Accounting for Partnership : Basic Concepts — 2

Learning Objectives

After studying this chapter, you will be able to :

- *Define partnership and list its essential features;*
- *Identify the provisions of the Indian Partnership Act 1932 that are relevant for accounting;*
- *Prepare partners' capital accounts under fixed and fluctuating capital methods;*
- *Explain the distribution profit or loss among the partners and prepare the Profit and Loss Appropriation Account;*
- *Calculate interest on capital and drawing under various situations;*
- *Explain how guarantee for a minimum amount of profit affects the distribution of profits among the partners;*
- *Make necessary adjustments to rectify the past errors in partners capital accounts; and*
- *Prepare final accounts of a partnership firm;*

You have learnt about the preparation of final accounts for a sole proprietary concern. As the business expands, one needs more capital and larger number of people to manage the business and share its risks. In such a situation, people usually adopt the partnership form of organisation. Accounting for partnership firms has it's own peculiarities, as the partnership firm comes into existence when two or more persons come together to establish business and share its profits. On many issues affecting distribution of profits, there may not be any specific agreement between the partners. In such a situation the provisions of the Indian Partnership Act 1932 apply. Similarly, calculation of interest on capital, interest on drawings and maintenance of partners capital accounts have their own peculiarities. Not only that a variety of adjustments are required on the death of a partner or when a new partner is admitted and so on. These peculiar situations need specific treatment in accounting that need to be clarified.

The present chapter discusses some basic aspects of partnership such as distribution of profit, maintenance of capital accounts, etc. The treatment of situations like admission of partner, retirement, death and dissolution have been taken up in the subsequent chapters.

2.1 Nature of Partnership

When two or more persons join hands to set up a business and share its profits and losses, they are said to be in partnership. Section 4 of the Indian Partnership Act 1932 defines partnership as the *'relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all'***.**

Persons who have entered into partnership with one another are individually called 'partners' and collectively called 'firm'. The name under which the business is carried is called the 'firm's name'. A partnership firm has no separate legal entity, apart from the partners constituting it. Thus, the essential features of partnership are:

1. *Two or More Persons:* In order to form partnership, there should be at least two persons coming together for a common goal. In other words, the minimum number of partners in a firm can be two. There is however, a limit on their maximum number. By virtue of Section 464 of the Companies Act 2013, the Central Government is empowered to prescribe maximum number of partners in a firm but the number of partners can not be more than 100. The Central government has prescribed the maximum number of partness in a firm to be 50 under Rule 10 of the Companies (Miscellaneous) Rules, 2014, So, a partnership firm cannot have more than 50 partners.
2. *Agreement:* Partnership is the result of an agreement between two or more persons to do business and share its profits and losses. The agreement becomes the basis of relationship between the partners. It is not necessary that such agreement is in written form. An oral agreement is equally valid. But in order to avoid disputes, it is preferred that the partners have a written agreement.
3. *Business:* The agreement should be to carry on some business. Mere co-ownership of a property does not amount to partnership. For example, if Rohit and Sachin jointly purchase a plot of land, they become the joint owners of the property and not the partners. But if they are in the business of purchase and sale of land for the purpose of making profit, they will be called partners.
4. *Mutual Agency:* The business of a partnership concern may be carried on by all the partners or any of them acting for all. This statement has two important implications. First, every partner is entitled to participate in the conduct of the affairs of its business. Second, that there exists a relationship of mutual agency between all the partners. Each partner carrying on the business is the principal as well as the agent for all the other partners. He can bind other partners by his acts and also is bound by the acts of other partners with regard to business of the firm. Relationship of mutual agency is so important that one can say that there would be no partnership, if the element of mutual agency is absent.
5. *Sharing of Profit:* Another important element of partnership is that, the agreement between partners must be to share profits and losses of a business. Though the definition contained in the Partnership Act describes partnership as relation between people who agree to share the profits of a business, the sharing of loss is implied. Thus, sharing of profits and

losses is important. If some persons join hands for the purpose of some charitable activity, it will not be termed as partnership.

6. *Liability of Partnership:* Each partner is liable jointly with all the other partners and also severally to the third party for all the acts of the firm done while he is a partner. Not only that the liability of a partner for acts of the firm is also unlimited. This implies that his private assets can also be used for paying off the firm's debts.

Limited Liability Partnership

Limited Liability Partnership (LLP) is an incorporated partnership formed and registered under the Limited Liability Partnership Act., 2008 with limited liability and peretual succession.

It is viewed as an alternative corporate business vehicle that provides the benefits of limited liability but allows its partners the flexibility of organising their internal structure as a partnership based on a mutually arrived agreement.

Salient Features

The salient features of Limited Liability Partnership are as follows :

1. Limited Liability Partnership is a corporate and a legal entity separate from is partners.
2. Every Limited Liability Partnership shall have at least two partners and shall also have at least two individuals as designated partners, of whom at least one shall be a resident in India.
3. The Indian Partnership Act, 1932, shall not be applicable to Limited Liability Partnership.
4. The Limited Liability Partnership has a perpetual succession.
5. The Central government has the power to investigate into the affairs of a Limited `Liability Partnership, if required, by appointment of a Competent Inspector for the purpose.

2.2 Partnership Deed

Partnership comes into existence as a result of agreement among the partners. The agreement can be either oral or written. The Partnership Act does not require that the agreement must be in writing. But wherever it is in writing, the document, which contains terms of the agreement is called 'Partnership Deed'. It generally contains the details about all the aspects affecting the relationship between the partners including the objective of business, contribution of capital by each partner, ratio in which the profits and the losses will be shared by the partners and entitlement of partners to interest on capital, interest on loan, etc.

The clauses of partnership deed can be altered with the *consent of all the partners*. The deed should be properly drafted and prepared as per the provisions of the 'Stamp Act' and preferably registered with the Registrar of Firms.

Contents of the Partnership Deed

The Partnership Deed usually contains the following details:

- Names and Addresses of the firm and its main business;
- Names and Addresses of all partners;

- Amount of capital to be contributed by each partner;
- The accounting period of the firm;
- The date of commencement of partnership;
- Rules regarding operation of Bank Accounts;
- Profit and loss sharing ratio;
- Rate of interest on capital, loan, drawings, etc;
- Mode of auditor's appointment, if any;
- Salaries, commission, etc, if payable to any partner;
- The rights, duties and liabilities of each partner;
- Treatment of loss arising out of insolvency of one or more partners;
- Settlement of accounts on dissolution of the firm;
- Method of settlement of disputes among the partners;
- Rules to be followed in case of admission, retirement, death of a partner; and
- Any other matter relating to the conduct of business.

Normally, the partnership deed covers all matters affecting relationship of partners amongst themselves. However, if there is no express agreement on certain matters, the provisions of the Indian Partnership Act, 1932 shall apply.

2.2.1 Provisions Relevant for Accounting

The important provisions affecting partnership accounts are as follows:

(a) *Profit Sharing Ratio:* If the partnership deed is silent about the profit sharing ratio, the profits and losses of the firm are to be shared equally by partners, irrespective of their capital contribution in the firm.

(b) *Interest on Capital:* No partner is entitled to claim any interest on the amount of capital contributed by him in the firm as a matter of right. However, interest can be allowed when it is expressly agreed to by the partners. Thus, no interest on capital is payable if the partnership deed is silent on the issue. Further the interest is payable only out of the profits of the business and not if the firm incurs losses during the period.

(c) *Interest on Drawings:* No interest is to be charged on the drawings made by the partners, if there is no mention in the Deed.

(d) *Interest on Advances:* If any partner has advanced some money to the firm beyond the amount of his capital for the purpose of business, he shall be entitled to get an interest on the amount at the rate of 6 per cent per annum.

(e) *Remuneration for Firm's Work:* No partner is entitled to get salary or other remuneration for taking part in the conduct of the business of the firm unless there is a provision for the same in the Partnership Deed.

Apart from the above, the Indian Partnership Act specifies that subject to contract between the partners:

(i) If a partner derives any profit for him/her self from any transaction of the firm or from the use of the property or business connection of the firm or the firm name, he/she shall account for the profit and pay it to the firm.

(ii) If a partner carries on any business of the same nature as and competing with that of the firm, he/she shall account for and pay to the firm, all profit made by him/her in that business.

Test your Understanding – I

1. Mohan and Shyam are partners in a firm. State whether the claim is valid if the partnership agreement is silent in the following matters:
   (i) Mohan is an active partner. He wants a salary of Rs. 10,000 per year;
   (ii) Shyam had advanced a loan to the firm. He claims interest @ 10% per annum;
   (iii) Mohan has contributed Rs. 20,000 and Shyam Rs. 50,000 as capital. Mohan wants equal share in profits.
   (iv) Shyam wants interest on capital to be credited @ 6% per annum.
2. State whether the following statements are true or false:
   (i) Valid partnership can be formulated even without a written agreement between the partners;
   (ii) Each partner carrying on the business is the principal as well as the agent for all the other partners;
   (iii) Maximum number of partners can be 50;
   (iv) Methods of settlement of dispute among the partners can't be part of the partnership deed;
   (v) If the deed is silent, interest at the rate of 6% p.a. would be charged on the drawings made by the partner;
   (vi) Interest on partner's loan is to be given @ 12% p.a. if the deed is silent about the rate.

2.3 Special Aspects of Partnership Accounts

Accounting treatment for partnership firm is similar to that of a sole proprietorship business with the exception of the following aspects:

- Maintenance of Partners' Capital Accounts;
- Distribution of Profit and Loss among the partners;
- Adjustments for Wrong Appropriation of Profits in the Past;
- Reconstitution of the Partnership Firm; and
- Dissolution of Partnership Firm.

The first three aspects mentioned above have been taken up in the following sections of this chapter. The remaining aspects have been covered in the subsequent chapters.

2.4 Maintenance of Capital Accounts of Partners

All transactions relating to partners of the firm are recorded in the books of the firm through their capital accounts. This includes the amount of money brought in as capital, withdrawal of capital, share of profit, interest on capital, interest on drawings, partner's salary, commission to partners, etc.

There are two methods by which the capital accounts of partners can be maintained. These are: (i) fixed capital method, and (ii) fluctuating capital method. The difference between the two lies in whether or not the transactions other than addition/withdrawal of capital are recorded in the capital accounts of the partners.

(a) *Fixed Capital Method:* Under the fixed capital method, the capitals of the partners shall remain fixed unless additional capital is introduced or a part of the capital is withdrawn as per the agreement among the partners.

All items like share of profit or loss, interest on capital, drawings, interest on drawings, etc. are recorded in a separate accounts, called Partner's Current Account. The partners' capital accounts will always show a credit balance, which shall remain the same (fixed) year after year unless there is any addition or withdrawal of capital. The partners' current account on the other hand, may show a debit or a credit balance. Thus under this method, two accounts are maintained for each partner viz., capital account and current account, While the partners' capital accounts shall always appear on the liabilities side in the balance sheet, the partners' current account's balance shall be shown on the liabilities side, if they have credit balance and on the assets side, if they have debit balance.

The partner's capital account and the current account under the fixed capital method would appear as shown below:

Partner's Capital Account

Dr. *Cr.*

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Bank (permanent withdrawal of capital)		xxx		Balance b/d (opening balance)		xxx
	Balance c/d (closing balance)		xxx		Bank (fresh capital introduced)		xxx
			xxx				xxx

Partner's Current Account

Dr. *Cr.*

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d (in case of debit opening bal,)		xxx		Balance b/d (in case of credit opening balance)		xxx
	Drawings		xxx		Salary		xxx
	Interest on drawings		xxx		Commission		xxx
	Profit & Loss a/c		xxx		Interest on capital		
					Profit & Loss Appropriation (share of profit)		xxx
	Balance c/d (in case of credit closing balance)		xxx		Balance c/d (in case of debit closing balance)		xxx
			xxxx				**xxxx**

Fig. 2.1: *Proforma of Partner's Capital and Current Account under Fixed Capital Method.*

(b) *Fluctuating Capital Method:* Under the fluctuating capital method, only one account, i.e. capital account is maintained for each partner. All the adjustments such as share of profit and loss, interest on capital, drawings, interest on drawings, salary or commission to partners, etc are recorded directly in the capital accounts of the partners. This makes the balance in the capital account to fluctuate from time to time. That's the reason why this method is called fluctuating capital method. In the absence of any instruction, the capital account should be prepared by this method. The proforma of capital accounts prepared under the fluctuating capital method is given below:

Partner's Capital Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs.)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs.)*
	Drawings		xxx		Balance b/d		xxx
					Bank (fresh capital introduced)		xxx
	Interest on drawings		xxx				
	Profit and Loss A/c (for share of loss)		xxx		Salaries		xxx
	Balance c/d				Interest on capital		xxx
					Profit and Loss Appropriation (for share of profit)		xxx
			xxxx				**xxxx**

Fig. 2.2: *Proforma of Partner's Capital Account under Fluctuating capital Method.*

2.4.1 Distinction between Fixed and Fluctuating Capital Accounts

The main points of differences between the fixed and fluctuating capital methods can be summed up as follows:

Basis of Distinction	*Fixed Capital Account*	*Fluctuating Capital Account*
(i) Number of accounts	Under this method, two separate accounts are maintained for each partner viz. 'capital account' and ' current account'.	Each partner has one account, i.e. capital account, under this method
(ii) Adjustments	All adjustments for drawings, salary, interest on capital, etc. are made in the current accounts and not in the capital accounts.	All adjustments for drawings, salary interest on capital, etc., are made in the capital accounts,
(iii) Fixed balance	The capital account balance remain unchanged unless there is addition to or withdrawal of capital.	The balance of the capital account fluctuates from year to year
(iv) Credit balance	The capital accounts always show a credit balance.	The capital account may sometimes show a debit balance.

Illustration 1

Sameer and Yasmin are partners with capitals of Rs.15,00,000 and Rs. 10,00,000 respectively. They agree to share profits in the ratio of 3:2. Show how the following transactions will be recorded in the capital accounts of the partners in case: (i) the capitals are fixed, and (ii) the capitals are fluctuating. The books are closed on March 31, every year.

Particulars	Sameer (Rs.)	Yasmin (Rs.)
Additional capital contributed on July 1, 2014	3,00,000	2.00,000
Interest on capital	5 %	5 %
Drawings (during 2014-15)	30,000	20,000
Interest on drawings	1,800	1,200
Salary	20.000	
Commission	10,000	7,000
Share in loss for the year 2014-15	60,000	40,000

Solution

Fixed Capital Method

Partner's Capital Accounts

Dr. Cr.

Date	Details	L.F.	Sameer Amount (Rs.)	Yasmin Amount (Rs.)	Date	Details	L.F.	Sameer Amount (Rs.)	Yasmin Amount (Rs.)
	Balance c/d		18,00,000	12,00,000		Balance b/d		15,00,000	10,00,000
						(Additional capital)		3,00,000	2,00,000
			18,00,000	**12,00,000**				**18,00,000**	**12,00,000**

Partner's Current Accounts

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs.) Sameer	Amount (Rs.) Yasmin	Date	Particulars	J.F.	Amount (Rs.) Sameer	Amount (Rs.) Yasmin
	Drawings		30,000	20,000		Interest on capital		82,500	55,000
	Interest on drawings		1,800	1,200		Partner's salary		20,000	7,000
	Profit and Loss A/c		60,000	40,000		Commission		10,000	
	Balance c/d		20,700	800					
			1,12,500	**62,000**				**1,12,500**	**62,000**

Working Notes:

Calculation of interest on capitals: *Rs.* *Rs.*

X 5% on Rs. 15,00,000 for 1 Year $= 5 \times \frac{15,00,000}{100}$ = 75,000

5% on Rs. 3,00,000 for 6 months $= 5 \times \frac{3,00,000}{100} \times \frac{6}{12}$ = 7,500

82,500

Y 5% on Rs. 10,00,000 for 1 year $= 5 \times \frac{10,00,000}{100}$ = 50,000

5% on Rs. 2,00,000 for 6 month $= 5 \times \frac{2,00,000}{100} \times \frac{6}{12}$ = 5,000

55,000

Fluctuating Capital Method

Dr, **Partner's Capital Accounts** *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs.) Sameer*	*Amount (Rs.) Yasmin*	*Date*	*Particulars*	*J.F.*	*Amount (Rs.) Sameer*	*Amount (Rs.) Yasmin*
	Drawings		30,000	20,000		Balance b/d		15,00,000	10,00,000
	Interest on Drawings		1800	1200		Bank		3,00,000	2,00,000
	Profit and Loss		60,000	40,000		Interest on capital		82,500	55,000
	Balance c/d		18,20,700	12,00,800		Salary		20,000	7000
						Commission		10,000	-
			19,12,500	**12,62,000**				**19,12,500**	**12,62,000**

Do it Yourself

1. Soumya and Bimal are partners in a firm Sharing profits and losses in the ratio of 3:2. The balance in their capital and current accounts as on April 01, 2017 were as under:

	Soumya (Rs.)	*Bimal (Rs.)*
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr.)	1,00,000	80,000

The partnership deed provides that Soumya is to be paid salary @ Rs, 500 per month where as Bimal is to get a commission of Rs. 40,000 for the year. Interest on capital is to be credited at 6% p.a. The drawings of Soumya and Bimal for the year were Rs. 30,000 and Rs. 10,000 respectively. The net profit of the firm before making these adjustment was Rs, 2,49,000. Interest on Soumya's drawings was Rs. 750 and Bimal's drawings, Rs. 250. Prepare Profit and Loss Appropriation Account and Partner's Capital and Current Accounts.

2. Soniya, Charu and Smita started a partnership firm on April 1, 2017. They contributed Rs, 5,00,000, Rs. 4,00,000 and Rs. 3,00,000 respectively as their capitals and decided to share profits and losses in the ratio of 3:2:1.

The partnership provides that Soniya is to be paid a salary of Rs. 10,000 per month and Charu a commission of Rs. 50,000. It also provides that interest on capital be allowed @6% p.a. The drawings for the year were Soniya Rs. 60,000, Charu Rs. 40,000 and Smita Rs. 20,000. Interest on drawings was charged as Rs. 2,700 on Soniya's drawings, Rs. 1,800 on Charu's drawings and Rs. 900 on Smita's drawings. The net amount of profit as per Profit and Loss Account for the year 2015-16 was Rs. 3,56,600.

(i) Record necessary journal entries.
(ii) Prepare profit and loss appropriation account
(iii) Show capital accounts of the partners.

2.5 Distribution of Profit among Partners

The profits and losses of the firm are distributed among the partners in an agreed ratio. However, if the partnership deed is silent, the firm's profits and losses are to be shared equally by all the partners.

You know that in the case of sole partnership the profit or loss, as ascertained by the profit and loss account is transferred to the capital account of the proprietor. In case of partnership, however, certain adjustments such as interest on drawings, interest on capital, salary to partners, and commission to partners are required to be made. For this purpose, it is customary to prepare a Profit and Loss Appropriation Account of the firm and ascertain the final figure of profit and loss to be distributed among the partners, in their profit sharing ratio.

2.5.1 Profit and Loss Appropriation Account

Profit and Loss Appropriation Account is merely an extension of the Profit and Loss Account of the firm. It shows how the profits are appropriated or distributed among the partners. All adjustments in respect of partner's salary, partner's commission, interest on capital, interest on drawings, etc. are made through this account. It starts with the net profit/net loss as per Profit and Loss Account is transfered to this account. The journal entries for preparation of Profit and Loss Appropriation Account and making various adjustments through it are given as follows:

Journal Entries

1. Transfer of the balance of Profit and Loss Account to Profit and Loss Appropriation Account:
   (a) If Profit and Loss Account shows a credit balance (net profit):
   Profit and Loss A/c Dr.
   To Profit and Loss Appropriation A/c
   (b) If Profit and Loss Account shows a debit balance (net loss)
   Profit and Loss Appropriation A/c Dr.
   To Profit and Loss A/c
2. Interest on Capital:
   (a) For crediting interest on capital to partners' capital account:
   Interest on Capital A/c Dr.
   To Partner's Capital/Current A/cs (individually)

(b) For transferring interest on capital to Profit and Loss Appropriation Account:
Profit and Loss Appropriation A/c Dr.
To Interest on Capital A/c

3. Interest on Drawings:

(a) For charging interest on drawings to partners' capital accounts:
Partners Capital/Current A/c's (individually) Dr.
To Interest on Drawings A/c

(b) For transferring interest on drawings to Profit and Loss Appropriation Account:
Interest on Drawings A/c Dr.
To Profit and Loss Appropriation A/c

4. Partner's Salary:

(a) For crediting partner's salary to partner's capital account:
Salary to Partner A/c Dr.
To Partner's Capital/Current A/c's (individually)

(b) For transferring partner's salary to Profit and Loss Appropriation Account:
Profit and Loss Appropriation A/c Dr.
To Salary to Partner's A/c

5. Partner's Commission:

(a) For crediting commission to a partner, to partner's capital account:
Commission to Partner A/c Dr.
To Partner's Capital/Current A/c's (individually)

(b) For transferring commission paid to partners to Profit and Loss Appropriation Account.
Profit and Loss Appropriation A/c Dr.
To Commission to Partners Capital/Current A/c

6. Share of Profit or Loss after appropriations:
If Profit:
Profit and Loss Appropriation A/c Dr.
To Partner's Capital/Current A/c's (individually)

The Proforma of Profit and Loss Appropriation Account is given as follows:

Profit and Loss Appropriation Account

Dr. *Cr.*

Particulars	*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
Profit and Loss (if there is loss)	xxx	Profit and Loss (if there is profit)	xxx
Interest on Capital	xxx	Interest on Drawings	xxx
Salary to Partner	xxx		xxx
Commission to Partner	xxx		
Interest on Partner's Loan	xxx		
Partners' Capital Accounts (distribution of profit)	xxx		
	xxxx		**xxxx**

Fig. 2.3: *Proforma of Profit and Loss Appropriation Account*

Illustration 2

Amit, Babu and Charu set up a partnership firm on April 1, 2015. They contributed Rs. 50,000, Rs. 40,000 and Rs. 30,000, respectively as their capitals and agreed to share profits and losses in the ratio of 3 : 2 :1. Amit is to be paid a salary of Rs. 1,000 per month and Babu, a Commission of Rs. 5,000. It is also provided that interest to be allowed on capital at 6% p.a. The drawings for the year were Amit Rs. 6,000, Babu Rs. 4,000 and Charu Rs. 2,000. Interest on drawings of Rs. 270 was charged on Amit's drawings, Rs. 180 on Babu's drawings and Rs. 90, on Charu's drawings. The net profit as per Profit and Loss Account for the year ending March 31, 2015 was Rs. 35,660. Prepare the Profit and Loss Appropriation Account to show the distribution of profit among the partners.

Solution

Profit and Loss Appropriation Account

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*		*Amount (Rs.)*
Amits' salary		12,000	Net profit		35,660
Babus' commission		5,000	Interest on drawings:		
Interest on Capitals :			Amit	270	
Amit	3,000		Babu	180	
Babu	2,400		Charu	90	540
Charu	1,800	7,200			
Share of profit transferred to Capital accounts :					
Amit	6,000				
Babu	4,000				
Charu	2,000	12,000			
		36,200			**36,200**

Illustration 3

Amitabh and Babul are partners sharing profits in the ratio of 3:2, with capitals of Rs. 50,000 and Rs. 30,000 respectively. Interest on capital is agreed @ 6% p.a. Babul is to be allowed an annual salary of Rs. 2,500. During the year 2016-17, the profits prior to the calculation of interest on capital but after charging Babul's salary amounted to Rs. 12,500. A provision of 5% of the profit is to be made in respect of commission to the Manager.

Prepare Profit and Loss Appropriation account showing the distribution of profit and the partners' capital accounts for the year ending March 31, 2017.

Solution

Profit and Loss Appropriation Account

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
Babul's salary		2,500	Net profit	15,000
Interest on capital:			(before Babul's salary)	
Amitabh		3,000		
Babul		1,800		
Manager's commission		750		
(5% of Rs. 15,000)				
Profit transferred to partner's capital account;				
Amitabh	4,170			
Babul	2,780	6,950		
		15,000		**15,000**

Amitabh's Capital Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs.)*	*Date 2016*	*Particulars*	*J.F.*	*Amount (Rs.)*
2017				2016			
Mar.31	Balance c/d		57,170	Apr.01	Balance b/d		50,000
				2017			
				Mar.31	Interest on capital		3,000
				Mar.31	Profit & Loss Appropriation a/c (share of profit)		4,170
			57,170				**57,170**

Babul's Capital Account

Dr. *Cr.*

Date 2017	*Particulars*	*J.F.*	*Amount (Rs.)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs.)*
2017				2016			
Mar.31	Balance c/d		37,080	Apr.01	Balance b/d		30,000
				2017	Salary		2,500
				Mar.31	Interest on capital		1,800
				Mar.31	Profit & Loss Appropriation (share of profit)		2,780
			37,080				**37,080**

Test your Unerstanding – II

1. Raju and Jai commenced business in partnership on April 1, 2017. *No partnership agreement was made whether oral or written.* They contributed Rs. 4,00,000 and Rs. 1,00,000 respectively as capitals. In addtion, Raju advanced Rs. 2,00,000 as loan to the firm on October 1, 2017. Raju met with an accident on July 1, 2017 and could not attend the business up to september 30, 2017. The profit for the year ended March 31, 2018 amounted to Rs, 50,600. Disputes have arisen between them on sharing the profits of the firm.

Raju Claims:

(i) He should be given interest at 10% p.a. on capital and so also on loan.
(ii) Profit should he distributed in the proportion of capitals.

Jai Claims:

(i) Net profit should be shared equally.
(ii) He should be allowed remuneration of Rs, 1,000 p.a. during the period of Raju's illness.
(iii) Interest on capital and loan should be given @ 6% p.a.
State the correct position on each issue as per the provisions of the Partnership Act. 1932.

2. Reena and Raman are partners with capitals of Rs. 3,00,000 and Rs. 1,00,000 respectively. The profit (as per Profit and Loss Account) for the year ended March 31, 2017 was Rs. 1,20,000. Interest on capital is to be allowed at 6% p.a. Raman was entitled to a salary of Rs. 30,000 p.a. The drawings of partners were Rs. 30,000 and 20,000. The interest on drawings to be charged to Reena was Rs. 1,000 and to Raman, Rs. 500.

   Assuming that Reena and Raman are equal partners. State their share of profit after necessary appropriations.

2.5.2 Calculation of Interest on Capital

No interest is allowed on partners' capitals unless it is expressly agreed among the partners. When the Deed specifically provides for it, interest on capital is credited to the partners at the agreed rate with reference to the time period for which the capital remained in business during a financial year. Interest on capital is generally provided for in two situations: (i) when the partners contribute unequal amounts of capitals but share profits equally, and (ii) where the capital contribution is same but profit sharing is unequal.

Interest on capital is calculated with due allowance for any addition or withdrawal of capital during the accounting period. For example, Mohini, Rashmi and Navin entered into partnership, bringing in Rs. 3,00,000, Rs. 2,00,000 and Rs. 1,00,000 respectively into the business. They decided to share profits and losses equally and agreed that interest on capital will be provided to the partners

@10 per cent per annum. There was no addition or withdrawal of capital by any partner during the year. The interest on capital works out to Rs. 30,000 (10% on 30,000) for Mohini, Rs. 20,000 (10% on 2,00,000) for Rashmi, and Rs. 10,000 (10% on 1,00,000) for Navin.

Take another case of Mansoor and Reshma who are partners in a firm and their capital accounts showed the balance of Rs. 2,00,000 and Rs. 1,50,000 respectively on April 1, 2016. Mansoor introduced additional capital of Rs. 1,00,000 on August 1, 2016 and Reshma brought in further capital of Rs. 1,50,000 on October 1, 2016. Interest is to be allowed @ 6% p.a. on the capitals. It shall be worked as follows:

For Mansoor $\left(\text{Rs. } 2{,}00{,}000 \times \frac{6}{100}\right) + \left(\text{Rs. } 1{,}00{,}000 \times \frac{6}{100} \times \frac{8}{12}\right)$

= Rs. 12,000 + Rs. 4,000 = Rs. 16,000

For Reshma $\left(\text{Rs. } 1{,}50{,}000 \times \frac{6}{100}\right) + \left(\text{Rs. } 1{,}50{,}000 \times \frac{6}{100} \times \frac{6}{12}\right)$

= Rs. 9,000+Rs. 4,500= Rs. 13,500

When there are both addition and withdrawal of capital by of partners during a financial year, the interest on capital is calculated as follows:

(i) On the opening balance of the capital accounts of partners, interest is calculated for the whole year;

(ii) On the additional capital brought in by any partner during the year, interest is calculated from the date of introduction of additional capital to the last day of the financial year.

(iii) On the amount of capital withdrawn (other than usual drawings) during the year interest for the period from the date of withdrawal to the last day of the financial year is calculated and deducted from the total of the interest calculated under points: (i) and (ii) above.
Alternatively, it can be calculated with respect to the amounts remained invested for the relevant periods.

Illustration 4

Saloni and Srishti are partners in a firm. Their capital accounts as on April 01. 2016 showed a balance of Rs. 2,00,000 and Rs. 3,00,000 respectively. On July 01, 2016, Saloni introduced additional capital of Rs. 50,000 and Srishti, Rs. 60,000. On October 01 Saloni withdrew Rs. 30,000, and on January 01, 2016 Srishti withdraw, Rs. 15,000 from their capitals. Interest is allowed @ 8% p.a. Calculate interest payable on capital to both the partners during the financial year 2016–2017.

Solution

Statement Showing Calculation of Interest on Capital

For Saloni

			(Rs.)
Interest on Rs. 2,00,000 for full year	= $\frac{\text{Rs. } 2,00,000 \times 8 \times 1}{100}$	=	16,000
Add: Interest on Rs. 50,000 for 9 months	= $\frac{\text{Rs.} 50,000 \times 9 \times 8}{12 \times 100}$	=	3,000
			19,000
Less: Interest on 30,000 for 6 months	= $\frac{\text{Rs.} 30,000 \times 8 \times 6}{12 \times 100}$	=	1,200
			17,800

Alternatively interest can be calculated on Rs. 2 lakh for 3 months, on Rs. 2,50,000 for 3 months, and on Rs. 2,20,000, for 6 months (Rs. 4,000 + Rs. 5,000 + Rs. 8,800 = Rs. 17,800).

For Srishti

			(Rs.)
Interest on Rs. 3,00,000, for full year @8%	= $\frac{\text{Rs.} 3,00,000 \times 8 \times 1}{100}$	=	24,000
Add: Interest on Rs. 60,000, for 9 months	= $\frac{\text{Rs.} 60,000 \times 8 \times 9}{100 \times 12}$	=	3,600
			27,600
Less: Interest on Rs. 15,000 for 3 months	= $\frac{\text{Rs.} 15,000 \times 8 \times 3}{100 \times 12}$	=	300
(Money withdrawn)			*27,300*

Alternatively interest can be charged on Rs. 3,00,000 for 3 months on Rs. 3,60,000 for 6 months and on Rs. 3,45,000 for 3 months (Rs. 6,000 + Rs. 14,400 + Rs. 6,900 = Rs. 27,300).

Illustration 5

Josh and Krish are partners sharing profits and losses in the ratio of 3:1. Their capitals at the end of the financial year 2015-2016 were Rs. 1,50,000 and Rs. 75,000. During the year 2015-2016, Josh's drawings were Rs. 20,000 and the drawings of Krish were Rs. 5,000, which had been duly debited to partner's capital accounts. Profit before charging interest on capital for the year was Rs. 16,000. The same had also been debited in their profit sharing ratio. Krish had brought additional capital of Rs. 16,000 on October 1, 2015. Calculate interest on capital @ 12% p.a. for the year 2015-2016.

Solution

Statement Showing Calculation of Capital at the Beginning

Particulars	*Josh* *Rs.*	*Krish* *Rs.*
Capital at the end	1,50,000	75,000
Add: Drawings during the year	20,000	5,000
	1,70,000	**80,000**
Less: Share of profit (credited)	12,000	4,000
	1,58,000	**76,000**
Less: Additional capital	—-	16,000
Capital in the beginning	1,58,000	60,000

Interest on capital will be as 18,960 (12% of Rs. 1,58,000) for Josh and Rs. 960 for krish calculated as follows:

$$\left(\text{Rs. } 60{,}000 \times \frac{12}{100}\right) + \left(\text{Rs. } 16{,}000 \times \frac{12}{100} \times \frac{6}{12}\right) = \text{Rs. } 7{,}200 + \text{Rs. } 960$$

$$= \text{Rs. } 8{,}160.$$

Sometimes opening capitals of partners may not be given. In such a situation before calculation of interest on capital the opening capitals will have to be worked out with the help of partners' closing capitals by marking necessary adjustments for the additions and withdrawal of capital, drawings, share of profit or loss, if already shown in the capital accounts the partners.

As clarified earlier, the interest on capital is allowed only when the firm has earned profit during the accounting year. Hence, no interest will be allowed during the year the firm has incurred net loss and if in a year, the profit of the firm is less than the amount due to the partners as interest on capital, the payment of interest will be restricted to the amount of profits. In that case, the profit will be effectively distributed in the ratio of interest on capital of each partner.

Illustration 6

Anupam and Abhishek are partners sharing profits and losses in the ratio of 3 : 2. Their capital accounts showed balances of Rs. 1,50,000 and Rs. 2,00,000 respectively on Jan 01, 2017. Show the treatment of interest on capital for the year ending December 31, 2017 in each of the following alternatives:

(a) If the partnership deed is silent as to the payment of interest on capital and the profit for the year is Rs. 50,000;

(b) If partnership deed provides for interest on capital @ 8% p.a. and the firm incurred a loss of Rs. 10,000 during the year;

(c) If partnership deed provides for interest on capital @ 8% p.a. and the firm earned a profit of Rs. 50,000 during the year;

(d) If the partnership deed provides for interest on capital @ 8% p.a. and the firm earned a profit of Rs. 14,000 during the year.

Solution

(a) In the absence of a specific provision in the Deed, no interest will be paid on the capital to the partners. The whole amount of profit will however be distributed among the partners in their profit sharing ratio.

(b) As the firm has incurred losses during the accounting year, no interest on capital will be allowed to any partner. The firm's loss will however be shared by the partners in their profit sharing ratio.

			Rs.
(c)	Interest to Anupam @ 8% on Rs. 1,50,000	=	12,000
	Interest to Abhishek @ 8% on Rs. 2,00,000	=	16,000
			28,000

As the profit is sufficient to pay interest at agreed rate, the whole amount of interest on capital shall be allowed and the remaining profit amounting to Rs. 22,000 (Rs. 50,000 – Rs. 28,000) shall be shared by the partners in their profit sharing ratio.

(d) As the profit for the year is Rs. 14,000, which is less than the amount of interest on capital due to partners, i.e. Rs. 28,000 (Rs. 12,000 for Anupam and Rs. 16,000 for Abhishek), interest will be paid to the extent of available profit i.e., Rs. 14,000. Anupam and Abhishek will be credited with Rs. 6,000 and Rs. 8,000, respectively. Effectively this amounts to sharing the firm's profit in the ratio of interest on capital.

Test your Understanding – III

1. Rani and Suman are in partnership with capitals of Rs, 80,000 and Rs. 60,000, respectively. During the year 2015-16, Rani withdrew Rs. 10,000 from her capital and Suman Rs. 15,000. Profits before charging interest on capital was Rs. 50,000. Ravi and Suman shared profits in the ratio of 3:2. Calculate the amounts of interest on their capitals @ 12% p.a. for the year ended March 31, 2016.
2. Priya and Kajal are partners in a firm, sharing profits and losses in the ratio of 5:3. The balance in their fixed capital accounts, on April 1, 2016 were: Priya, Rs. 6,00,000 and Kajal, Rs. 8,00,000. The profit of the firm for the year ended 2017 is Rs, 1,26,000. Calculate their shares of profits: (a) when there is no agreement in respect of interest on capital, and (b) when there is an agreement that the interest on capital will be allowed @ 12% p.a.

2.5.3 Interest on Drawings

The partnership agreement may also provide for charging of interest on money withdrawn out of the firm by the partners for their personal use. As stated earlier, no interest is charged on the drawings if there is no express agreement among the partners about it. However if the partnership deed so provides for it, the interest is charged at an agreed rate, for the period money remained outstanding from the partners during an accounting year. Charging interest on drawings discourages excessive amounts of drawings by the partners.

The calculation of interest on drawings under different situations is shown as here under.

When Fixed Amounts is Withdrawn Every Month

Many a time, a fixed amount of money is withdrawn by the partners, at equal time interval, say each month or each quarter. While calculating the time period, attention must be paid to whether the fixed amount was withdrawn at the beginning (first day) of the month, middle of the month or at the end (last day) of the month. If withdrawn on the first day of every month, interest on total amount will be calculated for 6½ months; if withdrawn at the end at every month, it will be calculated for 5½ months, and if withdrawn during the middle of the month, it will be calculated for 6 months.

Suppose, Aashish withdrew Rs. 10,000 per month from the firm for his personal use during the year ending March 31, 2017. The calculation of average period and the interest on drawings, in different situations would be as follows:

(a) When the amount is withdrawn at the beginning of each month:

$$\text{Average Period} = \frac{\text{Total Period in Months} + 1}{2} = \frac{12+1}{2} = 6\frac{1}{2} \text{ months.}$$

$$\text{Interest on Drawings} = \frac{\text{Rs.}1,20,000 \times 8 \times 13 \times 1}{100 \times 2 \times 12} = \text{Rs. } 5,200.$$

(b) When the amount is withdrawn at the end of each month

$$\text{Average Period} = \frac{\text{Total period in Months} - 1}{2} = \frac{12-1}{2} = 5\frac{1}{2} \text{ months}$$

$$\text{Interest on Drawings} = \frac{\text{Rs.}1,20,000 \times 8 \times 11 \times 1}{100 \times 2 \times 12} = \text{Rs. } 4,400.$$

(c) When money is withdrawn in the middle of the month

When money is withdrawn in the middle of the month, nothing is added or deduced from the total period.

$$\text{Average Period} = \frac{\text{Total period in Months}}{2} = \frac{12}{2} = 6 \text{ months}$$

$$\text{Interest on Drawings} = \frac{\text{Rs.}1,20,000 \times 8 \times 6 \times 1}{100 \times 12} = \text{Rs. } 4,800.$$

When Fixed Amount is withdrawn Quarterly

When fixed amount of money is withdrawn quarterly by partners, in such a situation, for the purpose of calculation of interest, the total period of time is ascertained depending on whether the money was withdrawn at the beginning or at the end of each quarter. If the amount is withdrawn at the beginning of each quarter, the interest is calculated on the total money withdrawn during the year, for a period of seven and half months and if withdrawn at the and of each quarter it will be calculated for a period of 4½ months.

Suppose Satish and Tilak are partners in a firm, sharing profits and losses equally. During financial year 2016–2017, Satish withdrew Rs. 30,000 quarterly. If interest is to be charged on drawings @ 8% per annum, the calculation of average period and interest on drawings will be as follows:

(a) *If the amount is withdrawn at the beginning of each quarter*

Statement Showing Calculation of Interest on Drawings

Date	*Amount (Rs.)*	*Time Period*	*Interest (Rs.)*
April 1, 2016	30,000	12 months	$30,000 \times \frac{8}{100} \times 1$ = 2,400

July 1, 2016	30,000	9 months	$30{,}000 \times \frac{9}{12} \times \frac{8}{100}$ = 1,800
Oct. 1, 2016	30,000	6 months	$30{,}000 \times \frac{6}{12} \times \frac{8}{100}$ = 1,200
Jan. 1, 2017	30,000	3 months	$30{,}000 \times \frac{3}{12} \times \frac{8}{100}$ = 600
Total	**1,20,000**		**= Rs. 6,000**

Alternatively, the interest can be calculated on the total amount withdrawn during the accounting year, i.e. Rs. 1,20,000 for a period of 7½ months (12+9+6+3)/4. as follows:

$$\text{Rs. } 1{,}20{,}000 \times \frac{8}{100} \times \frac{15}{2} \times \frac{1}{12} = \text{Rs. } 6{,}000.$$

(b) If the amount is withdrawn at the end of each quarter

Statement Showing Calculation of Interest on Drawings

Date	*Amount (Rs.)*	*Time Period*	*Interest (Rs.)*
June 30, 2016	30,000	9 months	$30{,}000 \times \frac{9 \times 8}{12 \times 100}$ = 1,800
September 30, 2016	30,000	6 months	$30{,}000 \times \frac{6}{12} \times \frac{8}{100}$ = 1200
December 31, 2016	30,000	3 months	$30{,}000 \times \frac{3}{12} \times \frac{8}{100}$ = 6,000
March 31, 2017	30,000	0 months	
Total	**1,20,000**		**= 3,600**

Alternatively, the interest can be calculated on the total amount withdrawn during the accounting year, i.e., Rs. 1,20,000 for a period of 4½ months (9 + 6 + 3 + 0)/4 months as follows:

$$= \text{Rs. } 1{,}20{,}000 \times \frac{8}{100} \times \frac{9}{2} \times \frac{1}{12} = \text{Rs. } 3{,}600$$

When Varying Amounts are Withdrawn at Different Intervals

When the partners withdraw different amounts of money at different time intervals, the interest is calculated using the product method. Under the product method, for each withdrawal, the money withdrawn is multiplied by the period (usually expressed in months) for which it remained withdrawn during the financial year. The period is calculated from the date of the withdrawal to the last day of the accounting year. The products so calculated are totalled and interest for 1 month at the specified rate is worked out, on the total of the products. The calculation of interest can be explained with the help of an example.

Shahnaz withdrew the following amounts from her firm, for personal use during the year ending March 31, 2017. Calculate interest on drawings by product method, if the rate of interest to be charged is 7 per cent per annum.

Date	*Amount (Rs.)*
April 1, 2016	16,000
June 30, 2016	15,000
October 31, 2016	10,000
December 31, 2016	14,000
March 1, 2017	11,000

Calculation of interest on drawings will be as follows:

Statement Showing Calculation of Interest on Drawings

Date	*Amount (Rs.)*	*Time Period*	*Product (Rs.)*
April 1, 2016	16,000	12 months	1,92,000
June 30, 2016	15,000	9 months	1,35,000
Oct. 31, 2016	10,000	5 months	50,000
Dec. 31, 2016	14,000	3 months	42,000
Mar. 1, 2017	11,000	1 month	11,000
Total			**4,30,000**

Interest = Sum of Products × Rate × $\frac{1}{12}$

$$= \text{Rs. } 4{,}30{,}000 \times \frac{7}{100} \times \frac{1}{12} = \frac{30100}{12} = \text{Rs. } 2{,}508 \text{ (approx.)}.$$

Illustration 7

John Ibrahm, a partner in Modern Tours and Travels withdrew money during the year ending March 31, 2017 from his capital account, for his personal use. Calculate interest in drawings in each of the following alternative situations, if rate of interest is 9 per cent per annum.

(a) If he withdrew Rs. 3,000 per month at the beginning of the month.
(b) If an amount of Rs. 3,000 per month was withdrawn by him at the end of each month.
(c) If the amounts withdrawn were : Rs. 12,000 on June 01, 2016, Rs. 8,000; on August 31, 2016, Rs. 3,000; on September 30, 2016, Rs. 7,000, on November 30, 2016, and Rs. 6,000 on January 31, 2017.

Solution

(a) As a fixed amount of Rs. 3,000 per month is withdrawn at the beginning of the month, interest on drawings will be calculated for an average period of $6\frac{1}{2}$ months.

Interest on drawings = Rs. $\frac{36,000 \times 9 \times 13 \times 1}{100 \times 2 \times 12}$ = Rs. 1,755

(b) As the fixed amount of Rs. 3,000 per month is withdrawn at the end of each month, interest on drawings will be calculated for an average period of $5\frac{1}{2}$ months.

= $\frac{\text{Rs.}36,000 \times 9 \times 11 \times 1}{100 \times 2 \times 12}$ = Rs. 1,485

(C) Statements showing Calculation of Interest on Drawings

1 *Date*	2 *Amount withdrawn (Rs.)*	3 *Period (in months)*	4 *(Interest)* *(Rs.)*
Jun. 1, 2016	12,000	10	$12,000 \times \frac{9}{100} \times \frac{10}{12} = 900$
Aug. 31, 2016	8,000	7	$8,000 \times \frac{9}{100} \times \frac{7}{12} = 420$
Sept. 30, 2016	3,000	6	$3,000 \times \frac{9}{100} \times \frac{6}{12} = 135$
Nov. 30, 2016	7,000	4	$7,000 \times \frac{9}{100} \times \frac{4}{12} = 210$
Jan. 31, 2017	6,000	2	$6,000 \times \frac{9}{100} \times \frac{2}{12} = 90$
Total Interest			**1,755**

Illustration 8

Manu, Harry and Ali are partners in a firm sharing profits and losses equally. Harry and Ali withdrew the following amounts from the firm, for their personal use, during 2015.

Date	*Harry (Rs.)*	*Ali (Rs.)*
2015		
January, 01	5,000	7,000
April, 01	8,000	4,000
September, 01	5,000	5,000
December, 01	4,000	9,000

Calculate interest on drawings if the rate of interest to be charged is 10 per cent, and the books are closed on December 31 every year.

Statement Showing Calculation of Interest on Drawings

Harry			*Ali*		
Amount (Rs.)	*Period (in months)*	*Product (Rs.)*	*Amount (Rs.)*	*Period (in months)*	*Product (Rs.)*
5000	12	60,000	7,000	12	84,000
8000	9	72,000	4,000	9	36,000
5000	4	20,000	5,000	4	20,000
4000	1	4,000	10,000	1	10,000
		1,56,000			**1,50,000**

Amount of Interest

Mannu $= \text{Rs. } \dfrac{1,56,000 \times 10 \times 1}{100 \times 12} = \text{Rs. } 1,300$

Ali $= \text{Rs. } \dfrac{1,50,000 \times 10 \times 1}{100 \times 12} = \text{Rs. } 1,250$

Do it Yourself

1. Govind is a partner in a firm. He withdrew the following amounts during the year 2015-16:

	(Rs.)
April 30, 2015	6,000
June 30, 2015	4,000
Sept. 30, 2015	8,000
Dec. 31, 2015	3,000
Jan. 31, 2016	5,000

The interest on drawings is to be charged @ 6% p.a. The books are closed on March 31, every year. calculate interest on drawing :

2. Ram and Syam are partners sharing profits/losses equally. Ram withdrew Rs. 1,000 p.m. regularly on the first day of every month during the year 2015-16 for personal expenses. If interest on drawings is charged @ 5% p.a. Calculate interest on the drawings of Ram.
3. Verma and Kaul are partners in a firm. The partnership agreement provides that interest on drawings should be charged @ 6% p.a. Verma withdraws Rs. 2,000 per month starting from April 01, 2015 to March 31, 2014. Kaul withdrew Rs, 3,000 per quarter, starting from April 01, 2015. Calculate interest on partner's drawings.

When Dates of Withdrawal are not specified

When the total amount withdrawn is given but the dates of withdrawals are not specified, it is assumed that the amount was withdrawn evenly throughout the year. *For example;* Shakila withdrew Rs. 60,000 from partnership firm during the year ending March 31, 2015 and the interest on drawings is to be charged at the rate of 8 per cent per annum. For calculation of interest, the period would be taken as six months, which is the average period assuming, that amount is withdrawn evenly in the middle of the month, throughout the year. The amount of interest on drawings works out to be Rs. 2,400 as follows:

$$\left(\text{Rs.}60{,}000 \times \frac{8}{100} \times \frac{6}{12}\right) = \text{Rs. } 2{,}400$$

2.6 Guarantee of Profit to a Partner

Sometimes a partner is admitted into the firm with a guarantee of certain minimum amount by way of his share of profits of the firm. Such assurance may be given by all the old partners in a certain ratio or by any of the old partners, individually to the new partner. The minimum guaranteed amount shall be paid to such new partner when his share of profit as per the profit sharing ratio is less than the guarnteed amount. For example, Madhulika and Rakshita, who are partners in a firm decide to admit Kanishka into their firm, giving her the guarantee of a minimum of Rs.25,000 as her share in firm's profits. The firm earned a profit of Rs.1,20,000 during the year and the agreed profit sharing ratio between the partners is decided as 2:3:1. As per this ratio, Madhulika's share in profit comes to Rs.40,000 (2/6 of Rs. 1,20,000); Rakshita, Rs. 60,000 (3/6 of Rs. 1,20,000) and Kanishka Rs. 20,000 (1/6 of Rs. 1,20,000). The share of Kanishka works out to be Rs.5,000 short of the guaranteed amount. This shall be borne by the guaranteeing partners Madhulika and Rakshita in their profit sharing ratio, which in this case is 2:3, Madhulika's share in the deficiency comes to Rs.2,000 (2/5 of Rs. 5,000), and that of Rakshita Rs.3,000. The total profit of the firm will be distributed among the partners as follows Madhulika will get Rs.38,000 (her share 40,000 minus share in deficiency Rs.2,000); Rakshita Rs.57,000 (60,000–3,000) and Kanishka Rs. 25,000 (Rs. 20,000 + Rs. 2,000 + Rs. 3,000).

If only one partner gives the guarantee, say in the above case, only Rakshita gives the guarantee, the whole amount of deficiency (Rs.5,000) will be borne by her only. In that case profit distribution will be Madhulika Rs.40,000, Rakshita Rs. 55,000 (60,000–5,000) and Kanishka Rs. 25,000 (Rs. 20,000 + Rs. 5,000).

Illustration 9

Mohit and Rohan share profits and losses in the ratio of 2:1. They admit Rahul as partner with 1/4 share in profits with a guarantee that his share of profit shall be at least Rs. 50,000. The net profit of the firm for the year ending March 31, 2015 was Rs. 1,60,000. Prepare Profit and Loss Appropriation Account.

Solution

Profit and Loss Appropriation Account

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
Mohit's capital			Net profit	1,60,000
(share of profit)	80,000			
Less: Share in deficiency	6,667	73,333		
Rohan's capital				
(share of profit)	40,000			
Less: Share in deficiency	3,333	36,667		
Rahul's capital				
(share of profit)	40,000			
Add: Deficiency received from:				
Mohit	6,667			
Rohan	3,333	50,000		
		1,60,000		**1,60,000**

Working Notes:

The new profit sharing ratio after admission of Rahul comes to 2:1:1. As per this ratio the share of partners in the profit comes to:

Mohit $= \text{Rs. } 1{,}60{,}000 \times \frac{2}{4}$ = Rs. 80,000

Rohan $= \text{Rs. } 1{,}60{,}000 \times \frac{1}{4}$ = Rs. 40,000

Rahul $= \text{Rs. } 1{,}60{,}000 \times \frac{1}{4}$ = Rs. 40,000

But, since Rahul has been given a guarantee of minimum of Rs. 50,000 as his share of profit. The deficiency of Rs. 10,000 (Rs. 50,000 – Rs. 40,000) shall be borne by Mohit and Rohan in the ratio in which they share profits and losses between themselves, viz. 2:1 as follows:

Mohit's share in deficiency comes to 2/3 × Rs. 10,000 = Rs. 6,667
Rohan's share in deficiency comes to 1/3 × Rs. 10,000 = Rs. 3,333

Thus Mohit will get Rs. 80,000 – Rs. 6,667 = Rs. 73,333, Rohan will get Rs. 40,000–Rs. 3,333 = Rs. 36,667 and Rahul will get Rs. 40,000 + Rs. 6,667 + Rs. 3,333 = Rs. 50,000 in the profit of the firm.

Calculation of new profit sharing ratio

The new partner Rahul's share is $\frac{1}{4}$ The remaining profit is $1 - \frac{1}{4} = \frac{3}{4}$, to be shared between Mohit and Rohan in the ratio of 2:1.

Mohit's new share = $\frac{3}{4} \times \frac{2}{3} = \frac{2}{4}$

Rohan's new share = $\frac{3}{4} \times \frac{1}{3} = \frac{1}{4}$

Thus, New profit sharing ratio comes to be $\frac{2}{4} : \frac{1}{4} : \frac{1}{4}$ or 2 : 1 :1.

Illustration 10

John and Mathew share profits and losses in the ratio of 3:2. They admit Mohanty into their firm to 1/6 share in profits. John personally guaranteed that Mohanty's share of profit, after charging interest on capital @ 10 per cent per annum would not be less than Rs. 30,000 in any year. The capital provided was as follows: John Rs. 2,50,000, Mathew Rs. 2,00,000 and Mohanty Rs. 1,50,000. The profit for the year ending March 31,2015 amounted to Rs. 1,50,000 before providing interest on capital. Show the Profit & Loss Appropriation Account if new profit sharing ratio is 3:2:1.

Solution

Profit and Loss Appropriation Account

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
Interest on capital			Net profit	1,50,000
John	25,000			
Mathew	20,000			
Mohanty	15,000	60,000		
Capital accounts shared info :				
John	45,000			
Less: Share of deficiency	15,000	30,000		
Mathew		30,000		
Mohanty	15,000			
Add: Deficiency received from John	15,000	30,000		
		1,50,000		**1,50,000**

Working Notes:

Profit after interest on capital is Rs. 90,000, which is to be distributed in the ratio of 3:2:1 as follows: John gets Rs. 45,000 (3/6 × Rs. 90,000), Mathew Rs. 30,000, Mohanty Rs. 15,000. Deficiency of Mohanty from the guaranteed profit of Rs. 15,000 will be borne by John. John will therefore get Rs. 45,000 – Rs. 15,000 = Rs. 30,000, Mathew Rs. 30,000 and Mohanty Rs. 30,000.

Illustration 11

Mahesh and Dinesh share profits and losses in the ratio of 2:1. From January 01, 2014 they admit Rakesh into their firm who is to be given a share of 1/10 of the profits with a guaranteed minimum of Rs. 25,000. Mahesh and Dinesh continue to share profits as before but agree to bear any deficiency on account of guarantee to Rakesh in the ratio of 3:2 respectively. The profits of the firm for the year ending December 31, 2015 amounted to Rs. 1,20,000. Prepare Profit and Loss Appropriation Account.

Profit and Loss Appropriation Account

Dr. Particulars		Amount (Rs.)	Particulars	Cr. Amount (Rs.)
Capital Accounts: (for share of profit)			Net profit	1,20,000
Mahesh 6/10 × 1,20,000	72,000			
Less: Deficiency share	7,800	64,200		
Dinesh 3/10 × 1,20,000	36,000			
Less: Deficiency share	5,200	30,800		
Rakesh	12,000			
Add: Share of Deficiency from				
Mahesh	7,800			
Dinesh	5,200	25,000		
		1,20,000		**1,20,000**

Working Notes:

New profit sharing Ratio will be calculated as follows:

Rakesh to share $\frac{1}{10}$ of the profits. The remaining profit $\frac{9}{10}$ will be shared by Mahesh and Dinesh in the ratio of 2:1.

Mahesh's share in profit will be $\frac{2}{3} \times \frac{9}{10} = \frac{3}{10}$

Dinesh's share will be $\frac{1}{3} \times \frac{9}{10} = \frac{3}{10}$

The New ratio becomes $\frac{3}{5} : \frac{3}{10} : \frac{1}{10}$ or 6 : 3 : 1.

Mahesh's share in profit = 1,20,000 × $\frac{6}{10}$ = Rs. 72,000,
Dinesh's share in profit = Rs. 36,000,
Rakesh's share in profit = Rs. 12,000.

Deficiency of Rakesh (Rs. 13,000) will be shared by Mahesh and Dinesh in the ratio of 3:2. Mahesh will bear 3/5 of 13,000, i.e. Rs. 7,800 and Rakesh, 2/5 of Rs. 13,000, i.e. Rs. 5,200.

Thus, the profits of the firm will be shared as follows.
Mahesh will get Rs. 72,000 – Rs. 7,800 = Rs. 64,200.
Dinesh will get Rs. 36,000 – Rs. 5,200 = Rs. 30,800
Rakesh will get Rs. 12,000 + Rs. 7,800 + Rs. 5,200 = Rs. 25,000.

Do It Yourself

Kavita and Lalit are partners sharing profits in the ratio of 2:1. They decide to admit Mohan with share in profits with a guaranteed amount of Rs. 25,000. Both Kavita and Lalita undertake to meet the liability arising out of Guaranteed amount to Mohan in their respective profit sharing ratio. The profit sharing ratio between Kavita and Lalit does not change. The firm earned profits of Rs. 76,000 for the year 2006–07.Show the distribution of profit amongst the partners.

2.7 Past Adjustments

Sometimes a few omissions or errors in the recording of transactions or the preparation of summary statements are found after the final accounts have been prepared and the profits distributed among the partners. The omission may be in respect of interest on capitals, interest on drawings, interest on partners' loan, partner's salary, partner's commission or outstanding expenses. There may also be some changes in the provisions of partnership deed or system of accounting having impact with retrospective effect. All these acts of omission and commission need adjustments for correction of their impact. Instead of altering old accounts, necessary adjustments can be made either; (a) through 'Profit and Loss Adjustment Account', or (b) directly in the capital accounts of the concerned partners. This is explained with the help of following example.

Rameez and Zaheer are equal partners. Their capitals as on April 01, 2015 were Rs. 50,000 and Rs. 1,00,000 respectively. After the accounts for the financial year ending March 31, 2016 have been prepared, it is discovered that interest at the rate of 6 per cent per annum, as provided in the partnership deed has not been credited to the partners' capital accounts before distribution of profit. In this case, the interest on capital not credited to the partners' capital accounts works out to be Rs. 3000 (6/100 × Rs. 50,000) for Rameez and Rs. 6,000 (6/100 × Rs. 1,00,000) for Zaheer. Had the interest on capital been duly provided, the firm's profit would have reduced by Rs. 9,000. By this omission, the whole amount of profit as per Profit and Loss Account (without adjustment of Rs. 9,000) has been distributed among the partners in their profit sharing ratio, and the amounts of interest on capital have not been credited to their capital accounts. This error can be rectified in any of the following ways;

(a) Through Profit and Loss Adjustment Account

(i)	Profit and Loss Adjustment A/c	Dr.	9,000	
	To Rameez's capital A/c			3,000
	To Zaheer's capital A/c			6,000
	(Interest on capital)			

(ii)	Rameez's capital A/c	Dr.	4,500	
	Zaheer's capital A/c	Dr.	4,500	
	To Profit and Loss Adjustment A/c			9,000
	(Loss on adjustment)			

(b) Directly in Partners' Capital Accounts

For direct adjustment in partners' capital accounts first a statement to ascertain the net effect of omission on partners' capital accounts will be worked out as follows and then the adjustment entries can be recorded.

Statement Showing Net Effect of Omitting Interest on Capital

Details	*Rameez (Rs.)*	*Zaheer (Rs.)*
(i) Amount which should have been credited as interest on capital	3,000	6,000
(ii) Amount actually credited by way of share of profit (Rs. 9,000 divided equally)—	4,500	4,500
(iii) Difference between (i) and (ii) (Net effect)	**Dr. 1,500 (Excess)**	**Cr. 1,500 (Short)**

The statement shows that Rameez has got excess credit of Rs. 1,500 while Zaheer's account has been credited less by Rs. 1,500. In order to rectify the error Rameez's capital account should be debited and that of Zaheer, credited with Rs. 1,500 by passing the following journal entry;
journal entry.

Rameez's Capital A/c	Dr.	1,500	
To Zaheer's Capital A/c			1,500
(Adjustment for omission of interest on capital)			

Illustration 12

Nusrat, Sonu and Himesh are partners sharing profits and losses in the ratio of 5 : 3 : 2. The partnership deed provides for charging interest on drawing's @ 10% p.a. The drawings of Nusrat, Sonu and Himesh during the year ending December 2015 amounted to Rs. 20,000, Rs. 15,000 and Rs. 10,000 respectively. After the final accounts have been prepared, it was discovered that interest on drawings has not been taken into consideration. Give necessary adjusting journal entry.

Statement showing Net Effect of Omitting Interest on Drawings

Particulars	*Nusrat (Rs.)*	*Sonu (Rs.)*	*Himesh (Rs.)*	*Total*
Amount which should have been debited by way of interest on drawings	2,000	1,500	1,000	4,500
Amount that should have been credited by way of share of profit	2,250	1,350	900	4,500
Required Adjustment	**Cr. 250 (Short)**	**Cr. 150 (Excess)**	**Cr.100 (Excess)**	

Journal Entry for adjustment of interest on drawings would be:

Sonu's Capital A/c	Dr.	150	
Himesh's Capital A/c	Dr.	100	
To Nusrat's Capital A/c			250
(Adjustment for omission of interest on drawings)			

Do it Yourself

1. Gupta and Sarin are partners in a firm sharing profits in the ratio of 3:2. Their fixed capitals are: Gupta 2,00,000, and Sarin 3,00,000. After the accounts for the year are prepared it is discovered that interest on capital @10% p.a. as provided in the partnership agreement, has not been credited in the capital accounts of partners before distribution of profits. Record adjustment entry to rectify the error.
2. Krishna, Sandeep and Karim are partners sharing profits in the ratio of 3:2:1. Their fixed capitals are: Krishan Rs. 1,20,000, Sandeep 90,000 and Karim 60,000. For the year 2014-15, interest was credited to them @ 6% p.a. instead of 5% p.a. Record adjustment entry.
3. Leela, Meera and Neha are partners and have omitted interest on capital @9% p.a. for three years ended March 31, 2013. Their fixed capitals on which interest was to be allowed throughout were: Leela Rs. 80,000, Meera Rs. 60,000 and Neha Rs. 1,00,000. Their profit sharing ratio during the last three years were:

Year	*Leela*	*Meera*	*Neha*
2015-16	2	2	2
2014-15	4	5	1
2013-14	1	2	2

Record adjustment entry.

2.8 Final Accounts

The final accounts of a partnership firm are prepared in the same way as those prepared for a sole trading concern with just one difference which relates to the distribution of profit among the partners. After preparing the Trading and Profit and Loss Account, the net profit or net loss is transferred to an account called Profit and Loss Appropriation Account as discussed earlier in this chapter. As you know, all adjustments in respect of interest on capital, interest on drawings, partner's salary, partners' share of profit and loss, interest on partner's loan, etc. are made through the Profit and Loss Appropriation Account. This is done in order to distinguish between the results of operations of business and the distribution of the profit among the owners. The preparation of final accounts and the Profit & Loss Appropriation Account is clarified with the help of Illustration 13.

Illustration 13

Kapil and Vineet were partners sharing profits and losses in the ratio of 3:2. The following balances were extracted from the books of account for the year ended March 31, 2017.

	Debit Amount (Rs.)	*Credit Amount (Rs.)*
Capitals		
Kapil	—	60,000
Vineet	—	50,000
Current accounts (on April 01, 2013)		2,800
Kapil	—	
Vineet	—	1,600
Drawings:		—
Kapil	12,000	—
Vineet	8,000	—
Stock as on 1.4.2016	11,000	
Purchases and Sales	54,000	80,000
Returns	2,000	1,500
Wages	2,500	—
Salaries	4,000	—
Printing and Stationery	500	—
Bills receivables	12,000	—
Bills payables	—	2,000
Debtors and Creditors	36,000	8,000
Discounts	1,200	1,500
Rent and Rates	800	—
Bad debts	1,400	—
Insurance	400	—
Postage and Telegrams	300	—
Salesman's commission	3,400	—
Land and Building	24,000	—
Plant and Machinery	20,000	—
Furniture	13,500	—
Overdraft	—	2,000
Trade expenses	400	—
Cash in hand	500	—
Cash at bank	1,500	—
	2,09,400	**2,09,400**

Prepare the final accounts for the year ended March 31, 2017 firm taking into consideration the following:

(a) Stock on March 31, 2017 was Rs. 18,000;
(b) Provision for doubtful debts is to be provided at 5% on debtors;
(c) Outstanding salaries were Rs. 1,000;
(d) Goods worth Rs. 8,000 were destroyed by fire on December 10, 2016. The Insurance Company agreed to pay Rs. 7,000 in full settlement of the claim;
(e) Interest on capitals is allowed at 6% per annum and interest on drawings is also charged at 6% per annum;
(f) Kapil is entitled to a Salary of Rs. 1,200 per annum;
(g) Write-off Land and buildings at 5%, Furniture at 10% and Plant and Machinery at 15%.

Solution

Trading and Profit & Loss Account for the year ending March 31, 2017

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*		*Amount (Rs.)*
Opening stock		11,000	Sales	80,000	
Purchases	54,000		*Less:* Returns	2,000	78,000
Less: Returns	1,500	52,500	Closing stock		18,000
Wages		2,500	Goods destroyed by fire		8,000
Gross Profit c/d		38,000			
		1,04,000			**1,04,000**
Salaries	4,000		Gross Profit b/d		38,000
Add: Outstanding	1,000	5,000	Discount received		1,500
Printing and Stationery		500			
Rent and Rates		800			
Insurance		400			
Discount allowed		1,200			
Trade expenses		400			
Postage and Telegrams		300			
Bad debts	1,400				
Add: Provision	1,800	3,200			
Salesman's commission		3,400			
Loss due to fire (Rs. 8000–Rs. 7000)		1,000			
Depreciation:					
Land and Buildings	1,200				
Furniture	1,350				
Plant and Machinery	3,000	5,550			
Net Profit transferred to Profit and Loss Appropriation		17,750			
		39,500			**39,500**

Profit and Loss Appropriation Account

Dr. *Cr.*

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
Interest on capital:			Profit and Loss		17,750
Kapil	3,600		Interest on drawings:		
Vineet	3,000	6,600	(for 6 months)		
Salary to Kapil		1,200	Kapil	360	
Net profit (transferred to capital accounts)			Vineet	240	600
Kapil	6,330				
Vineet	4,220	10,550			
		18,350			**18,350**

Partner's Current Accounts

Dr. *Cr.*

Date	Particulars	J.F.	Kapil (Rs.)	Vineet (Rs.)	Date	Particulars	J.F.	Kapil (Rs.)	Vineet (Rs.)
	Drawings		12,000	8,000		Balance b/d		2,800	1,600
	Interest on drawings		360	240		Interest on capital		3,600	3,000
	Balance c/d		1,570	580		Salary		1,200	—
						Share of profit		6,330	4,220
			13,930	**8,820**				**13,930**	**8,820**
						Balance c/d		1,570	580

Balance Sheet as on March 31, 2017

Liabilities		Amount (Rs.)	Assets		Amount (Rs.)
Overdraft		2,000	Land and Building	24,000	
Bill payables		2,000	*Less:* Depreciation	1,200	22,800
Creditors		8,000	Plant and Machinery	20,000	
Outstanding salaries		1,000	*Less:* Depreciation	3,000	17,000
Capital:			Furniture	13,500	
Kapil	60,000		*Less:* Depreciation	1,350	12,150
Vineet	50,000	1,10,000	Stock		18,000
Current Accounts			Debtors	36,000	
Kapil	1,570		*Less:* Provision for discount on debtors	1,800	34,200
Vineet	580	2,150			
			Insurance company		7,000
			Bill receivables		12,000
			Cash at bank		1,500
			Cash in hand		500
		1,25,150			**1,25,150**

Terms Introduced in the Chapter

- Partnership
- Partnership Firm
- Partnership Deed
- Fixed Capital Account
- Fluctuating Capital Account
- Profit and Loss Adjustment Account
- Interest on Capital
- Interest on Drawings
- Average Period
- Profit and Loss Appropriation Account
- Partner's Current Account

Summary

1. *Definition of partnership and its essential features:* Partnership is defined as "Relation between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all". The essential features of partnership are : (i) To form a partnership, there must be at least two persons; (ii) It is created by an agreement; (iii) The agreement should be for carrying on some legal business; (iv) sharing of profits and losses; and (v) relationship of mutual agency among the partners.
2. *Meaning and contents of partnership deed:* A document which contains the terms of partnership as agreed among the partners is called 'Partnership Deed'. It usually contains information about all aspects affecting relationship between partners, including objective of business, contribution of capital by each partner, ratio in which profit and losses will be shared by the partners, entitlement of partners to interest on capital, interest on loan and the rules to be followed in case of admission, retirement, death, dissolution, etc.
3. *Provisions of Partnership Act 1932 applicable to accounting:* If partnership deed is silent in respect of certain aspects, the relevant provisions of the Indian Partnership Act, 1932 become applicable. According to the Partnership Act, the partners share profits equally, no partner is entitled to remuneration, no interest on capital is allowed and no interest on drawings is charged. However, if any partner has given some loan to the firm, he is entitled to interest on such amount @ 6% per annum.
4. *Preparation of capital accounts under fixed and fluctuating capital methods:* All transactions relating to partners are recorded in their respective capital accounts in the books of the firm. There can be two methods of maintaining Capital Accounts. These are; (i) fluctuating capital method, (ii) fixed capital method. Under fluctuating capital method, all the transactions relating to a partner are directly recorded in the capital account. Under fixed capital method, however the amount of capital remains fixed, the transactions like interest on capital, drawings, interest on drawings, salary, commission, share of profit or loss are recorded in a separate account called 'Partner's Current Account'.

5. *Distribution of profit and loss:* The distribution of profits among the partners is shown through a Profit and Loss Appropriation Account, which is merely an extension of the Profit and Loss Account. It is usually debited with interest on capital and salary/commission allowed to the partners, and credited with net profit as per Profit and Loss Account and the interest on drawings. The balance being profit or loss is distributed among the partners in the profit sharing ratio and transferred to their respective capital accounts.
6. *Treatment of guarantee of minimum profit to a partner:* Sometimes, a partner may be guaranteed a minimum amount by way of his share in profits. If, in any year, the share of profits as calculated according to his profit sharing ratio is less than the guaranteed amount, the deficiency is made good by the guaranteeing partners' in the agreed ratio which usually is the profit sharing ratio. If, however, such guarantee has been given by any of them, he or they alone shall bear the amount of deficiency.
7. *Treatment of past adjustments:* If, after the final accounts have been prepared, some omission or commissions are noticed say in respect of the interest on capital, interest on drawings, partner's salary, commission, etc. necessary adjustments can be made in the partner's capital accounts through the Profit and Loss Adjustment Account, to rectify the same.
8. *Preparation of final accounts of a partnership firm:* There is not much difference in the final accounts of a sole proprietary concern and that of a partnership firm except that in case of a partnership firm an additional account called Profit and Loss Appropriation Account is prepared to show distribution of profit and loss among the partners.

Questions for Practice

Short Answer Questions

1. Define Partnership Deed.
2. Why it is considered desirable to make the partnership agreement in writing.
3. List the items which may be debited or credited in capital accounts of the partners when:
   (i) Capitals are fixed.
   (ii) Capital are fluctuating.
4. Why is Profit and Loss Adjustment Account prepared? Explain.
5. Give two circumstances under which the fixed capitals of partners may change.
6. If a fixed amount is withdrawn on the first day of every quarter, for what period the interest on total amount withdrawn will be calculated?

7. In the absence of Partnership deed, specify the rules relating to the following :
   (i) Sharing of profits and losses.
   (ii) Interest on partner's capital.
   (iii) Interest on Partner's drawings.
   (iv) Interest on Partner's loan
   (v) Salary to a partner.

Long Answer Questions

1. What is partnership? What are its chief characteristics? Explain.
2. Discuss the main provisions of the Indian Partnership Act 1932 that are relevant to partnership accounts if there is no partnership deed.
3. Explain why it is considered better to make a partnership agreement in writing.
4. Illustrate how interest on drawings will be calculated under various situations.
5. How will you deal with a change in profit sharing ratio among existing partners? Take imaginary figures to illustrate your answer?

Numerical Questions

Fixed and Fluctuating Capitals

1. Triphati and Chauhan are partners in a firm sharing profits and losses in the ratio of 3:2. Their capitals were Rs.60,000 and Rs.40,000 as on January 01, 2015. During the year they earned a profit of Rs. 30,000. According to the partnership deed both the partners are entitled to Rs. 1,000 per month as salary and 5% interest on their capital. They are also to be charged an interest of 5% on their drawings, irrespective of the period, which is Rs. 12,000 for Tripathi, Rs. 8,000 for Chauhan. Prepare Partner's Accounts when, capitals are fixed.

   (**Ans :** Tripathi's Current account Balance Rs. 3,600,Chauhan's Current account Balance Rs.6,400)

2. Anubha and Kajal are partners of a firm sharing profits and losses in the ratio of 2:1. Their capital, were Rs.90,000 and Rs.60,000. The profit during the year were Rs. 45,000. According to partnership deed, both partners are allowed salary, Rs. 700 per month to Anubha and Rs. 500 per month to Kajal. Interest allowed on capital @ 5%p.a. The drawings at the end of the period were Rs. 8,500 for Anubha and Rs. 6,500 for Kajal. Interest is to be charged @ 5% p.a. on drawings. Prepare partners capital accounts, assuming that the capital account are fluctuating.
   (**Ans :** Anubha's Capital Account Balance Rs.1,09,075, Kajal's Capital Account Balance Rs.70,175)

Distribution of Profits

3. Harshad and Dhiman are in partnership since April 01, 2016. No Partnership agreement was made. They contributed Rs. 4,00,000 and 1,00,000 respectively as capital. In addition, Harshad advanced an amount of Rs. 1,00,000 to the firm, on October 01, 2016. Due to long illness, Harshad could not participate in business activities from August 1, to September 30, 2016. The profits for the year ended March 31, 2017 amounted to Rs. 1,80,000.
   Dispute has arisen between Harshad and Dhiman.

   Harshad Claims:
   (i) he should be given interest @ 10% per annum on capital and loan;
   (ii) Profit should be distributed in proportion of capital;

   Dhiman Claims:
   (i) Profits should be distributed equally;
   (ii) He should be allowed Rs. 2,000 p.m. as remuneration for the period he managed the business, in the absence of Harshad;
   (iii) Interest on Capital and loan should be allowed @ 6% p.a.

   You are required to settle the dispute between Harshad and Dhiman. Also prepare Profit and Loss Appropriation Account.

   (**Ans :** Harshad's share in profit Rs. 88,500, Dhiman's share in profit Rs. 88,500)

4. Aakriti and Bindu entered into partnership for making garment on April 01, 2016 without any Partnership agreement. They introduced Capitals of Rs. 5,00,000 and Rs. 3,00,000 respectively on October 01, 2016. Aakriti Advanced. Rs, 20,000 by way of loan to the firm without any agreement as to interest. Profit and Loss account for the year ended March 31 2017 showed profit of Rs, 43,000. Partners could not agree upon the question of interest and the basis of division of profit. You are required to divide the profits between them giving reason for your solution.

   (**Ans :** Profit shares equal Aakriti and Bindu Rs. 21,200)

5. Rakhi and Shikha are partners in a firm, with capitals of Rs. 2,00,000 and Rs, 3,00,000 respectively. The profit of the firm, for the year ended 2016-17 is Rs. 23,200. As per the Partnership agreement, they share the profit in their capital ratio, after allowing a salary of Rs. 5,000 per month to Shikha and interest on Partner's capital at the rate of 10% p.a. During the year Rakhi withdrew Rs. 7,000 and Shikha Rs. 10,000 for their personal use. As per partnership deed, salary and interest are caption treated as charged. You are required to prepare Profit and Loss Account and Partner's Capital Accounts.

   (**Ans :** Loss Transferred to Rakhi Capital Rs.34,720 and Shikha Capital Rs.52,080)

6. Lokesh and Azad are partners sharing profits in the ratio 3:2, with capitals of Rs. 50,000 and 30,000, respectively. Interest on capital is agreed to be paid

@ 6% p.a. Azad is allowed a salary of Rs. 2,500 p.a. During 2016, the profits prior to the calculation of interest on capital but after charging Azad's salary amounted to Rs. 12,500. A provision of 5% of profits is to be made in respect of manager's commission. Prepare accounts showing the allocation of profits and partner's capital accounts.

(**Ans :** Profit transferred to Lokesh's Capital Rs. 4,170 and Azad's Capital Rs.2,780)

7. The partnership agreement between Maneesh and Girish provides that:
   (i) Profits will be shared equally;
   (ii) Maneesh will be allowed a salary of Rs. 400 p.m;
   (iii) Girish who manages the sales department will be allowed a commission equal to 10% of the net profits, after allowing Maneesh's salary;
   (iv) 7% interest will be allowed on partner's fixed capital;
   (v) 5% interest will be charged on partner's annual drawings;
   (vi) The fixed capitals of Maneesh and Girish are Rs. 1,00,000 and Rs. 80,000, respectively. Their annual drawings were Rs. 16,000 and 14,000, respectively. The net profit for the year ending March 31, 2015 amounted to Rs. 40,000;
   Prepare firm's Profit and Loss Appropriation Account.

   (**Ans :** Profit transferred to the Capital accounts of Maneesh and Girish each, Rs.10,290)

8. Ram, Raj and George are partners sharing profits in the ratio 5 : 3 : 2. According to the partnership agreement George is to get a minimum amount of Rs. 10,000 as his share of profits every year. The net profit for the year 2013 amounted to Rs, 40,000. Prepare the Profit and Loss Appropriation Account.

   (**Ans :** Profit transferred to Ram's Capital Rs.18,750 Raj's Capital Rs.11,250 and George's Capital Rs.10,000)

9. Amann, Babita and Suresh are partners in a firm. Their profit sharing ratio is 2:2:1. Suresh is guaranteed a minimum amount of Rs. 10,000 as share of profit, every year. Any deficiency on that account shall be met by Babita. The profits for two years ending March 31, 2016 and March 31, 2017 were Rs. 40,000 and Rs. 60,000, respectively. Prepare the Profit and Loss Appropriation Account for the two years.

   (**Ans :** For the year 2016, Profits transferred to Amann's Capital, Rs.16,000; Babita's Capital Rs.14,000; Suresh's capital Rs.10,000 and for the year 2017, Profit transferred to Amann's Capital Rs.24,000, Babita's Capital Rs.24,000, Suresh's capital, Rs.12,000)

10. Simmi and Sonu are partners in a firm, sharing profits and losses in the ratio of 3:1. The profit and loss account of the firm for the year ending March 31, 2017 shows a net profit of Rs. 1,50,000. Prepare the Profit and Loss Appropriation Account by taking into consideration the following information:
    (i) Partners capital on April 1, 2016;
    Simmi, Rs. 30,000; Sonu, Rs. 60,000;

(ii) Current accounts balances on April 1, 2016;
Simmi, Rs. 30,000 (cr.); Sonu, Rs. 15,000 (cr.);

(iii) Partners drawings during the year amounted to
Simmi, Rs. 20,000; Sonu, Rs. 15,000;

(iv) Interest on capital was allowed @ 5% p.a.;

(v) Interest on drawing was to be charged @ 6% p.a. at an average of six months;

(vi) Partners' salaries : Simmi Rs. 12,000 and Sonu Rs. 9,000. Also show the partners' current accounts.

(**Ans :** Profit transferred to Simmi's Capital, Rs. 94,162 and Sonu's Capital, Rs. 31,388)

11. Ramesh and Suresh were partners in a firm sharing profits in the ratio of their capitals contributed on commencement of business which were Rs. 80,000 and Rs. 60,000 respectively. The firm started business on April 1, 2016. According to the partnership agreement, interest on capital and drawings are 12% and 10% p.a., respectively. Ramesh and Suresh are to get a monthly salary of Rs. 2,000 and Rs. 3,000, respectively.

The profits for year ended March 31, 2017 before making above appropriations was Rs. 1,00,300. The drawings of Ramesh and Suresh were Rs. 40,000 and Rs. 50,000, respectively. Interest on drawings amounted to Rs. 2,000 for Ramesh and Rs. 2,500 for Suresh. Prepare Profit and Loss Appropriation Account and partners' capital accounts, assuming that their capitals are fluctuating.

(**Ans :** Profit transferred to Ramesh's Capital Rs.16,000 and Suresh's Capital, Rs.12,000)

12. Sukesh and Vanita were partners in a firm. Their partnership agreement provides that:

(i) Profits would be shared by Sukesh and Vanita in the ratio of 3:2;

(ii) 5% interest is to be allowed on capital;

(iii) Vanita should be paid a monthly salary of Rs. 600.

The following balances are extracted from the books of the firm, on March 31, 2017.

	Sukesh (Rs.)	*Vanita (Rs.)*
Capital Accounts	40,000	40,000
Current Accounts	(Cr.) 7,200	(Cr.) 2,800
Drawings	10,850	8,150

Net profit for the year, before charging interest on capital and after charging partner's salary was Rs. 9,500. Prepare the Profit and Loss Appropriation Account and the Partner's Current Accounts.

(**Ans :** Profit transferred to Sukesh's Capital, Rs.3,300 and Vanita's Capital, Rs. 2,200)

Calculation of Interest on Capital and Interest on Drawings

13. Rahul, Rohit and Karan started partnership business on April 1, 2016 with capitals of Rs. 20,00,000, Rs. 18,00,000 and Rs. 16,00,000, respectively. The profit for the year ended March 2017 amounted to Rs.1,35,000 and the partner's drawings had been Rahul Rs. 50,000, Rohit Rs. 50,000 and Karan Rs. 40,000. The profits are distributed among partner's in the ratio of 3:2:1. Calculate the interest on capital @ 5% p.a.

    (**Ans :** Rahul, Rs. 1,00,000, Rohit, Rs. 90,000, Karan Rs. 80,000)

14. Sunflower and Pink Rose started partnership business on April 01, 2016 with capitals of Rs. 2,50,000 and Rs.1,50,000, respectively. On October 01, 2016, they decided that their capitals should be Rs. 2,00,000 each. The necessary adjustments in the capitals are made by introducing or withdrawing cash. Interest on capital is to be allowed @ 10% p.a. Calculate interest on capital as on March 31, 2017.

    (**Ans :** Total interest on Sunflower's Capital Rs. 22,500 and on Pink Rose's Capital, Rs. 17,500)

15. On March 31, 2017 after the close of accounts, the capitals of Mountain, Hill and Rock stood in the books of the firm at Rs. 4,00,000,Rs.3,00,000 and Rs. 2,00,000, respectively. Subsequently, it was discovered that the interest on capital @ 10% p.a. had been omitted. The profit for the year amounted to Rs. 1,50,000 and the partner's drawings had been Mountain: Rs. 20,000, Hill Rs. 15,000 and Rock Rs. 10,000.
    Calculate interest on capital.

    (**Ans :** Interest on Capital: Mountain, Rs.37,000; Hill, Rs.26,500; Rock, Rs.16,000)

16. Following is the extract of the Balance Sheet of, Neelkant and Mahdev as on March 31, 2017:

Balance Sheet as at March 31, 2017

Liabilities	*Amount (Rs.)*	*Assets*	*Amount (Rs.)*
Neelkant's Capital	10,00,000	Sundry Assets	30,00,000
Mahadev's Capital	10,00,000		
Neelkant's Current Account	1,00,000		
Mahadev's Current Account	1,00,000		
Profit and Loss Apprpriation (March 2017)	8,00,000		
	30,00,000		**30,00,000**

During the year Mahadev's drawings were Rs. 30,000. Profits during 2016-17 is Rs. 10,00,000. Calculate interest on capital @ 5% p.a for the year ending March 31, 2017.

(**Ans :** Interest on Neelkant's Capital, Rs. 50,000 and Mahadev's Capital, Rs. 50,000)

17. Rishi is a partner in a firm. He withdrew the following amounts during the year ended March 31, 2017.

May 01, 2017	Rs. 12,000
July 31, 2017	Rs. 6,000
September 30, 2017	Rs. 9,000
November 30, 2017	Rs. 12,000
January 01, 2018	Rs. 8,000
March 31, 2018	Rs. 7,000

Interest on drawings is charged @ 9% p.a.
Calculate interest on drawings

(**Ans :** Interest on Drawing Rs. 2,295)

18. The capital accounts of Moli and Golu showed balances of Rs.40,000 and Rs. 20,000 as on April 01, 2016. They shared profits in the ratio of 3:2. They allowed interest on capital @ 10% p.a. and interest on drawings, @ 12 p.a. Golu advanced a loan of Rs. 10,000 to the firm on August 01, 2016.
During the year, Moli withdrew Rs. 1,000 per month at the beginning of every month whereas Golu withdrew Rs. 1,000 per month at the end of every month. Profit for the year, before the above mentioned adjustments was Rs.20,950. Calculate interest on drawings show distribution of profits and prepare partner's capital accounts.

(**Ans :** Interest on Drawings : Moli, Rs. 780; Golu, Rs. 660; Profits Moli, Rs. 9,594; Golu, Rs. 6,396)

19. Rakesh and Roshan are partners, sharing profits in the ratio of 3:2 with capitals of Rs. 40,000 and Rs. 30,000, respectively. They withdrew from the firm the following amounts, for their personal use:

Rakesh	*Month*	*Rs.*
	May 31, 2016	600
	June 30, 2016	500
	August 31, 2016	1,000
	November 1, 2016	400
	December 31, 2016	1,500
	January 31, 2017	300
	March 01, 2017	700
Rohan	*At the beginning of each month*	*400*

Interest is to be charged @ 6% p.a. Calculate interest on drawings, assuming that book of accounts are closed on March 31, 2017, every year.

(**Ans :** Interest on Rakesh's Drawings : Rs. 126.50; Rohan's Drawings Rs. 156 rounded off to nearest rupee)

20. Himanshu withdrews Rs. 2,500 at the end Month of each month. The Partnership deed provides for charging the interest on drawings @ 12% p.a. Calculate interest on Himanshu's drawings for the year ending 31st December, 2017.

(**Ans :** Interest on Drawings Rs.1,650)

21. Bharam is a partner in a firm. He withdraws Rs. 3,000 at the starting of each month for 12 months. The books of the firm closes on March 31 every year. Calculate interest on drawings if the rate of interest is 10% p.a.

    (**Ans :** Interest on Drawings, Rs.1,950)

22. Raj and Neeraj are partners in a firm. Their capitals as on April 01, 2017 were Rs. 2,50,000 and Rs. 1,50,000, respectively. They share profits equally. On July 01, 2017, they decided that their capitals should be Rs. 1,00,000 each. The necessary adjustment in the capitals were made by introducing or withdrawing cash by the partners'. Interest on capital is allowed @ 8% p.a. Compute interest on capital for both the partners for the year ending on March 31, 2018.

    (**Ans :** Raj Rs. 11,000 and Neeraj's Rs. 9,000)

23. Amit and Bhola are partners in a firm. They share profits in the ratio of 3:2. As per their partnership agreement, interest on drawings is to be charged @ 10% p.a. Their drawings during 2017 were Rs. 24,000 and Rs. 16,000, respectively. Calculate interest on drawings based on the assumption that the amounts were withdrawn evenly, throughout the year.

    (**Ans :** Interest on Amit's Drawings, Rs. 1,200 and Bhola's, Rs.800)

24. Harish is a partner in a firm. He withdrew the following amounts during the year 2017 :

	Rs.
February 01	4,000
May 01	10,000
June 30	4,000
October 31	12,000
December 31	4,000

    Interest on drawings is to be charged @ $7\frac{1}{2}$ % p.a.
    Calculate the amount of interest to be charged on Harish's drawings for the year ending December 31, 2017.

    (**Ans :** Interest on Drawings, Rs.1,075)

25. Menon and Thomas are partners in a firm. They share profits equally. Their monthly drawings are Rs. 2,000 each. Interest on drawings is to be charged @ 10% p.a. Calculate interest on Menon's drawings for the year 2006, assuming that money is withdrawn: (i) in the beginning of every month, (ii) in the middle of every month, and (iii) at the end of every month.

    (**Ans :** (i) Interest on Drawings, Rs.1,300; (ii) Rs.1,200; (iii) Rs.1,100)

26. On March 31, 2017, after the close of books of accounts, the capital accounts of Ram, Shyam and Mohan showed balance of Rs. 24,000 Rs. 18,000 and Rs. 12,000, respectively. It was later discovered that interest on capital @ 5% had been omitted. The profit for the year ended March 31, 2017, amounted to Rs. 36,000 and the partner's drawings had been Ram, Rs. 3,600; Shyam, Rs. 4,500 and Mohan, Rs. 2,700. The profit sharing ratio of Ram, Shyam and Mohan was 3:2:1. Calculate interest on capital.

    (**Ans :** Interest on Ram's Capital Rs.480; Shyam's Capital, Rs.525 and Mohan's Capital, Rs.435)

Guarantee of Profit to the Partners

27. Amit, Sumit and Samiksha are in partnership sharing profits in the ratio of 3:2:1. Samiksha' share in profit has been guaranteed by Amit and Sumit to be a minimum sum of Rs. 8,000. Profits for the year ended March 31, 2017 was Rs. 36,000. Divide profit among the partners.

    (**Ans :** Profit to Amit Rs. 16,800; Sumit, Rs. 11,200; Samiksha, Rs. 8,000)

28. Pinki, Deepati and Kaku are partner's sharing profits in the ratio of 5:4:1. Kaku is given a guarantee that his share of profits in any given year would not be less than Rs. 5,000. Deficiency, if any, would be borne by Pinki and Deepti equally. Profits for the year amounted to Rs. 40,000. Record necessary journal entries in the books of the firm showing the distribution of profit.

    (**Ans :** Deficiency borne by Pinki and Deepti Rs.500 each)

29. Abhay, Siddharth and Kusum are partners in a firm, sharing profits in the ratio of 5:3:2. Kusum is guaranteed a minimum amount of Rs. 10,000 as per share in the profits. Any deficiency arising on that account shall be met by Siddharth. Profits for the years ending March 31, 2016 and 2017 are Rs. 40,000 and 60,000 respectively. Prepare Profit and Loss Appropriation Account.

    (**Ans :** year 2015 - Abhay Rs. 20,000, Siddharth Rs. 10,000, Kusum Rs. 10,000; year 2016- Abhay Rs. 30,000, Siddharth Rs. 18,000, Kusum Rs. 12,000)

30. Radha, Mary and Fatima are partners sharing profits in the ratio of 5:4:1. Fatima is given a guarantee that her share of profit, in any year will not be less than Rs. 5,000. The profits for the year ending March 31, 2017 amounts to Rs. 35,000. Shortfall if any, in the profits guaranteed to Fatima is to be borne by Radha and Mary in the ratio of 3:2. Record necessary journal entry to show distributioin of profit among partner.

    (**Ans :** Deficiency borne by Radha, Rs. 900 and Mary, Rs. 600)

31. X, Y and Z are in Partnership, sharing profits and losses in the ratio of 3 : 2 : 1, respectively. Z's share in the profit is guaranteed by X and Y to be a minimum of Rs. 8,000. The net profit for the year ended March 31, 2017 was Rs. 30,000. Prepare Profit and Loss Appropriation Account, indicating the amount finally due to each partner.

    (**Ans :** Profit to X Rs.13,200; Y Rs.8,800; Z Rs.8,000)

32. Arun, Boby and Chintu are partners in a firm sharing profit in the ratio or 2:2:1. According to the terms of the partnership agreement, Chintu has to get a minimum of Rs. 60,000, irrespective of the profits of the firm. Any Deficiency to Chintu on Account of such guarantee shall be borne by Arun. Prepare the profit and loss appropriation account showing distribution of profits among partners in case the profits for year 2015 are: (i) Rs. 2,50,000; (ii) 3,60,000.

    (**Ans :** (i) Profit to Arun Rs.90,000, Boby Rs.1,00,000 and Chintu Rs.60,000 (ii) Profit to Arun Rs.1,44,000, Boby Rs.1,44,000 and Chintu Rs.72,000)

33. Ashok, Brijesh and Cheena are partners sharing profits and losses in the ratio of 2 : 2 : 1. Ashok and Brijesh have guaranteed that Cheena share in any year shall be less than Rs. 20,000. The net profit for the year ended March 31, 2017 amounted to Rs. 70,000. Prepare Profit and Loss Appropriation Account.

    (**Ans :** Profit to Ashok Rs.25,000, Brijesh Rs. 25,000 and Cheena Rs. 20,000)

34. Ram, Mohan and Sohan are partners with capitals of Rs. 5,00,000, Rs. 2,50,000 and 2,00,000 respectively. After providing interest on capital @ 10% p.a. the profits are divisible as follows:

    Ram $\frac{1}{2}$, Mohan $\frac{1}{3}$ and Sohan $\frac{1}{6}$. But Ram and Mohan have guaranteed that Sohan's share in the profit shall not be less than Rs. 25,000, in any year. The net profit for the year ended March 31, 2017 is Rs. 2,00,000, before charging interest on capital.

    You are required to show distribution of profit.

    (**Ans :** Profit to Ram, Rs. 48,000, Mohan, Rs. 32,000 and Sohan, Rs. 25,000)

35. Amit, Babita and Sona form a partnership firm, sharing profits in the ratio of 3 : 2 : 1, subject to the following :
    (i) Sona's share in the profits, guaranteed to be not less than Rs. 15,000 in any year.
    (ii) Babita gives guarantee to the effect that gross fee earned by her for the firm shall be equal to her average gross fee of the proceeding five years, when she was carrying on profession alone (which is Rs. 25,000). The net profit for the year ended March 31, 2017 is Rs. 75,000. The gross fee earned by Babita for the firm was Rs. 16,000.

    You are required to show Profit and Loss Appropriation Account (after giving effect to the alone).

    (**Ans :** Profit transferred to Capital Accounts of; Amit, Rs. 41,400, Babita, Rs.27,600 and Sona, Rs.15,000)

Past Adjustment

36. The net profit of X, Y and Z for the year ended March 31, 2016 was Rs. 60,000 and the same was distributed among them in their agreed ratio of 3 : 1 : 1. It was subsequently discovered that the under mentioned transactions were not recorded in the books :
    (i) Interest on Capital @ 5% p.a.
    (ii) Interest on drawings amounting to X Rs. 700, Y Rs. 500 and Z Rs. 300.
    (iii) Partner's Salary : X Rs. 1000, Y Rs. 1500 p.a.

    The capital accounts of partners were fixed as : X Rs. 1,00,000, Y Rs. 80,000 and Z Rs. 60,000. Record the adjustment entry.

    [**Ans :** X Dr. Rs.2,500 , Y credit Rs.2,400 and Z credit Rs.100]

37. The firm of Harry, Porter and Ali, who have been sharing profits in the ratio of 2 : 2 : 1, have existed for same years. Ali wants that he should get equal share in the profits with Harry and Porter and he further wishes that the change in

the profit sharing ratio should come into effect retrospectively were for the last three year. Harry and Porter have agreement on this account.
The profits for the last three years were:

	(Rs.)
2014-15	22,000
2015-16	24,000
2016-17	29,000

Show adjustment of profits by means of a single adjustment journal entry.

(**Ans :** Harry (Dr.) Rs.5,000, Porter (Dr.) Rs.5,000 and Ali (Cr.) Rs.10,000)

38. Mannu and Shristhi are partners in a firm sharing profit in the ratio of 3 : 2. Following is the balance sheet of the firm as on March 31, 2017.

Balance Sheet as at March 31, 2017

Liabilities		*Amount (Rs.)*	*Assets*		*Amount (Rs.)*
Mannu's Capital	30,000		Drawings :		
Shristhi's Capital	10,000	40,000	Mannu	4,000	
			Shristhi	2,000	6,000
			Other Assets		34,000
		40,000			**40,000**

Profit for the year ended March 31, 2017 was Rs. 5,000 which was divided in the agreed ratio, but interest @ 5% p.a. on capital and @ 6% p.a. on drawings was inadvertently enquired. Adjust interest on drawings on an average basis for 6 months. Give the adjustment entry.
(**Ans :** Mannu (Cr.) Rs.288 and Shrishti (Dr.) Rs.288)

39. On March 31, 2017 the balance in the capital accounts of Eluin, Monu and Ahmed, after making adjustments for profits, drawing, etc; were Rs. 80,000, Rs. 60,000 and Rs. 40,000 respectively. Subsequently, it was discovered that interest on capital and interest on drawings had been omitted.

The partners were entitled to interest on capital @ 5% p.a. The drawings during the year were Eluin Rs. 20,000; Monu, Rs. 15,000 and Ahmed, Rs. 9,000. Interest on drawings chargeable to partners were Eluin Rs, 500, Monu Rs. 360 and Ahmed Rs. 200. The net profit during the year amounted to Rs. 1,20,000. The profit sharing ratio was 3 : 2 : 1. Record necessary adjustment entries.

(**Ans :** Eluin (Dr.) Rs.570, Monu (Cr.) Rs.10 and Ahmed (Cr.) Rs.560)

40. Azad and Benny are equal partners. Their capitals are Rs. 40,000 and Rs. 80,000, respectively. After the accounts for the year have been prepared it is discovered that interest at 5% p.a. as provided in the partnership agreement, has not been credited to the capital accounts before distribution of profits. It is decided to make an adjustment entry at the beginning of the next year. Record the necessary journal entry.

(**Ans :** Azad (Dr.)1,000 and Benny (Cr.)1,000)

41. Kavita and Pradeep are partners, sharing profits in the ratio of 3 : 2. They employed Chandan as their manager, to whom they paid a salary of Rs. 750 p.m. Chandan deposited Rs. 20,000 on which interest is payable @ 9% p.a. At the end of 2017 (after the division of profit), it was decided that Chandan should be treated as partner w.e.f. Jan. 1, 2014 with $\frac{1}{6}$th share in profits. His deposit being considered as capital carrying interest @ 6% p.a. like capital of other partners. Firm's profits after allowing interest on capital were as follows:

		(Rs.)
2014	Profit	59,000
2015	Profit	62,000
2016	Loss	(4,000)
2017	Profit	78,000

Record the necessary journal entries to give effect to the above.

(**Ans :** Kavita (Dr.) 300, Pradeep (Dr.) 200 and Chandan (Cr.) 500)

42. Mohan, Vijay and Anil are partners, the balance on their capital accounts being Rs. 30,000, Rs. 25,000 and Rs. 20,000 respectively. In arriving at these figures, the profits for the year ended March 31, 2017 amounting to Rupees 24,000 had been credited to partners in the proportion in which they shared profits. During the tear their drawings for Mohan, Vijay and Anil were Rs. 5,000, Rs. 4,000 and Rs. 3,000, respectively. Subsequently, the following omissions were noticed:

(a) Interest on Capital, at the rate of 10% p.a., was not charged.

(b) Interest on Drawings: Mohan Rs. 250, Vijay Rs. 200, Anil Rs. 150 was not recorded in the books.

Record necessary corrections through journal entries.

(**Ans :** Debit Anil's Capital Account by Rs. 550 and Credit Mohan's Capital Account by Rs. 550)

43. Anju, Manju and Mamta are partners whose fixed capitals were Rs. 10,000, Rs. 8,000 and Rs. 6,000, respectively. As per the partnership agreement, there is a provision for allowing interest on capitals @ 5% p.a. but entries for the same have not been made for the last three years. The profit sharing ratio during there years remained as follows:

Year	Anju	Manju	Mamta
2014	4	3	5
2015	3	2	1
2016	1	1	1

Make necessary and adjustment entry at the beginning of the fourth year i.e. Jan. 2015.

(**Ans :** Mamta (Dr.) Rs. 200, Anju (Cr.) Rs. 100 and manju (Cr.) Rs. 100)

44. Dinker and Ravinder were partners sharing profits and losses in the ratio of 2:1. The following balances were extracted from the books of account, for the year ended December 31, 2017.

Account Name	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
Capital		
Dinker		2,35,000
Ravinder		1,63,000
Drawings		
Dinker	6,000	
Ravinder	5,000	
Opening Stock	35,100	
Purchases and Sales	2,85,000	3,75,800
Carriage inward	2,200	
Returns	3,000	2,200
Stationerry	1,200	
Wages	12,500	
Bills receivables and Bills payables	45,000	32,000
Discount	900	400
Salaries	12,000	
Rent and Taxes	18,000	
Insurance premium	2,400	
Postage	300	
Sundry expenses	1,100	
Commission		3,200
Debtors and creditors	95,000	40,000
Building	1,20,000	
Plant and machinery	80,000	
Investments	1,00,000	
Furniture and Fixture	26,000	
Bad Debts	2,000	
Bad debts provision		4,600
Loan		35,000
Legal Expenses	200	
Audit fee	1,800	
Cash in hand	13,500	
Cash at Bank	23,000	
	8,91,200	**8,91,200**

Prepare final accounts for the year ended December 31,2017, with following adjustment:

(a) Stock on December 31,2017, was Rs. 42,500.
(b) A Provision is to be made for bad debts at 5% on debtors.
(c) Rent outstanding was Rs.1,600.
(d) Wages outstanding were Rs.1,200.
(e) Interest on capital to be allowed on capital @ 4% per annum and interest on drawings to be charged @ 6% per annum.
(f) Dinker and Ravinder are entitled to a Salary of Rs.2,000 per annum
(g) Ravinder is entitled to a commission Rs.1,500.

(h) Depreciation is to be charged on Building @ 4%, Plant and Machinery, 6%, and furniture and fixture, 5%.

(i) Outstanding interest on loan amounted to Rs. 350.

(**Ans :** Gross Profit Rs. 81,500, Net Profit Rs.32,200, Dinker 's Capital Rs. 2,47,627 Ravinder's Capital Rs.1,71,573, Total of Balance Sheet Rs. 5,29,350)

45. Kajol and Sunny were partners sharing profits and losses in the ratio of 3:2. The following Balances were extracted from the books of account for the year ended March 31, 2015.

Account Name	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
Capital		
Kajol		1,15,000
Sunny		91,000
Current accounts [on 1-04-2005]		
Kajol		4,500
Sunny	3,200	
Drawings		
Kajol	6,000	
Sunny	3,000	
Opening stock	22,700	
Purchases and Sales	1,65,000	2,35,800
Freight inward	1,200	
Returns	2,000	3,200
Printing and Stationery	900	
Wages	5,500	
Bills receivables and Bills payables	25,000	21,000
Discount	400	800
Salaries	6,000	
Rent	7,200	
Insurance premium	2,000	
Traveling expenses	700	
Sundry expenses	1,100	
Commission		1,600
Debtors and Creditors	74,000	78,000
Building	85,000	
Plant and Machinery	70,000	
Motor car	60,000	
Furniture and Fixtures	15,000	
Bad debts	1,500	
Provision for doubtful debts		2,200
Loan		25,000
Legal expenses	300	
Audit fee	900	
Cash in hand	7,500	
Cash at bank	12,000	
	5,78,100	**5,78,100**

Prepare final accounts for the year ended March 31,2017, with following adjustments:

(a) Stock on March 31,2015 was Rs.37,500.
(b) Bad debts Rs.3,000; Provision for bad debts is to be made at 5% on debtors.
(c) Rent Prepaid were Rs.1,200.
(d) Wages outstanding were Rs.2,200.
(e) Interest on capital to be allowed on capital at 6% per annum and interest on drawings to be charged @ 5% per annum.
(f) Kajol is entitled to a Salary of Rs. 1,500 per annum.
(g) Prepaid insurance was Rs. 500.
(h) Depreciation was charged on Building, @ 4%; Plant and Machinery, @ 5%; Motor car, @ 10% and furniture and fixture, @ 5%.
(i) Goods worth Rs.7,000 were destroyed by fire on January 20, 2015. The Insurance company agreed to pay Rs.5,000 in full settlement of the claim.

(**Ans :** Gross Profits Rs. 84,900; Net Profit, Rs. 48,000; Kajol's Current account, Rs. 27,369; Sunny's Current Account, Rs. 12,931; Total of Balance Sheet, Rs. 3,72,500)

Check-list to Test your Understanding

Test your Understanding – I

1. (i) Invalid (ii) Invalid (iii) Valid (iv) Invalid
2. (i) True (ii) True (iii) True (iv) False (v) False (vi) False

Test your Understanding – II

1. (i) Interest on loan given 6% p.a.
   (ii) No interest allowed on capital and charged on drawings
   (iii) Salary and Commission not given to partner
   (iv) Profit to the shared equally
2. Profit : Reena, Rs. 33,750; Raman, Rs. 33,750

Test your Understanding – III

1. Interest on capital; Rani, Rs. 9,600; Suman, Rs. 7,200
2. (a) Profit : Priya, Rs. 78,750; Kajal, Rs. 47,250
   (b) Profit NIL. Interest on capital: Priya, Rs. 54.000; Kajal, Rs. 72,000