

CHAPTER 5

Retirement/Death of a Partner

Introduction - Like admission and change in profit sharing ratio, in case of retirement or death also the existing partnership deed comes to an end and the new one comes into existence among the remaining partners. There is not much difference in the accounting treatment at the time of retirement or in the event of death.

Amount due to retiring deceased Partner

(To be credited to his capital account)

1. Credit Balance of his capital.
2. Credit Balance of his current account (if any)
3. Share of Goodwill.
4. Share of Reserves or Undistributed profits.
5. His share in the profit revaluation of assets and liabilities.
6. Share in profits upto the date of Retirement/Death.
7. Interest on capital if involved.
8. Salary if any

Deduction from the above sum (to be debited to the capital account)

1. Debit balance of his current account (if any)
2. Share of Goodwill to be written off.
3. Share of Accumulated loss.
4. Drawings and interest on drawings (if any)
5. Share of loss on account of Revaluation of assets and liabilities.
6. His share of business loss.

Accounting Treatment

1. Calculation of new profit sharing ration and gaining ratio
2. Treatment of goodwill.
3. Revaluation a/c preparation with the adjustment in the respect of unrecorded assets/liabilities.
4. Distribution of reserves and accumulated profits/loss.
5. Ascertainment of share of profits/loss till the date of retirement/death.
6. Adjustment of capital if required
7. Settlement of the Accounts due to Retired/Deceased partner.

New Profit Sharing Ratio & Gaining Ratio

New Profit Sharing Ratio - It is the ratio in which the remaining partners will share further profits after retirement/death.

Gaining ratio - It is the ratio in which the continuing partners have acquired the share from the outgoing partner

Calculation of the two ratios

Following situations may arise.

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1. When no information about new ratio or gaining ratio is given in the question

In this case it is considered that the share of the retiring partner is acquired by the remaining partners in the old ratio. Then no need to calculate the new ratio/gaining ratio as it will be the same as before.

Example 1 :- A Band C are partners sharing profit and loss in the ratio of 3:2:1 then on retirement of the gaining ratio/new ratio will be

A- 2:1

B- 3:1

C- 3:2

2. Gaining ratio is given which is different than the old ratio

In this case

New share of continuing partner = his old share + gained from the outgoing partner.

Example 2 : A, B & C share profits in the ratio 3:2:1. On C's death his share is taken by A & B in the ratio of 2:1 Calculate new ratio

Solution - In this case gaining ratio = 2:1 (given)

A's old share = $\frac{3}{6}$, B's old share = $\frac{2}{6}$ & C's share = $\frac{1}{6}$

A's gain = $\frac{2}{3}$ of C's share = $\frac{2}{3} \times \frac{1}{6} = \frac{2}{18}$

B's gain = $\frac{1}{3}$ of C's share = $\frac{1}{3} \times \frac{1}{6} = \frac{1}{18}$

A's new share = A's old share + A's gain

= $\frac{3}{6} + \frac{2}{18} = \frac{11}{18}$

B's new share = B's old share + B's gain

= $\frac{2}{6} + \frac{1}{18} = \frac{7}{18}$

New ratio = 11:7

3. If the new ratio is given then

Gaining ratio = New Ratio - Old Ratio

Example 3 :- A, B & C are partners in the ratio of 3:2:1 C retires & A & B decide to share future profit in the ratio of 5:3

A's Gain = $\frac{5}{8} - \frac{3}{6} = \frac{3}{24}$

B's Gain = $\frac{3}{8} - \frac{2}{6} = \frac{1}{24}$

Gaining ratio = 3:1

Distinction between the Sacrificing and Gaining Ratio

Basis	Sacrificing Ratio	Gaining Ratio
1. Meaning	It is the ratio in which the old partners surrender a part of their share of profits in favour of a new partner.	It is the ratio in which the remaining partner's acquire the outgoing partner's share of profit
2. When calculated	At the time of admission of a new partner	At the time of retirement or death of a partner.
3. Formula	Sacrificing Ratio = Old Ratio - New Ratio	Gaining Ratio = New Ratio - Old Ratio
4. Purpose	New partners share of goodwill is divided between old partners in this ratio.	Retiring or deceased partner's share of goodwill is paid by the continuing partners in this ratio

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Treatment of Goodwill

According to accounting standard - 10, Goodwill account can't be raised. Therefore only adjustment entry is done for goodwill.

Steps to be followed :-

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

Remember Old Goodwill Old Ratio

All Partners' capital A/c Dr

To Good will A/c

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

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

To Retiring/Deceased Partner's Cap A/c

Example 4 : M, N & P are partners in a firm. P retires & the goodwill of the firm is valued at Rs.30000.

M & N decide to share future profits in the ratio of 3:2. Pass necessary adjustment entries.

1. If goodwill A/c already appears in the books at Rs.18000

2. When no goodwill A/c appears in the books.

Solution :- Old ratio of M, N & P = 1:1:1 (since profit sharing ratio is not given it is treated as equal)

New ratio= 3:2

M's gain = $3/5 - 1/3 = 4/15$

N's gain = $2/5 - 1/3 = 1/15$

Gaining ratio = 4:1

P's share of goodwill = $30,000 * 1/3 = 10,000$

Case 1.

1. Old goodwill will be written off in the old ratio i.e. 1:1:1

M's Capital A/c Dr 6000

N's Capital A/c Dr 6000

P's Capital A/c Dr 6000

To Goodwill A/c 18000

2. Adjustment entry will be done in gaining ratio

M's Capital A/c Dr 8000

N's Capital A/c Dr 2000

To P's Capital A/c 10,000

Case 2. When No goodwill already appears in the books then only second entry will be done.

Hidden goodwill

Sometimes goodwill is not given in the question directly. But if a firm **agrees to pay a sum which is more than his balance in capital a/c after making all adjustment with respect to reserves, revaluation of assets and liabilities etc. then excess amount is treated as his share of goodwill (known as hidden goodwill)**

EXAMPLE 5 : Let R, S & T are partners in a firm sharing profit & loss in the ratio of 2:2:1. T Retires and his balance in capital a/c after adjustment for reserve & revaluation of assets & liabilities comes out to be Rs.50000. R & S agree to pay him Rs.60000. Give journal entry for the adjustment of goodwill.

Solution

New ratio between R & S = gaining ratio = 2:2 or 1:1

T's share of goodwill (hidden) = $Rs.60000 - 50000 = 10000$

Hence adjustment entry is

R's capital a/c Dr 5000

S's capital a/c Dr 5000

To T's capital a/c 10000

(T's share of goodwill adjusted in gaining ratio i.e. 1:1)

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3. Revaluation of Assets and Reassessment Liabilities

Revaluation A/c is prepared in the same way as in the case of admission of a new partner. Profit and loss on revaluation is transferred among all the partners in old ratio.

4. Adjustment of Reserves and Surplus (Profits)

(Appearing in the Balance Sheet- Liability Side)

(a) General Reserve A/c	Dr.
Reserve Fund A/c	Dr.
P & LA/c (Credit Balance)	Dr.

To all partners Capital/Current A/c in old ratio.

Example 6 :- X, Y and Z are partners in a firm sharing profits and losses in the ratio of 2:1:1, Y retires on 31st March, 2011. On that date, there was a balance of Rs.24,000 in general reserve and Rs.16,000 in profit and loss A/c of the firm. Give Journal entries.

Solution

General Reserve A/c	Dr 24,000	
P & LA/c	Dr 16,000	
To X's Cap A/c		20,000
To Y's Cap A/c		10,000
To Z's Cap A/c		10,000

(Reserve & Surplus amount distributed in old ratio on Y's retirement)

b) Specific Funds - If the specific funds such as workmen's compensation fund or investment fluctuation fund are in excess of actual requirement, the excess will be transferred to the Capital A/c in old ratio.

Workmen Compensation Fund A/c Dr

Investment Fluctuation Fund A/c Dr

To All Partner's Cap A/cs

Example 7 : P, Q and R are partners sharing profits and losses in the ratio of 3:2:1. R retires and on that date there was workmen's compensation fund amount Rs.30,000 in the Balance Sheet. But actual liability on this account was for Rs.12,000 only on that date. Give Journal Entry.

Solution

Excess amount in Workmen's Compensation Fund =

Rs.30,000-Rs.12,000= Rs.18,000 (Cr)

This will be transferred to all partner's Capital A/c in old ratio

Journal Entry

W. Compensation Fund A/c	Dr 18,000	
To P's Cap A/c		9000
To Q's Cap A/c		6000
To R's Cap A/c		3000

(Excess amount in W. Comp. Fund istrfd to partner's Cap A/cs in old ratio)

c) For distributing accumulated losses

(I.e. P & L A/c debit balance shown on the Asset side of Balance Sheet)

All partner's Cap/Current A/c Dr (in old ratio)

To P & L A/c

Example 8 :- A, B and C are equal partner's. A retires and on that date there was a debit balance of Rs.15,000 in P & L A/c. Give Journal entry.

Solution

A's Cap A/c Dr 5,000

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B's Cap A/c	Dr	5,000	
C's Cap A/c	Dr	5,000	
To P & L A/c			15,000

(Loss in P & L A/c written off in old ratio on A's retirement)

5. Adjustmetn of Joint Life Policy (JLP)

Introduction

JLP means the policy taken by the firm on the lives of the partners. When any of teh partners dies the insurance company pays the whole amount which makes the payment easy to deceased partner's legal representatives in case of death.

Accounting treatment in case of retirement

Case1. . When premium paid is considered as Revenue Expenditure – In this case the premium paid is debited to P&L A/c and JLP A/c doesn't appear in the balance sheet. In this case the **Retiring partner's share** in the **surrender value** of **JLP will be debited to the remaining partners Cap A/c in gaining ratio.**

I.e. Remaining Partner's Cap A/c Dr

To Retiring Partner's Cap A/c

Example 9: -D, E and F are partners in a firm sharing profit & losses in the ratio of 3:2:1. F retires on 31st March 2011. The firm had a JLP of Rs. 80,000, the surrender value of which was Rs.18,000 on that date annual premium paid on the policy of Rs.10,000 which was debited to P&L A/c every Year. Give adjustment entry if no JLP A/c appears in the Balance Sheet.

Solution

F's share in the surrender value = $1/6 * 18000 = \text{Rs.}3000$

Gaining Ratio b/w D: E=3:2

Adjustment Entry

D's Cap A/c Dr1800

E's Cap A/c Dr1200

To F's Cap A/c 3000

(F's share in the surrender value of JLP adjusted in gaining ratio)

Case2. . When premium paid is considered as Capital Expenditure- In this case the JLP A/c will be

already appearing in the Balance Sheet at surrender value. Then no further treatment is required because it

means that the retiring partners share is already included in his Cap A/c.

Disposal of the Amount Due to the Retiring Partner

The outgoing partners A/c is settled as per the terms of partnership deed. Three cases maybe there as given below-

1. When the retiring partner is paid full amount either in cash or by cheque.

Retiring Partner's Cap A/c

Dr

To Cash or Bank A/c

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2. When the retiring partner is paid nothing in cash then the whole amount due is trfd to his loan

A/c.

Retiring Partner's Cap A/c Dr

To retiring partner's Loan A/c

3. When Retiring Partner is partly paid in cash and the remaining amount is treated as Loan.

Retiring Partner's Cap A/c Dr (Total Amount due)

To Cash/Bank A/c (Amount Paid)

To Retiring Partner's Loan A/c(Amount of Loan)

Settlement of Loan of the Retiring Partner

Loan of the retiring partner is disposed off according to the pre decided terms and conditions among the partners. Normally the Principal amount is paid in **few equal installments**. In such cases **interest is credited to the Loan A/c on the basis of the amount outstanding at the beginning of each year** and the amount paid is debited to loan A/c. The following Journal entries are done

a) For interest on Loan.

Interest A/c Dr

To Retiring partner's Loan A/c

b) For the payment of installment.

Retiring Partner's Loan A/c Dr

To Cash/ Bank A/c

Example 10: -A, B, and C are partners in a firm. B retires from the firm on 1st Jan 2008. On the date of his retirement Rs.66, 000 were due to him. It was decided that the payment will be done in 3 equal yearly installments together with interest @ 10%p.a. on the unpaid balance. Prepare B's Loan A/c.

B's Loan A/c

Date	Particulars	LF	Amt.(₹)	Date	Particulars	L	Amt (₹)
2008				2008	B's Cap A/c	F	66,000
Dec 31	Bank A/c (22,000+6600)		28,600	Jan 1			
"	Balance c/d		44,000	Dec31	Interest A/c		6,600
2009			<u>72,600</u>		(10% of 66,000)		<u>(72,600)</u>
Dec 31	Bank A/c		26,400	2009	Balance b/d		44,000
"	Balance c/d		22,000	Jan 1			
			<u>48,400</u>	Dec 31	Interest A/c (10% of 44,000)		4,400
2010				2010			<u>48,400</u>
Dec 31	Bank A/c (Final Payment)		24,200	Jan 1	Balance b/d		22,000
			<u>24,200</u>	Dec 31	Interest A/c (10% of 22,000)		2,200
							<u>24,200</u>

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Adjustment of Capitals

At the time of retirement /death, the remaining partners may decide to **adjust their capitals** in their **new profit sharing Ratio**. Then

- **The sum of their capitals will be treated as the total capital of the new firm which will be divided in their New Profit Sharing Ratio.**
- **Excess or Deficiency of capital in the individual capital A/c is calculated.**
- **Such excess or shortage is adjusted by withdrawal or contribution in cash or transferring to their current A/cs.**

JOURNAL ENTRIES

a) For excess Capital withdrawn by the Partners

Partner's capital A/c Dr
 To Cash/Bank A/c

b) For deficiency, cash will be brought in by the partner

Cash/Bank A/c Dr
 To Partner's Cap A/c

Example 11:-X, Y and Z are partners in a firm sharing profits in the ratio of 2:2:1. X retires and after all adjustments the Capital A/cs of the Y and Z have a balance of ₹ 70,000 and ₹ 50, 000 respectively. They decided to adjust their capitals in new profit sharing ratio by withdrawing or bringing cash. Give necessary Journal entries and show your working clearly.

Solution

The capital of the new firm

= Total capital of Y and Z after adjustments

= ₹ 70, 000+50, 000

= ₹ 1,20,000

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	Y	Z
New Capital based on New Ratio i.e. 2:1 (total being 1,20,000)	80,000	40,000
Existing capital after adjustments	70,000	50,000
Cash is being brought in or paid off	10,000 (brought in)	10,000 (to be paid)

Journal Entries

	Dr. (₹)	Cr. (₹)
1. Bank A/c Dr To Y's Cap A/c (Amount to be brought in by Y)	10,000	10,000
2. Z's Cap A/c Dr (Amount to be withdrawn by Z)	10,000	10,000

Problem : (Preparation of balance sheet of the reconstituted firm) Vijay, Vivek and Vinay were partners in a firm sharing profits in 2:2:1 ratio. On 31.03.2006 Vivek retired from the firm. On the date of Vivek's retirement the balance sheet of the firm was as follows :

Balance Sheet of Vijay, Vivek and Vinay

As at 31.03.2006

Liabilities	Amount (₹)	Assets	Amount (₹)
Creditors	54,000	Bank	55,200
Bills Payable	24,000	Debtors 12,000	
Outstanding Rent	4,400	Less : Provision for	
Provision for Legal	12,000	doubtful debts 800	11,200
Claims		Stock	18,000
Capitals :		Furniture	8,000
Vijay 92,000		Premises	1,94,000
Vivek 60,000			
Vinay 40,000	1,92,000		
	2,86,400		2,86,400

On Vivek's retirement it was agreed that:

- i. Premises will be appreciated by 5% and furniture will be appreciated by ₹ 2,000. Stock will be depreciated by 10%.
- ii. Provision for bad debts was to be made at 5% on debtors and provision for legal damages to be made for ₹ 14,400.
- iii. Goodwill of the firm is valued at ₹ 48,000.
- iv. ₹ 50,000 from Vivek's Capital A/C will be transferred to his loan A/c and the balance will be paid by cheque.

Prepare revaluation a/c, partners Capital A/cs And Balance Sheet of Vijay and Vinay after Vivek's retirement.

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Solution :-

Revaluation Account

Dr.			Cr.
Particulars	Amount (₹)	Assets	Amount (₹)
To Stock	1,800	By Premises	9,700
To Provision for legal Claim	2,400	By Furniture	2,000
To profit Transferred		By Provision For doubtful debts	
Vijay 3,080			
Vivek 3,080			
Vinay 1,540			
	7,700		
	11,900		11,900

Capital Accounts

Dr.							Cr.
Particulars	Piyush	Pooja	Praveen	Particulars	Piyush	Pooja	Praveen
To Vivek's Capital	12,800	-	6,400	By Balance b/d	92,000	60,000	40,000
To Vivek's Loan	-	50,000	-	By revaluation A/c	3,080	3,080	1,540
To Bank	-	32,280	-	By Vijay's Capital	-	12,800	-
To Balance	82,280	-	35,140	By Vinay's c/d Capital	-	6,400	-
	95,080	82,280	41,540		95,080	82,280	41,540

Balance Sheet

As at 31st March 2006

Liabilities	Amount (₹)	Assets	Amount (₹)
Creditors	54,400	Bank	22,920
Bills payable	24,000	Debtors	11,400
Outstanding Rent	4,400	12,000	
Provision for legal claims	14,400	Less provision	16,200
Vivek's Loan	50,000	<u>600</u>	10,000
Vijay's Capital	82,280	Stock	2,03,700
Vinay's Capital	35,140	Furniture	
		Premises	
	2,64,220		2,64,220

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WORKING NOTE:-

1. New provision of bad debts on debtors(5%)=5%of Rs.12,000=600
Old provision = Rs. 800 as given in the balance Sheet
Excess of Rs. 200 is profit &trfd to revaluation A/c
2. Goodwill of the firm =48,000
Vivek share =48,000*2/5=Rs.19,200
Will be given by Vijay & Vinay in Gaining Ratio i.e. 2:1
3. Vivek's total amount due on retirement= Rs. 82,280
Less amount trfd to his loan A/c = Rs. 50,000
Amount to be paid by cheque = Rs.32,280

Death of a Partner

Accounting treatment in the case of death is same as in the case of retirement except the following:-

1. The deceased partners claim is transferred to **his executor's account**.
2. Normally the **retirement** takes place at the **end of the Accounting Period** but the **death may occur at any time**. Hence the **claim of deceased partner** shall also **include his share of profit or loss, interest on capital and drawings if any from the date of the last balance sheet to the date of his death**.
3. On death of a partner, the **insurance company** pays the **entire amount of the sum assured on JLP**.

The treatment of profits and JLP will be taken up one by one as follows-

I. Calculation of Profits/Loss for the Intervening Period

It is calculated by any one of the two methods given below:-

- a) **On Time Basis**: - in this method **proportionally profit** for the time period is calculated either on the **basis of last year's profit or on the basis of average profits of last few years** and then deceased partner's share is calculated based on his share of profits.

Example 1.- A, B and C are partners sharing profits in the ratio of 3:2:1. A dies on 31st July 2011. The profits of the firm for the year ending 31st March 2011 were ₹ 42000. Calculate A's share for the period from 1st April to 31st July 2011 on the basis of last year's profits. Pass necessary journal entry also.

Solution – A's profit = Preceding year's profit x Proportionate Period x Share of A
= ₹ 42,000 x 4/12 x 3/6
= ₹ 7,000

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Journal Entry

	Dr. (Rs.)	Dr. (Rs.)
P&L Suspense A/c Dr	7,000	
To A's Capital A/c		7,000

b) On Turnover or Sales Basis- In this method the profits upto the date of death for the current year are calculated on the **basis of current year's sales upto the date of death by using the formula.**

Profits for the current year upto the date of death =

(Sales of the current year upto the date of death/total sales of last year)x Profit for the last year.

Then from this **profit the deceased partner's share of profit is calculated.**

Example2 – If in the example- 1 given above the sales for the last year are Rs.2, 10, 000 and for the current year upto 31st July are say Rs.90, 000 then Profits from 1st April to 31st July 2011

$$= (90,000/2,10,000) \times 42,000$$

$$= \text{Rs.} 18,000$$

$$\text{A's share} = \text{Rs.} 18,000 \times \frac{3}{6} = \text{Rs.} 9,000$$

Journal Entry will be

P&L Suspense A/c Dr 9,000

To A's Capital A/c 9,000

c) Life Policy- Life policies on the lives of the partners is taken by a firm to arrange money to settle the account of deceased partner. It may be of two types:-

1) Joint Life Policy- It is taken jointly by the firm **on the lives of all the partners. If any of the partners dies, the insurance company pays whole of the amount.**

2) Individual life policies- Sometimes the firm takes **individual life policies** on the lives of partners **instead of one single Joint life policy.** In this case the insurance company pays the **full sum assured** on the **life policy of the deceased partner only.**

Accounting Treatment

Case 1 – When surrender values are not appearing in the books.

a) For the amount to be received on maturity (death) of a partner.

i. Insurance Co. A/c Dr

To Life Policy A/C

(For the amount due on the death of a partner)

ii. Life Policy A/c Dr

To All Partner's Capital A/cs

(For the amount due transferred to all partners' capital A/cs in old ratio)

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b) For **deceased partners share in the surrender values** of the life policies of **surviving partners**.

Remaining Partners Capital A/c Dr

To Deceased Partner's Capital A/c

(For deceased partner's share in the surrender values of surviving partner's life policies **adjusted in gaining ratio**)

Example3 : A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1, **B dies** and on that there was a JLP for R.60, 000 for which annual premium of Rs.6, 000 was paid out of profits.

Surrender value of the policy on the date of death was Rs.12, 000. Give necessary journal entries.

Solution –

Note . Here (In case of JLP) surrender value is not important because on death of any partner, insurance company pays the full amount as on maturity i.e. Rs.60, 000.

Journal entry

1. Insurance Co. A/c Dr	60, 000	
To Joint Life Policy A/c		60,000
(Sum due on B's death)		
2. JL Policy A/c Dr	60,000	
To A's Cap A/c		30,000
To B's Cap A/c		20,000
To C's Cap A/c		10,000

(Amount transferred in all partners Capital in old ratio)

Example 4. X, Y and Z are partners in a firm sharing profits and losses in the ratio of 3:2:1, A dies and on that date there were three life policies of Rs.30, 000 on the life of A, Rs.20, 000 on life of B and Rs.10, 000 on the life of C. Surrender value of this policies on the date of death was 40%. Give journal entries on A's death if no policy A/c appears in the Balance Sheet.

Solution –

1) For A's policies

(a) Insurance Co. A/c Dr	30,000	
To Life Policy A/c		30,000
(Amount due on A's Policy on A's Death)		
(b)Life Policy A/c Dr	30, 000	
To A's Cap A/c		15,000

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To B's Cap A/c	10,000
To C's Cap A/c	5,000

(Amount transferred in old ratio)

ii) For B's and C's Policies

Maturity amount of B's Policy= 20, 000

Maturity amount of C's Policy= 10, 000

Total = 30,000

Surrender Value = 40% of Rs. 30, 000

= Rs. 12, 000

A's share in the surrender value = $(\frac{3}{6}) \times 12, 000 = \text{Rs. } 6,000$

Gaining ratio between B and C = 2:1

Adjustment entry

B's capital A/c Dr 4,000

C's capital A/c Dr 2,000

To A's capital A/c 6, 000

(Adjustment of retiring partners share in surrender values of B and C's policies in gaining ratio)

Case2- when surrender values already appears in the Balance Sheet.

- For the amount to be received from the Insurance Co. on Joint Life policy or the Policy in the name of deceased partner.
 - Insurance Co. A/c Dr
To life policy A/c
(For the amount due on the death of a Partner)
 - Life policy A/c Dr (By the Amount received less surrender value)
To All Partner's Capital A/c
- No entry for the surviving partners policies.

Example 5- In the 3rd example if the surrender value of Rs. 12, 000 is shown in the Balance Sheet then following entries will be passed.

Solution -

1. Insurance Co. A/c Dr 60, 000

To JLP A/c 60,000

(Amount due on JLP on B's death)

2. J.L Policy A/c Dr 48,000

To A's Capital A/c 24,000

To B's Capital A/c 16,000

To C's Capital A/c 8,000

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(Balance in JL Policy A/c has transferred to all Partners Capital A/cs in old ratio)

Working note- J.L.Policy A/c

Amount due to Insurance Co. (Credited to JLP) =	Rs 60,000
Less Surrender value already Appearing on the debit of JLP =	Rs 12,000
Balance amount in the credit side of JLP to be transferred top all partners Cap A/cs	=Rs48, 000

Complete question generally asked for 6 marks

Problem- (Death of a partner) M, N and O were partners in a firm sharing profits and losses equally.

Their Balance Sheet on 31-12-2009 was as follows

Liabilities	Amount (₹)	Assets	Amount (₹)
Capitals : M 70,000		Plant and machinery	60,000
N 70,000		Stock	30,000
O 70,000		Sundry Debtors	95,000
General Reserve	2,10,000	Cash at Bank	40,000
Creditors	30,000	Cash in Hand	35,000
	20,000		
	2,60,000		2,60,000

N died on 14th March, 2010. According to the Partnership Deed, executors of the deceased partner are entitle to:

- (i) Balance of partner's capital A/c.
- (ii) Interest on capital @ 5% p.a.
- (iii) Share of goodwill calculated on the basis of twice the average of past three years profits.
- (iv) Share of profits from the closure of the last accounting year till the date of death on the basis of twice the average of three completed year's profits before death.

Profits for 2007, 2008 and 2009 were Rs. 80, 000, Rs. 90,000, Rs 1, 00,000 respectively. Show the working for deceased partner's share of goodwill and profits till the date of his death. Pass the necessary journal entries and prepare N's Capital A/c to be renderer to his executors.

(CBSE 2011, Delhi)

Solution

Date	Particulars	L.F.	Debit ₹	Credit ₹
2010 14th March	General Reserve A/c Dr To N's Capital A/c (Being transfer of N's share of general reserve of his Capital A/c)		10,000	10,000

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Interest on Capital A/c Dr To N's Capital A/c (Being interest 5% p. a. credited to N's Capital A/c upto 14/03/2010)		700	
M's Capital A/c Dr O's Capital A/c Dr To N's Capital A/c (Being goodwill adjusted in gaining ratio i.e. 1:1)		30,000 30,000	60,000
Profit and Loss Suspense A/c Dr To N's Capital A/c (Being the transfer to N's share of profit to his capital A/c)		12,000	12,000
N's Capital A/c Dr To N's Executor A/c (Being the transfer of amount due to N's executor A/c)		1,52,700	1,52,700

N's Capital A/c

Particulars	Rs.	Particulars	Rs.
To N's Executors A/c	1,52,700	By Balance b/d	70,000
		By General Reserve A/c	10,000
		By Interest on Capital A/c (70,000 * 5/100 * 73/365)	700
		By M's Capital A/c	30,000
		By O's Capital A/c	30,000
		By Profit & Loss Suspense A/c (90,000 * 2 * 73/365 * 1/3)	12,000
	1,52,700		1,52,700

Working Note:

1) Calculation of Goodwill

Average profit for 3 years = $(Rs. 80,000 + 90,000 + 1,00,000) / 3$
 = 90,000

Goodwill of the firm = Average Profit * No. Of Year of Purchase = $90,000 * 2 = Rs. 1,80,000$

Total N's Share in Goodwill = $1,80,000 * 1/3 = 60,000$

2) Time from the date of last balance Sheet (31st December, 2009) to the date of death (14th March, 2010)

= 31 days of January + 28 days of Feb (2010 is not a leap year) + 14 days of March

= 73 days