Chapter - 4 Part – A
Retirement or Death of a partner

Retirement of a partner means ceasing to be partner of the firm. A partner may retire (i) of there is agreement of this effect (ii) all partners give consent (iii) At will by giving written notice.

Introduction

Like admission and changes in profit sharing ratio in case of retirement or death also the existing partnership deep comes to end and the new once comes into exist- tense among the remaining partner. 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 Blanca of his capital.

2. Credit Balance of his current account (if any).

3. Share of Goodwill. (By gaining partners)

4. Share of Reserves of Undistributed profits.

5. His share in the profit on revaluation of assets and liabilities.

6. Share in profits up to the date of Retirement/Death. (By p & L suspense A/c)

7. Interest on capital if involved.

8. Salary if any

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

1. Debit balance of his current account (if any)

2. Share of existing Goodwill to be written off.

3. share of accumulated loss.

4. Drawing and interest on drawings (if any)

5. Share of loss on account of Revaluation of assets and liabilities.

6. His share of business loss up to the date of Retirement/Death (To p & L) suspense A/C)

Accounting Treatment

1. Calculation of new profit sharing ratio and gaining ratio

2. Treatment of goodwill.

3. Evaluation 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 profit/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 share future profits after retirement/death.

Gaining ratio: it is the ratio in which the continuing partners have acquired the share from the outgoing partner. Gaining Ratio = New Ratio -Old Ratio.

Calculation of the two ratios.

Following situations may arise

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

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

2. Gaining ratio is given which is different than the old ratio in this New share of continuing partner = has old share + gained from outgoing partner.

3. if the new ratio is given the Gaining ratio = New Ratio -Old Ratio

TREATMENT OF GOOD WILL

According to accounting standards – 10, Good will account can't be raised as only purchased goodwill is recorded in books. Therefore only adjustment entry is done for goodwill

Steps to be followed

1. When old good will appears in the books then first of all this is writer in the old ratio**. Remember Old Good will old Ratio**

All Partner's capital A/C   Dr.

To Good Will A/c

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

Remaining Partner's Capital, A/C Dr. (in gaining

To Retiring/Deceased Partner's Capital A/c

Hidden Goodwill

Sometimes goodwill is not given in the question directly, But if a firm agrees to pay a sum which is more than retiring partner's balance in capital also after making all adjustment with respect to resaves, revaluation of assets and liabilities etc. then cases amount is treated as his share of goodwill (known as hidden goodwill).

3. Revaluation of Assets and Reassessment of 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 Reservation and Surplus (Profits)

(Appearing in the Balance Sheet – Liability Side)

(a) General Reserve A/cDr.

Reserve Fund A/cDr.

Profit & Loss A/c (Credit Balance)Dr.

To all partners Capital/Current A/c (in old ratio)

(b) Specific Funds – If the specific funds such as workmen's compensation funds 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/cDr.

Investment Fluctuation Funds A/cDr.

To All Partner's Capital A/cs

(c) For distributing accumulated losses

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

All partner's Capital/Current A/cDr. (in old ratio)

To P & L A/c

Disposal of the Amount Due to the Retiring Partner

This outgoing partners A/c is settled as per the terms of partnership deed. Three cases may be there as given below –

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

Retiring Partner's Capital A/cDr.

To Cash Bank A/c

2. When the retiring partner is paid nothing in cash then the whole amount due is transferred to his loan A/c

Retiring Partner’s Capital A/cDr.

To retiring partner’s Loon A/c

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

Retiring Partner’s Capital A/cDr. (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 accordingly of the pre decided term 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 basic of the amount outstanding at the beginning of each year** and the amount paid it debited to loan A/c. The following Journal entries are done

a. For interest on Loan.

Interest A/cDr.

To Retiring partner’s Loan A/c

b. For the payment of installment.

Retiring Partner’s Loan A/cDr.

To Cash/Bank A/c (including interest)

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 of Deficiency of capital in the individual capital A/c is calculated.

· Such excess or shortage is adjusted by withdrawal or contribution in case or transferring to their current A/cs.

Journal Entries

(a) For excess Capital withdrawn by the Partners

Partner's capital A/cDr.

To Cash/Bank A/c

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

Cash/Bank A/cDr.

To Partner's capital A/c

DEATH OF A PARTNER

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

1. The deceased partners claim is transferred to **his executer's account.**

2. Normally the **retirement** takes place at the **end of the Accounting pried** but the **death** may **occur at any time.** Hence the **claim of deceased part** shall also **include his share or profit or loss, interest on capital drawings if any from the date of the last balance sheet to the date his death.**

1. Calculation of profit/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 basis of average profits of last few years**

and then deceased profit share is calculated based on his share of profits.

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) × Profit for the last year.

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