Revaluation A/c	1080	1080	1080
				By Cash-bank A/c	7500	1000	–
	18,000	**8500**	**9500**		**18,000**	**8500**	**9500**

Cash-Bank Account

Dr | Cr

Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	1500	By R's capital A/c	8500
To P's capital A/c	7500	By Balance c/d	1500
To Q's capital A/c	1000		
	10,000		**10,000**

Balance Sheet as on 1-4-2016 After Retirement

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Land-Building	15,000
P	15,000		X Ltd.'s share	1200
Q	7500	22,500	Stock	3000
Creditors		4600	Debtors	3000
Outstanding salary		2000	Cash-bank	1500
			Trademark	5400
		29,100		**29,100**

Explanation : (1) Valuation and distribution of goodwill

Average profit $= \frac{6000 + 2000 + 3000 + 2000 - 3000}{5} =$ ₹ 2000

Goodwill = ₹ 2000 × 3 = ₹ 6000

R's share in goodwill $= 6000 \times \frac{1}{3} =$ ₹ 2000

∴ R's share of profit is to be transferred to P.

∴ P gives goodwill to R.

Journal Entries :

P's capital A/c...Dr	2000	
To R's capital A/c...Dr		2000

(2) New profit-loss sharing ratio

Old sharing ratio of P, Q and R = 1:1:1

R retires and his share is gained by P.

New share = Old share + Gain

∴ P's share $= \frac{1}{3} + \frac{1}{3} = \frac{2}{3}$

Q's share $= \frac{1}{3} + 0 = \frac{1}{3}$

∴ New profit-loss sharing ratio = 2:1

(3) New capital of P and Q

	P's capital (₹ 10,500 – ₹ 3000)	= ₹ 7500
+	Q's capital (₹ 7500 – ₹ 1000)	= ₹ 6500
+	Paid to R (Additional capital)	= ₹ 8500
	Total capital of new firm	= ₹ 22,500

∴ New capital of P $= 22{,}500 \times \frac{2}{3} =$ ₹ 15,000

New capital of Q $= 22{,}500 \times \frac{1}{3} =$ ₹ 7500

Illustration 23 : E, F and G are partners sharing profit and loss in the ratio of 4:3:3. E retires on 31-3-2015. Balance sheet of the firm on that day was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Goodwill	1000
E	8000		Land-building	6000
F	5000		Furniture	4000
G	2000	15,000	Stock	6600
General reserve		2000	Debtors	9000
Creditors		8000	Cash	400
Bills payable		2000		
		27,000		**27,000**

Following conditions were decided at the time of retirement :

(1) Value of goodwill is ₹ 4000.

(2) Value of fixed assets is to be appreciated by 20 %.

(3) Stock is found overvalued by 10 %.

(4) New profit-loss sharing ratio of F and G is decided at 4:1.

(5) Amount due to E is to be paid in cash and casn balance of ₹ 1000 in the new firm is to be maintained. For this purpose F and G brought cash in such a way as to make their capitals proportionate to their new profit sharing ratio.

Prepare necessary accounts and balance sheet of the new firm.

Ans. :

Revaluation Account

Dr | Cr

Particulars		Amt. (₹)	Particulars	Amt. (₹)
To Stock A/c		600	By Land-building A/c	1200
To Partners capital A/c (Profit) :			By Furniture A/c	800
E	560			
F	420			
G	420	1400		
		2000		**2000**

Capital Accounts of Partners

Dr | Cr

Particulars	E (₹)	F (₹)	G (₹)	Particulars	E (₹)	F (₹)	G (₹)
To Goodwill A/c	400	300	300	By Balance b/d	8000	5000	2000
To E's capital A/c	–	1600	–	By General reserve A/c	800	600	600
To G's capital A/c	–	400	–	By F's capital A/c	1600	–	400
To Cash A/c	10,560	–	–	By Revaluation A/c	560	420	420
To Balance c/f	–	14,400	3600	By Cash A/c	–	10,680	480
	10,960	**16,700**	**3900**		**10,960**	**16,700**	**3900**

Cash Account

Dr | Cr

Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Balance b/d	400	By E's capital A/c	10,560
To F's capital A/c	10,680	By Balance c/f	1000
To G's capital A/c	480		
	11,560		**11,560**

Balance Sheet as on 1-4-2015 After Retirement

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Creditors		8000	Land-Building	7200
Bills payable		2000	Furniture	4800
Capital Accounts :			Stock	6000
F	14,400		Debtors	9000
G	3600	18,000	Cash	1000
		28,000		**28,000**

Explanation : (1) Gaining ratio

Old profit-loss sharing ratio of E, F and G = 4:3:3

New profit-loss sharing ratio of F and G = 4:1

Gain = New share − Old share

$F = \frac{4}{5} - \frac{3}{10} = \frac{5}{10}$

$G = \frac{1}{5} - \frac{3}{10} = -\frac{1}{10}$ (Sacrifice)

(2) Distribution of goodwill

G sacrifice his share, so he will receive goodwill.

Goodwill receivable by E = $\frac{4}{10} \times 4000$ = ₹ 1600

Goodwill payable by F = $\frac{5}{10} \times 4000$ = ₹ 2000

Goodwill receivable by G = $\frac{1}{10} \times 4000$ = ₹ 400

Journal Entries :

F's capital A/c...Dr	2000	
To E's capital A/c		1600
To G's capital A/c		400

(3) : New capital of F and G

F's capital (₹ 6020 − ₹ 2300) = ₹ 3720

G's capital (₹ 3420 − ₹ 300) = ₹ 3120

Additional necessary capital = ₹ 11,160

(Paid to E ₹ 10,560 + Required closing cash ₹ 1000 − Opening balance of cash ₹ 400)

Total capital of F and G = ₹ 18,000

∴ New capital of F = 18,000 × $\frac{4}{5}$ = ₹ 14,400

New capital of G = 18,000 × $\frac{1}{5}$ = ₹ 3600

9. Determination of Amount Payable to the Deceased Partner and Payment to his Executor

The retirement of a partner normally takes place at a planned date but the death of partner may occur any time. When a partner dies, his heirs are entitled to receive the amount due to the deceased partner. The heirs of the deceased partner are also entitled to receive the share of profits of the firm from the begining of the year to the date of death, interest on capital, salary etc. as well. The heirs of the deceased partner are entitled to receive the following :

(i) The amount standing to the credit of the deceased partner's capital account and current account

(ii) His share of accumulated profits and reserves

(iii) His share of profit of the revaluation account

(iv) His share in the goodwill of the firm

(v) His share in profits of the firm form the begining of the year to the date of death

(vi) Interest on capital upto the date of his death if provided by the partnership deed

(vii) His salary or commission upto the date of his death, if provided by the partnership deed

(viii) Loan given to the firm and its interest upto the date of his death

Following amounts are debited to his capital account :

(i) Debit balance of current account

(ii) His share in the loss of revaluation account

(iii) His share in accumulated losses

(iv) His share in deffered revenue expenditure

(v) His share in the old goodwill of the firm shown in the books of the firm

(vi) His drawings

(vii) Interest on drawings

(viii) His share in the loss that may have occurred till the date of his death, from the last balance sheet

The above adjustments are made in the capital account of the deceased partner and thereafter the balance of the capital account is transferred to his executor's account.

Deceased partners' capital A/c...Dr

To deceased partners' executor's A/c

- **Profit share to the deceased partner :**

He is entitled to receive his share in profit of the firm from the beginning of the year to the date of death. If he dies during the year before year ends, his share in profit is calculated without calculating the profit for the year of death. Therefore his share in profit from the beginning of the year till the date of death is calculated on the basis of the past profit or sales as follows :

(1) On the basis of last year's profit

(2) On the basis of average profit of past few years

(3) On the basis of previous year's sales and profit

e.g. 'A' died on 30-6-2016. His share in profit is $\frac{1}{5}$. Financial year ended on 31st March. Last three year's profit is as under :

2013-14 ₹ 80,000

2014-15 ₹ 60,000

2015-16 ₹ 40,000

Sales for the year 2015-16 amounted to ₹ 2,00,000. Sales from the first three months of current year is ₹ 60,000.

Find out the deceased partners' share in the profit of the firm under following basis :

(1) On the basis of last year's profit

(2) On the basis of average profit of last three years

(3) On the basis of last year's sales and profit

Ans. : (1) On the basis of last year's profit :

Profit share for three months from 1-4-2016 to 30-6-2016 will be payable to A. Last year, 2015-16 profit is ₹ 40,000.

Share in profit of A = ₹ 40,000 $\times \frac{1}{5} \times \frac{3}{12}$ = ₹ 2000

(2) On the basis of average profit of last three years :

Average profit = $\frac{80,000 + 60,000 + 40,000}{3}$ = ₹ 60,000

A's share of profit = ₹ 60,000 $\times \frac{1}{5} \times \frac{3}{12}$ = ₹ 3000

(3) On the basis of last year's profit and sales :

Sales of 2015-16 ₹ 2,00,000 : Profit ₹ 40,000

Three months of 2016-17 sales ₹ 60,000 : (?)

$\frac{40,000 \times 60,000}{2,00,000}$ = ₹ 12,000 (Profit of the firm for 3 months)

Profit share of B = 12,000 $\times \frac{1}{5}$ = ₹ 2400

B's share of profit is payable before accounting year ends. Following journal entry is passed to give profit share to B.

Profit and loss suspense A/c...Dr

To B's capital A/c

Other payments which affect profit like interest on capital, interest on loan, salary, commission etc. are also transferred to the profit and loss suspense account. For this journal entry will be :

(i) Interest on capital A/c...Dr

Interest on loan A/c...Dr

Salary A/c...Dr

Commission A/c...Dr

To Deceased partners' capital A/c

(ii) Profit and loss suspense A/c...Dr

To Interest on capital A/c

To Interest on loan A/c

To Salary A/c

To Commission A/c

Deceased Partners' Capital Account

Dr | Cr

Particulars	Amt. (₹)	Particulars	Amt. (₹)
To Current A/c (Debit balance)	✓	By Balance b/d	✓
To Revaluation A/c		By Current A/c (Credit balance)	✓
(Share in loss of revaluation account)	✓	By Reserve A/c (Share in reserve)	✓
To Profit and loss A/c		By Profit and loss A/c	
(Accumulated losses)	✓	(Share in accumulated profit)	✓
To Goodwill A/c - written off		By Revaluation A/c (Share in profit)	✓
(Share in old goodwill)	✓	By Other partners' capital A/c	
To Drawings A/c	✓	(Share in goodwill)	✓
To Interest on drawings A/c	✓	By Interest on capital A/c	✓
To Advertisement campaign exp. A/c	✓	By Salary or commission A/c	✓
To Profit and loss suspense A/c		By Loan A/c (given to firm)	✓
(Share in loss till the date of death)	✓	By Interest on loan A/c	✓
		By Profit and loss suspense A/c	
		(Share in profit till the date of death)	✓
	✓✓✓		✓✓✓

- **Payment to deceased partner :**

Payment to the executors of deceased partner is made as provided in the partnership deed or as agreed by the remaining partners and the executors. The dues may be paid :

Amount payable to the deceased partner is paid as under :

(1) Full in one instalment

(2) In more than one instalment

Following journal entries are passed when the payment is made as per above method :

(1) Full amount is paid in one installment,

Deceased partners' executors' A/c...Dr

To Bank A/c

(2) When payment is made in more than one instalment : In this case the executor is entitled to interest at 6 % p.a. unless agreed otherwise. As per Indian Partnership Act, 1932 the executor has option to take the share of profit instead of interest.

When instalment with interest is paid, following journal entry will be passed :

(i) When interest is due :

Interest A/c ...Dr

To Deceased partners' executors' A/c

(ii) When installment is paid including interest :

Deceased partners' executors' A/c...Dr

To Bank A/c

Illustration 24 : X, Y and Z are the partners sharing profit and loss in the ratio of 5:3:2. Balance sheet of the firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities		**Amt. (₹)**	**Assets**	**Amt. (₹)**
Capital Accounts :			Fixed capital	80,000
X	50,000		Debtors	20,000
Y	80,000		Stock	80,000
Z	70,000	2,00,000	Cash	30,000
General reserve		20,000	Advertisement campaign expenditure	40,000
Creditors		30,000		
		2,50,000		**2,50,000**

Z died as on 31-12-2016. The terms of partnership deed are as under :

(1) Share of profit for the period from the closing of the last financial year to the date of death on the basis of the last year's profit to be given.

(2) Goodwill of the firms is to be valued on the basis of twice the average of the past three years' profits. Profit of last three years was as under :

2013-14 ₹ 80,000

2014-15 ₹ 70,000

2015-16 ₹ 60,000

Calculate amount payable to Z's executor by preparing his capital.

Ans. :

Z's Capital Account

Dr Cr

Particulars	**Amt. (₹)**	**Particulars**	**Amt. (₹)**
To Advertisement campaign expenditure	8000	By Balance b/d	70,000
To Z's executors' A/c	1,03,000	By General reserve A/c	4000
		By Profit and loss suspense A/c (Share in profit)	9000
		By X's capital A/c (goodwill)	17,500
		By Y's capital A/c (goodwill)	10,500
	1,11,000		**1,11,000**

Explanation : (1) Z's share in profit

On the basis of last year, 2015-16 profit, from 1-4-2016 to till date of death 31-12-2016, for 9 months profit is payable to Z.

$$Z\text{'s share in profit} = 60{,}000 \times \frac{2}{10} \times \frac{9}{12}$$

$$= ₹\ 9000$$

(2) Valuation of goodwill and share of Z in goodwill

$$\text{Average profit} = \frac{80{,}000 + 70{,}000 + 60{,}000}{3}$$

$$= ₹\ 70{,}000$$

Goodwill of firm = ₹ 70,000 × 2

= ₹ 1,40,000

$$Z\text{'s goodwill} = 1{,}40{,}000 \times \frac{2}{10}$$

= ₹ 28,000

X and Y will give goodwill to Z in their gaining ratio :

Old ratio of X, Y and Z = 5:3:2

Old ratio of X and Y = Gaining ratio = 5:3

$$\text{Goodwill given by X} = ₹\ 28{,}000 \times \frac{5}{8}$$

= ₹ 17,500

$$\text{Goodwill given by Y} = ₹\ 28{,}000 \times \frac{3}{8}$$

= ₹ 10,500

Illustration 25 : A, B and C are the partners in a firm. Following are the balances as on 31-3-2015 in the books of the firm.

Capital : A ₹ 90,000, B ₹ 50,000, C ₹ 60,000

Contigency reserve ₹ 9000; Investment fluctuation reserve ₹ 3000; Goodwill ₹ 15,000

B died as on 30-6-2015

It was agreed by the remaining partners that :

(1) Interest on capital to B is to be allowed 12 % p.a.

(2) Drawing of B was ₹ 6000. Interest on drawing ₹ 300 will be charged.

(3) B's share of goodwill is to be valued at the profits credited to his account during the previous three completed years.

(4) B's share of profit is to be allowed on the basis of average of three completed years' profit before death. Profit of last three years was ₹ 60,000, ₹ 70,000 and ₹ 50,000 respectively.

(5) B's executors is to be paid ₹ 9200 immediately and the balance in two equal yearly instalments with interest at 6 % p.a.

(6) Profit and loss sharing ratio of A and C is to be kept 2:1 after B's death. Prepare B's executor's account and executor's loan account till it is finally paid.

Ans. :

B's Executor's Account

Dr | Cr

Date	Particulars	Amt. (₹)	Date	Particulars	Amt. (₹)
1-7-15	To Goodwill A/c	5000	1-7-15	By B's capital A/c	50,000
”	To Drawings A/c	6000	”	By Contigency reserve A/c	3000
”	To Interest on drawings A/c	300	”	By Investment fluctuation reserve A/c	1000
”	To Bank A/c	9200			
”	To B's executor's loan A/c	1,00,000	”	By Capital's Interest A/c	1500
				By A's capital A/c	60,000
				By Profit and loss suspense A/c	5000
		1,20,500			**1,20,500**

B's Executor's Loan Account

Dr | Cr

Date	Particulars	Amt. (₹)	Date	Particulars	Amt. (₹)
31-3-16	To Balance c/f	1,04,500	1-7-15	By B's executor's A/c	1,00,000
			31-3-16	By Interest A/c (₹ 1,00,000 $\times \frac{6}{100} \times \frac{9}{12}$)	4500
		1,04,500			**1,04,500**
30-6-16	To Bank A/c (50,000 + 4500 + 1500)	56,000	1-4-16	By Balance b/d	1,04,500
			30-6-16	By Interest A/c (₹ 1,00,000 $\times \frac{6}{100} \times \frac{3}{12}$)	1500
31-3-17	To Balance c/f	52,250	31-3-17	By Interest A/c (₹ 50,000 $\times \frac{6}{100} \times \frac{9}{12}$)	2250
		1,08,250			**1,08,250**
30-6-17	To Bank A/c (₹ 50,000 + ₹ 2250 + ₹ 750)	53,000	1-4-17	By Balance b/d	52,250
			30-6-17	By Interest A/c (₹ 50,000 $\times \frac{6}{100} \times \frac{3}{12}$)	750
		53,000			**53,000**

Explanation : (1) Interest on capital

₹ 50,000 $\times \frac{12}{100} \times \frac{3}{12}$ = ₹ 1500

(2) Gaining ratio

Old ratio of A, B and C = 1:1:1

New ratio of A and C = 2:1

Gain = New share − Old share

A's gain = $\frac{2}{3} - \frac{1}{3} = \frac{1}{3}$

C's gain = $\frac{1}{3} - \frac{1}{3} = 0$. Entire share of B received by A.

(3) Share of goodwill payable to B

Goodwill of B to be calculated at the profits credited to his account during the previous three completed years.

Average profit of last three years = ₹ 60,000 + ₹ 70,000 + ₹ 50,000 = ₹ 1,80,000

Goodwill payable to B = ₹ 1,80,000 × $\frac{1}{3}$ = ₹ 60,000

A will give goodwill to B

(4) Share in profit of B

Average profit of last three years = $\frac{60{,}000 + 70{,}000 + 50{,}000}{3}$ = ₹ 60,000

B's Share in profit = ₹ 60,000 × $\frac{1}{3} \times \frac{3}{12}$ = ₹ 5000

Note : As per Partnership Act 1932, the deceased partners' executors are entitled to interest at 6 % p.a. on their loan.

Illustration 26 : M, N and O are the partners sharing profit and loss in the ratio of 2:1:2. Balance sheet as on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Land-building	1,00,000
M	1,00,000		Machinery	60,000
N	60,000		Stock	36,000
O	80,000	2,40,000	Debtors	40,000
General reserve		10,000	Cash	11,000
Workmen compensation reserve		18,000	Loan to O	30,000
Creditors		42,000	O's current A/c	4000
Bad debt reserve		6000	Advertisement campaign expenditure	5000
Current Accounts :			Profit-loss A/c	60,000
M	20,000			
N	10,000	30,000		
		3,46,000		**3,46,000**

O died as on 1-12-2016. Provisions of partnership deed were as under :

(1) Land-building is to be appreciated by 10 %. (2) Value of machinery is to be reduced by 5 %.

(3) Provision for doubtful debts is to be kept at 10 % on debtors.

(4) Goodwill is to be valued at 3 years' purchase of the average profit of last 5 years.

(5) Previous 4 years profit was as under :

2011-12	₹ 80,000	2012-13	₹ 60,000
2013-14	₹ 70,000	2014-15	₹ 50,000

(6) O's share of profit till the date of his death based on last year's profit.

(7) New profit and loss sharing ratio of M and N is decided at 3:2.

(8) O's executors is to be paid ₹ 6800 immediately and the balance in 4 equal half yearly instalments with interest at 12 % p.a.

Prepare O's capital account and O's executor's account till it is finally paid.

Ans. :

O's Capital Account

Dr | Cr

Date	Particulars	Amt. (₹)	Date	Particulars	Amt. (₹)
1-12-16	To Advertisement campaign expenditure A/c	2000	1-12-16	By Balance b/d	80,000
,,	To Profit and loss A/c	24,000	,,	By General reserve A/c	4000
,,	To O's loan A/c	30,000	,,	By Workmen compensation reserve A/c	7200
,,	To O's current A/c	4000	,,	By Revaluation A/c	3600
,,	To Profit and loss suspense A/c (Loss)	16,000	,,	By M's capital A/c (goodwill)	24,000
,,	To Bank A/c	6800	,,	By N's capital A/c (goodwill)	24,000
,,	To O's executor's A/c	60,000			
		1,42,800			**1,42,800**

O's Executor's Account

Dr | Cr

Date	Particulars	Amt. (₹)	Date	Particulars	Amt. (₹)
31-3-17	To Balance c/f	62,400	1-12-16	By O's capital A/c	60,000
			31-3-17	By Interest A/c (₹ 60,000 $\times \frac{12}{100} \times \frac{4}{12}$)	2400
		62,400			**62,400**
31-5-17	To Bank A/c (15,000 + 2400 + 1200)	18,600	1-4-17	By Balance b/d	62,400
30-11-17	To Bank A/c (15,000 + 2700)	17,700	31-5-17	By Interest A/c (₹ 60,000 $\times \frac{12}{100} \times \frac{2}{12}$)	1200
31-3-18	To Balance c/f	31,200	30-11-17	By Interest A/c (₹ 45,000 $\times \frac{12}{100} \times \frac{6}{12}$)	2700
			31-3-18	By Interest A/c (₹ 30,000 $\times \frac{12}{100} \times \frac{4}{12}$)	1200
		67,500			**67,500**
31-5-18	To Bank A/c (₹ 15,000 + ₹ 1200 + ₹ 600)	16,800	1-4-18	By Balance b/d	31,200
30-11-18	To Bank A/c (₹ 15,000 + ₹ 900)	15,900	31-5-18	By Interest A/c (₹ 30,000 $\times \frac{12}{100} \times \frac{2}{12}$)	600
			30-11-18	By Interest A/c (₹ 15,000 $\times \frac{12}{100} \times \frac{6}{12}$)	900
		32,700			**32,700**

Explanation : (1) **Revaluation Account**

Dr Cr

Particulars		Amt. (₹)	Particulars	Amt. (₹)
To Machinery A/c		3000	By Land-building A/c	10,000
To Partners' capital A/c (Profit) :			By Bad debt reserve A/c	2000
M	3600			
N	1800			
O	3600	9000		
		12,000		**12,000**

(2) Valuation of goodwill

5 years average profit $= \frac{80{,}000 + 60{,}000 + 70{,}000 + 50{,}000 - 60{,}000}{5}$

$= \frac{2{,}00{,}000}{5}$

$=$ ₹ 40,000

Goodwill $= 40{,}000 \times 3$

$=$ ₹ 1,20,000

(3) Distribution of goodwill

Share of O in goodwill $= 1{,}20{,}000 \times \frac{2}{5}$

$=$ ₹ 48,000

Gaining ratio of M and N :

Gain = New share − Old share

$M = \frac{3}{5} - \frac{2}{5} = \frac{1}{5}$

$N = \frac{2}{5} - \frac{1}{5} = \frac{1}{5}$

∴ Gaining ratio of M and N = 1:1

∴ Goodwill is to be given by M and N to O in equal proportion.

Journal Entry :

M's capital A/c...Dr	24,000	
N's capital A/c...Dr	24,000	
To O's capital A/c...Dr		48,000

(4) : O's share in profit :

O died as 1-12-2016, so O will receive his share in profit from 1-4-2016 to 1-12-2016 i.e. for 8 months.

Last year 2015-16, the amount of loss is ₹ 60,000.

∴ O's share in loss $= 60{,}000 \times \frac{8}{12} \times \frac{2}{5}$

$=$ ₹ 16,000

Illustration 27 : A, B and C are the partners sharing profit and loss in the ratio of 3:2:1. The balance sheet of the firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Creditors		10,000	Goodwill	30,000
Partners' loan :			Patents	25,000
A	12,000		Building	80,000
B	20,000	32,000	Furniture	60,000
General reserve		18,000	Stock	50,000
Capital Accounts :			Debtors	60,000
A	90,000		Cash	15,000
B	90,000			
C	80,000	2,60,000		
		3,20,000		**3,20,000**

B died on 30-6-2016. Under the partnership agreement, the executor of B is entitled to receive following:

(1) Interest on his capital at 10 % p.a.

(2) Share in general reserve.

(3) His loan and outstanding interest on loan.

(4) Value of goodwill is decided at ₹ 30,000.

(5) Share of profit upto the date of death on the basis of last year's sales and profit. Sales for the year 2015-16 was ₹ 12,00,000. First three months sales of current year was ₹ 4,50,000. Net profit for the year 2015-16 was ₹ 2,40,000.

(6) Patents are to be written off fully. Building is to be appreciated by 20 %.

Prepare the balance sheet as on 30-6-2016 after the death of B.

Ans. :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Creditors		10,000	Building	96,000
A's loan		12,000	Furniture	60,000
B's executor's A/c		1,45,550	Stock	50,000
Capital Accounts :			Debtors	60,000
A	72,000		Cash	15,000
C	74,000	1,46,000	Profit and loss suspense A/c (30,000 profit + 2250 Interest on capital + 300 interest on loan)	32,550
		3,13,550		**3,13,550**

Explanation : (1) **Revaluation Account**

Dr Cr

Particulars	Amt. (₹)	Particulars		Amt. (₹)
To Patents A/c	25,000	By Building A/c		16,000
		By Partners' capital A/c (Profit) :		
		A	4500	
		B	3000	
		C	1500	9000
	25,000			**25,000**

(2) **Capital Accounts of Partners**

Dr Cr

Particulars	A (₹)	B (₹)	C (₹)	Particulars	A (₹)	B (₹)	C (₹)
To Revaluation A/c	4500	3000	1500	By Balance b/d	90,000	90,000	80,000
To Goodwill A/c	15,000	10,000	5000	By General reserve A/c	9000	6000	3000
To B's capital A/c	7500	–	2500	By Interest on capital A/c	–	2250	–
To B's executors' A/c	–	1,45,550	–	By B's loan A/c	–	20,000	–
To Balance c/f	72,000	–	74,000	By Interest on B's loan A/c	–	300	–
				By A's capital A/c	–	7500	–
				By C's capital A/c	–	2500	–
				By Profit and loss suspense A/c	–	30,000	–
	99,000	**1,58,550**	**83,000**		**99,000**	**1,58,550**	**83,000**

(3) Interest on capital to B from 1-4-2016 to 30-6-2016 = 3 months

$= ₹\ 90,000 \times \frac{10}{100} \times \frac{3}{12} = ₹\ 2250$

(4) Outstanding interest on loan to B for 3 months at 6 % p.a. (As not stated in the partnership deed)

$= ₹\ 20,000 \times \frac{6}{100} \times \frac{3}{12} = ₹\ 300$

(5) Distribution of goodwill and share of B in goodwill

Old ratio of A, B and C = 3:2:1

B died; gaining ratio of A and C = 3:1

Share of B in goodwill = $\frac{2}{6} \times 30,000 = ₹\ 10,000$

Which will be given by A and C in the ratio of 3:1.

Journal Entry :

A's capital A/c...Dr	7500	
C's capital A/c...Dr	2500	
To B's capital A/c		10,000

(6) B's share in the profit of the firm from 1-4-2016 to 30-6-2016 means 3 month's profit

If sales of 2015-16 ₹ 12,00,000 : Net profit ₹ 2,40,000

∴ 3 months sales of 2016-17 ₹ 4,50,000 : (?)

$\frac{2,40,000 \times 4,50,000}{12,00,000}$ = ₹ 90,000 (Three month's profit of the firm)

B's share in profit = 90,000 × $\frac{2}{6}$ = ₹ 30,000

Note : B's share in profit, interest on capital and interest on loan should be transferred to profit and loss suspense account and it is shown on assets side of balance sheet.

	Interest on capital	₹	2250
+	Interest on loan	₹	300
+	Share in profit	₹	30,000
		₹	32,550

EXERCISE

1. Select appropriate alternative for each question :

(1) Debit balance of profit and loss account shown in the balance sheet at the time of retirement of a partner is ....

(a) recorded on the debit side of all partners' capital accounts including the retiring partner in their old profit-loss sharing ratio

(b) recorded on the credit side of all partners' capital accounts including the retiring partner in their old profit-loss sharing ratio

(c) credit side of the retiring partners' capital account only

(d) debit side of the remaining partners' capital accounts in their gaining ratio

(2) Goodwill shown in the balance sheet at the time of the retirement of a partner is recorded as ....

(a) shown in new balance sheet, if decided by partners

(b) debit side of all partners' capital accounts in their old profit-loss sharing ratio

(c) credit side of all partners' capital accounts in their old profit-loss sharing ratio

(d) debit side of reriting partners' capital account only

(3) Goodwill payable to the retiring partner is recorded as ....

(a) credit side of all partners' capital accounts, in their old profit-loss sharing ratio

(b) credit side of all partners' capital accounts, in their gaining ratio

(c) debit side of continuing partners' capital accounts, in their gaining ratio

(d) debit side of continuing partners' capital accounts, in their new profit-loss sharing ratio

(4) When only old profit-loss sharing ratio is given, gaining ratio of remaining partners will be ....

(a) 1:1 (b) old ratio

(c) capital ratio (d) can not be calculated

(5) A partner, except the retiring partner also receives goodwill when ....
 (a) his capital is more
 (b) new share in new profit-loss sharing ratio is more than his old share
 (c) new share in new profit-loss sharing ratio is less than his old share
 (d) new share and old share are equal

(6) Loss of revaluation account at the time of retirement or death is recorded in .... account in .... ratio on .... side of the capital accounts.
 (a) remaining partners, new profit-loss sharing, debit
 (b) all partners, old profit-loss sharing, credit
 (c) all partners, old profit-loss sharing, debit
 (d) all partners, equal proportion, debit

(7) If partnership deed is silent, interest is payable at .... on unpaid amount payable to the retiring partner.
 (a) 10 % p.a. (b) 12 % p.a.
 (c) 6 % p.a. (d) zero

(8) Accounting year ends on 31-3-2016. A partner dies on 30-6-2016. Deceased partners' share in profit is $\frac{1}{3}$. Profit share payable to the partner is to be calculated on the basis of last year's profit ₹ 24,000. .... amount will be paid as share in profit at the time of death.
 (a) ₹ 8000 (b) ₹ 24,000
 (c) ₹ 1333 (d) ₹ 2000

(9) Sweta, Geeta and Jyoti are equal partners. Gita retires. Gita's share is gained by Sweta and Jyoti equally. New profit and loss sharing ratio of Sweta and Jyoti will be ....
 (a) 3:1 (b) 2:1
 (c) 1:2 (d) 1:1

(10) Workmen profit sharing fund is recorded as .... at the time of the retirement of a partner.
 (a) a liability in new balance sheet
 (b) credited to all partners' capital account in their old profit-loss sharing ratio
 (c) debited to all partners' capital account in their old profit-loss sharing ratio
 (d) credited to the retiring partners' capital account

2. Answer following questions in one sentence :

(1) State the circumstances of the retirement of a partner.

(2) Which important accounting aspects are considered at the time of the retirement or death of a partner ?

(3) Which balances are credited to all partners' capital accounts in their old profit-loss sharing ratio ?

(4) Which balances are debited to all partners' capital accounts in their old profit-loss sharing ratio ?

(5) Explain accounting treatment of old goodwill appearing in the balance sheet of the firm at the time of the retirement of a partner.

(6) Explain accounting treatment of the new goodwill of the firm valued at the time of the retirement of a partner.

(7) When and why the profit and loss adjustment account is prepared ?

(8) Who gives the share in goodwill to the retiring or deceased partner ? Why ?

3. Calculate the new profit and loss ratio and gaining ratio for the following questions :

(1) X, Y and Z are the partners sharing profit and loss in the ratio of 5:3:2. Z retires.

(2) A, B and C are the partners sharing profit and loss in the ratio of $\frac{1}{2}$, $\frac{1}{3}$ and $\frac{1}{6}$ respectively. (A) If A retires (B) If B retires (C) If C retires.

(3) P, Q and R are the partners sharing profit and loss in the ratio of 40 %, 20 % and 40 % respectively. Q retires. P is acquiring $\frac{3}{20}$ and R is acquiring $\frac{1}{20}$ from Q's share.

(4) M, N and O are the partners sharing profit and loss in the ratio of 3:2:1. M retires. N is acquiring $\frac{1}{10}$ from M's share and balance is acquired by O.

(5) C, B and D are the partners sharing profit and loss in the ratio of 4:5:3. D retires and his share is taken up by C and B in the ratio of 2:1.

(6) A, M and C are the partners sharing profit and loss in the ratio of 3:5:2. M retires and his share is taken up by C only.

(7) P, Q, R and S are the partners sharing profit and loss in the ratio of 4:3:2:1. Q retires and his share of profit is gained equally by R and S.

(8) M, N, O and P are the partners sharing profit and loss in the ratio of 5:3:2:2. N and P retired. N's share is acquired by O and P's share is acquired by M.

(9) A, B and C are the partners sharing profit and loss in the ratio of $\frac{1}{2}$, 30 % and $\frac{1}{5}$ respectively. B's share is taken over by A and C in the ratio of 3:2.

(10) A, B and C are the partners sharing profit and loss in the ratio of 5:3:2. B and C sharing profit in the ratio of 40 % and 60 % after the retirement of A.

(11) A, B and C are the partners sharing profit and loss in the ratio of 3:2:1. C retires. The new profit and loss sharing ratio of A and B is decided at 7:5.

(12) A, B and C are the partners sharing profit in the ratio of 4:5:1. Following journal entry for goodwill is passed at the time of the retirement of B :

A's capital A/c...Dr	6000	
C's capital A/c...Dr	4000	
To B's capital A/c...		10,000

(13) A, B, C and D are the partners sharing profit and loss in the ratio of 4:3:2:1. C retires. After the retirement of C, A will maintain his old profit share.

4. Give necessary entry of goodwill for the following :

(1) Akruti, Prakruti and Sanskruti are the partners sharing profit and loss in the ratio of 5:3:2. Sanskruti retires. At the time of her retirement the goodwill is valued at ₹ 30,000.

(2) X, Y and Z are the partners sharing profit and loss in equal proportions. Goodwill appears at ₹ 42,000 in the books of the firm. At the time of retirement of X, the goodwill of the firm is valued at ₹ 1,20,000.

(3) L, M, N and O are the partners sharing profit and loss in the ratio of 5:4:3:3. L retires on 1-4-2017. At the time of retirement of L, goodwill appears at ₹ 75,000 in the books of old firm. The new profit and loss sharing ratio of M, N and O is decided at 3:1:1. On L's retirement, the goodwill of the firm is valued at ₹ 90,000.

(4) A, B and C are the partners of a firm. B retires. At the time of B's retirement, the goodwill of the firm is valued at ₹ 60,000. The new profit-loss sharing ratio of A and C decided at 7:2.

(5) B, R, T and S are the partners sharing profit and loss in the ratio of 4:3:1:2. B retires. Goodwill is appearing in their books at ₹ 20,000 and at the time of B's retirement, goodwill is valued at ₹ 60,000. R, T and S decided to share the future profits of new firm in the ratio of 1:2:2.

(6) A, M, U and L are the partners sharing profit and loss in the ratio of 6:4:3:2. U retires. His capital account after making adjustments for reserves and profit on revaluation is ₹ 80,000. Remaining partners have agreed to pay him ₹ 1,40,000 in full settlement of his claim. The new profit-loss sharing ratio of A, M and L is decided at 6:5:4 after the retirement of U.

5. Dhaval, Kamal and Naval are the partners sharing profit and loss in the ratio of 2:2:1. Naval retires on 31-3-2016. Balance sheet of the firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Goodwill	10,000
Dhaval	30,000		Machinery	20,000
Kamal	20,000		Investments	10,000
Naval	10,000	60,000	Debtors	30,000
General reserve		5000	Stock	10,000
Investment fluctuation fund		2500	Cash-bank	5000
Bad debt reserve		2000		
Creditors		15,500		
		85,000		**85,000**

Following adjustments are agreed at the time of retirement :

(1) Value of machinery is ₹ 25,000 and value of stock is ₹ 5000.

(2) Value of investments is ₹ 8000, which is taken by Naval at this price.

(3) An amount of ₹ 5000 included in creditors is no longer payable.

(4) The provision for workmen compensation to be credited at ₹ 2000.

(5) The provision for doubtful debts is to be kept at 10 % on debtors.

(6) Goodwill of the firm is valued at ₹ 40,000.

Pass journal entries. Prepare necessary accounts and the balance sheet of the firm after Naval's retirement.

6. Rohit, Mohit and Virat are partners sharing profit and loss in the ratio of 4:3:2. Balance sheet of the firm as on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Goodwill		36,000
Rohit	1,60,000		Land-building		1,50,000
Mohit	96,000		Machinery		90,000
Virat	80,000	3,36,000	Stock		85,000
Reserve fund		45,000	Debtors	60,000	
Workmen compensation reserve		13,500	− Bad debt reserve	4000	56,000
Partners' loan :			Bank		63,000
Rohit	10,000		Advertisement campaign expenditure		4500
Mohit	16,000	26,000			
Creditors		64,000			
		4,84,500			**4,84,500**

Rohit retired on 1-4-2017. Terms of retirement is as under :

(1) Value of land-building is ₹ 1,80,000.

(2) Value of machinery is to be reduced by ₹ 15,000.

(3) Provision for doubtful debts is to be kept at 10 % on debtors.

(4) ₹ 5000 not payable to creditors.

(5) Valuation of goodwill is ₹ 1,80,000.

(6) New profit-loss sharing ratio of Mohit and Virat is 2:1.

(7) ₹ 20,000 are to be paid to Rohit and balance will be kept as loan.

Prepare Revaluation account, Partners' capital accounts and Balance sheet after retirement.

7. Vijay, Laxmi and Siddhi are the partners sharing profit and loss in the ratio of 5:3:2. Siddhi retired on 1-4-2016. Terms of retirement are as under :

(1) New profit-loss sharing ratio of Vijay and Laxmi is 2:3.

(2) Goodwill of the firm is valued at ₹ 60,000.

(3) Market value of investments is ₹ 40,000. Siddhi will take over investment at this value.

(4) ₹ 3000 to be written off from debtors and 5 % bad debt reserve is to be maintained.

(5) Value of stock shown in the book is ₹ 1000 more than its cost. It is to be recorded at cost.

(6) Claim of ₹ 7000 is accepted for workmen compensation.

(7) ₹ 12,000 to be paid to Siddhi immediately.

Balance sheet of the firm on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Land-building		1,30,000
Vijay	85,000		Machinery		70,000
Laxmi	64,000		Investments		60,000
Siddhi	71,000	2,20,000	Stock		35,000
Investment fluctuation fund		15,000	Debtors	23,000	
Workmen compensation fund		17,000	– Bad debt reserve	4000	19,000
Creditors		56,000	Cash		36,000
Provident fund		42,000			
		3,50,000			**3,50,000**

Prepare necessary accounts and balance sheet after retirement.

8. Jaya, Mamta and Smruti are the partners sharing profit and loss in the ratio of $\frac{2}{5}$, $\frac{5}{10}$ and $\frac{1}{10}$. Balance sheet of the firm on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Creditors		90,000	Goodwill	30,000
General reserve		70,000	Building	2,82,000
Capital Accounts :			Machinery	1,45,000
Jaya	2,00,000		Investments	33,000
Mamta	1,00,000		Stock	20,000
Smruti	90,000	3,90,000	Debtors	50,000
Current Accounts :			Loan to Smruti	30,000
Jaya	26,000		Current account : Smruti	10,000
Mamta	14,000	40,000		
Bad debt reserve		10,000		
		6,00,000		**6,00,000**

Smruti retired on 1-4-2017 as a partner. At the time of her retirement, partners decided that :

(1) ₹ 4000 is outstanding for rent payable.

(2) Interest on investment is receivable ₹ 2500.

(3) Investments to be sold for ₹ 35,000.

(4) Goodwill of the firm is valued at ₹ 2,00,000.

(5) Jaya and Mamta will share future profit in the ratio of 1:1.

Prepare necessary accounts and balance sheet after retirement.

9. Madhav, Radha and Gopi are the partners sharing profit and loss in the ratio of $\frac{1}{2}$, $\frac{1}{3}$ and $\frac{1}{6}$. Balance sheet of the firm on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Cash-bank		12,000
Madhav	1,36,000		Debtors	80,000	
Radha	50,000		− Bad debt reserve	5000	75,000
Gopi	54,000	2,40,000	Stock		62,000
Creditors		50,000	Investments (Market value ₹ 64,000)		58,000
Workmen compensation reserve		24,000	Patent		35,000
Employee provident fund		15,000	Building		75,000
Investment fluctuation reserve		12,000	Advertisement campaign expenditure		24,000
		3,41,000			**3,41,000**

Radha retired from 1-4-2016. Partners decided that :

(1) Value of patent is to be reduced by 20 % whereas value of building is to be reduced to 90 %.

(2) Liability of workmen compensation reserve is decided at ₹ 30,000.

(3) Bad debt reserve on debtors is to be increased by 5 %.

(4) ₹ 40,000 is to be paid to Radha as her share in goodwill.

(5) ₹ 500 received from bad debt written off earlier ₹ 3000.

(6) ₹ 5000 to be paid to Radha in cash and balance amount in two equal annual instalment with 10 % interest per annum.

Prepare Revaluation account, Partners' capital account and Balance sheet. Also prepare Radha's loan account till it is finally paid.

10. Deep, Jyoti and Geeta are the partners sharing profit and loss in the ratio of their capitals. Balance sheet of their firm as 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Goodwill		14,000
Deep	1,00,000		Land-building		2,90,000
Jyoti	1,50,000		Trademark		60,000
Geeta	1,00,000	3,50,000	Stock		50,000
General reserve		28,000	Debtors	40,000	
Creditors		60,000	− Bad debt reserve	6000	34,000
Provident fund		32,000	Bank		22,000
		4,70,000			**4,70,000**

Jyoti retired on the above date. Partners decided that,

(1) New profit and loss sharing ratio of Deep and Geeta is to be kept at 1:1. Goodwill of the firm valued at ₹ 70,000.

(2) Bad debt reserve on debtors is to be reduced upto 10 %.

(3) Stock is shown in the books at 25 % more than its cost, stock to be recorded at cost.

(4) ₹ 60,000 is paid for trademark during current year, which is for total 6 years.

(5) Liability of provident fund is decided at ₹ 35,000.

(6) Total capital of the new firm is to be kept as the total capital of the old firm. Deep and Geeta will maintain this capital in their new profit-loss sharing ratio. For this purpose the difference is to be transferred to their current accounts.

Prepare necessary accounts and balance sheet after retirement.

11. Moon, Star and Sun are the partners of a firm. Sun retires on 31-3-2017. Moon and Star will distribute future profit and loss in the ratio of 5:1. Balance sheet of their firm on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Building	2,40,000
Moon	1,60,000		Machinery	1,30,000
Star	2,00,000		Furniture	80,000
Sun	1,80,000	5,40,000	Stock	45,000
General reserve		90,000	Debtors	30,000
Creditors		60,000	Bank	1,75,000
Bills payable		10,000		
		7,00,000		**7,00,000**

Conditions of retirement were as under :

(1) Goodwill of the firm is valued at ₹ 60,000.

(2) Creditors are payable after one month, which are to be paid immediately at 12 % discount per annum.

(3) Computer, written off from the books is now valued at ₹ 12,000. Moon will take over the computer at this value.

(4) After retirement of Sun, Moon and Star will maintain their capital in the new profit and loss sharing ratio and difference is to be tansferred to bank account.

Prepare necessary accounts and balance sheet after retirement.

12. E, M and I are partners sharing profit and loss in the ratio of 5:3:2. Balance sheet of their firm on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital Accounts :			Building		1,20,000
E	60,000		Machinery		80,000
M	30,000		Stock		30,000
I	50,000	1,40,000	Debtors	40,000	
Reserve fund		50,000	– Bad debt reserve	2000	38,000
Workmen profit sharing fund		30,000	Cash		22,000
Creditors		70,000			
		2,90,000			**2,90,000**

I retired on 31-3-2017. Conditions of retirement were as under :

(1) I's profit share will be gained by E and M in the ratio of 2:3.

(2) Goodwill of the firm is valued at ₹ 1,00,000.

(3) Bad debt reserve on debtors is to be increased by 10 %.

(4) Building is valued at 110 %.

(5) Value of machinery is to be reduced by 10 %.

(6) Annual insurance premium of ₹ 24,000 is paid for the year ended on 30-6-2017.

(7) E and M will maintain total capital of the firm ₹ 1,00,000 in their new profit and loss sharing ratio after retirement of I.

Prepare necessary accounts and balance sheet after retirement.

13. L, B and W are the partners of a firm sharing profit and loss in the ratio of 2:2:1. Balance sheet of their firm on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital Accounts :			Goodwill	8000
L	20,000		Building	37,000
B	12,500		Debtors	13,000
W	5000	37,500	Stock	5500
General reserve		5000	Cash	2000
Creditors		20,000		
Outstanding expenses		3000		
		65,500		**65,500**

W retired on 1-4-2016. Terms of retirement were decided as under :

(1) Market value of building is ₹ 50,000.

(2) Book value of stock is 10 % more than its cost. Stock is to be recorded at its cost.

(3) Personal expenses of W ₹ 500 was debited to profit and loss account.

(4) Goodwill of the firm is valued at ₹ 80,000.

(5) L will gain $\frac{5}{40}$ and B will gain $\frac{3}{40}$ from W's share of profit.

(6) Amount due to W is to be paid in cash and the same amount will be brought in cash by L and B in such a manner that their capital may remain in their new profit-loss sharing ratio in the new firm.

Prepare necessary accounts and balance sheet of the new firm.

14. Chirag, Jigar and Keshav are the partners sharing profit and loss in ratio of 3:2:1. Balance sheet of their firm on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital :			Land-building		50,000
Chirag	30,000		Machinery		20,000
Jigar	20,000		Investments		10,000
Keshav	10,000	60,000	Stock		10,000
General reserve		6000	Debtors	20,000	
Creditors		44,000	– Bad debt reserve	2000	18,000
			Cash		2000
		1,10,000			**1,10,000**

Keshav retired on 31-3-2016. Following conditions were decided at the time of retirement :

(1) Value of land-building is to be increased by 20 %.

(2) Machinery is valued at 90 % of its book value.

(3) Market value of investment is 150 % of its book value.

(4) Bad debt reserve on debtors is to be reduced by 5 %.

(5) Goodwill of the firm is valued at ₹ 36,000.

(6) ₹ 2000 is outstanding for salary payable to an employee.

(7) Chirag and Jigar will bring necessary amount in cash in such a manner that amount due to Keshav is to be paid in cash and balance of cash may remain in the firm as working capital ₹ 14,000 and their capital in the new firm become proportionate to their new profit-loss sharing ratio.

Prepare necessary accounts and balance sheet of new firm.

15. E, F and G are the partners sharing profit and loss in the ratio of 4:3:3. E retires on 31-3-2017. Balance sheet of the firm on that date was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital :			Goodwill	1000
E	8000		Land-building	6000
F	5000		Free hold assets	3000
G	2000	15,000	Furniture	3000
General reserve		2000	Stock	6600
Creditors		8000	Debtors	7000
Bills payable		2000	Cash	400
		27,000		**27,000**

Following terms of retirement were decided in partnership agreement and among the partners :

(1) Goodwill of the firm is valued at ₹ 7000.

(2) Value of land-building ₹ 7000 and furniture ₹ 2000 is decided.

(3) Stock is over valued by 10 %. ₹ 5000 to be paid to E immediately and balance to be transferred to his loan account.

(4) F and G will bring necessary cash in equal proportion in such a manner that E is to be paid his dues fully and ₹ 2000 remain as working capital (cash).

Prepare profit and loss adjustment account, cash account, partners' capital accounts and balance sheet.

16. Kamal, Bimal and Vimal are the partners sharing profit and loss in the ratio of 1:2:3. Their balance sheet shows following balances on 31-3-2016.

Capital : Kamal ₹ 10,000, Bimal ₹ 20,000 and Vimal ₹ 30,000

General reserve	₹ 24,000
Loan of Vimal	₹ 10,000
Goodwill	₹ 12,000

Vimal died on 31-5-2016. Following conditions were provided in partnership deed :

(1) Goodwill of the firm is to be valued at two years purchase of average profit of last three years.

Profit of last three years were ₹ 25,000, ₹ 40,000 and ₹ 25,000.

(2) Profit share of the deceased partner till the date of death is to be decided on the basis of average profit of last three years.

(3) Interest on capital is to be allowed at 12 % per annum.

Prepare Vimal's capital account.

17. C, S and T are the partners of a firm sharing profit and loss in the ratio of 2:1:2. Balance sheet of their firm on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital :			Land-building	1,40,000
C	80,000		Investments	70,000
S	70,000		Stock	50,000
T	1,00,000	2,50,000	Debtors	25,000
Workmen accident compensation fund		10,000	Cash	20,000
T's loan		25,000	Advertisement suspense account	15,000
Creditors		35,000		
		3,20,000		**3,20,000**

T died on 30-6-2017. As per partnership deed, following accounting treatments are necessary to be given at the time of death of a partner :

(1) Interest on capital is to be allowed at 6 % per annum.

(2) Interest on drawings is to be charged at 12 % p.a. T withdrew ₹ 20,000 on 1-5-2017.

(3) Goodwill is to be valued at two times the average profit of last three years :

Profit of last three years was as under :

2014-15 ₹ 80,000, 2015-16 ₹ 75,000 and 2016-17 ₹ 85,000

(4) Profit share to be given on the basis of profit of previous year.

Prepare T's executor's account.

18. E, V and M are the partners of a firm sharing profit and loss in the ratio of 3:2:1. Balance sheet of their firm on 31-3-2016 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital :			Goodwill	24,000
E	1,00,000		Land-building	2,00,000
V	1,20,000		Machinery	60,000
M	90,000	3,10,000	Debtors	80,000
Investment reserve		10,000	Investments (Market value ₹ 26,000)	30,000
Bad debt reserve		6000	Cash	40,000
Provident fund		70,000	Profit-loss A/c	42,000
Workmen profit sharing fund		30,000		
Creditors		50,000		
		4,76,000		**4,76,000**

V died on 1-10-2016. As per partnership deed, following was decided among partners :

(1) Goodwill is valued at ₹ 1,20,000.

(2) New profit-loss sharing ratio of E and M decided at 2:1.

(3) V is to be given profit share till the date of his death on the basis of the profit of last year.

(4) 10 % reserve for bad debt to be provided on debtors.

(5) Land and building is valued 10 % more.

(6) ₹ 1000 salary per month is payable to V.

(7) ₹ 45,000 to be paid to V's executor immediately and balance amount in two equal yearly instalments with interest at 10 % per annum.

Prepare V's executor account and executor's loan account till it is finally paid.

19. A, T and M are the partners sharing profit and loss in the ratio of 4:1:1. Balance sheet of their firm on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital :			Land-building	12,000
A	15,000		Furniture	6000
T	12,000		Motor car	8000
M	9000	36,000	Debtors	15,000
General reserve		3000	Stock	6000
Creditors		17,000	Loan to M	9000
Bills payable		1000	Cash	1000
		57,000		**57,000**

M died on 1-7-2017. As per partnership agreement among partners :

(1) Value of land and building and furniture is to be increased by 10 %

(2) Cost of stock is ₹ 5500, which is to be brought in the books.

(3) ₹ 400 to be written off as bad debt from debtors.

(4) Goodwill is valued at ₹ 7200.

(5) M is to be given share in profit till the date of his death on basis of sales and net profit of last year. Sales of last year was ₹ 8,00,000. Sales of first three months of current year was ₹ 4,00,000. Net profit of last year was ₹ 2,40,000.

(6) ₹ 1850 to be paid to M's executor in cash and balance amount in two equal annual instalments with interest at 12 % interest per annum.

Prepare M's executor's account and executor's loan account till it is finally paid.

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