UNIT 5

ADMISSION OF A PARTNER

Contents

Points to recall

The following points are to be recalled before learning admission of a partner:

- Meaning and features of partnership firm
- Partnership deed
- Partners' capital accounts
- Valuation of goodwill

Learning objectives

To enable the students to

- Understand the accounting treatment at the time of admission of a partner
- Prepare revaluation account, capital accounts and balance sheet of the firm after admission of a partner.

Key terms to know

- Admission of a partner
- Sacrificing ratio
- Revaluation account

5.1 Introduction

Student activity 5.1

Assume you are a partner in a firm. You are going to admit a new partner into your firm. Think of any five agreements that you may want to include in your partnership deed.

A person may join as a new partner in an existing partnership firm. This is called admission of a partner. The purpose of admission of a new partner may be to raise additional capital for expansion of business or managerial skill of the new partner or both. Generally, the new partner has to contribute capital to the firm and thereby he / she acquires the right to share the future profits and the assets of the firm.

On admission of a new partner, the firm is reconstituted with a new agreement and the existing agreement comes to an end.

According to Section 31(1) of the Indian Partnership Act, 1932, subject to contract between the partners no person shall be introduced as a partner into a firm without the consent of all the existing partners.

5.2 Adjustments required at the time of admission of a partner

On admission, the new partner may bring capital in cash or in kind or both. The following journal entry is passed to record the capital brought in.

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Cash or Bank A/c	Dr.		xxx	
	Assets A/c	Dr.		xxx	
	To Partner's capital A/c				xxx

On the admission of a partner, generally there is a change in the mutual rights of the partners. The new partner becomes liable for all the acts which are carried out by the firm from the date of his / her admission into the firm. Hence, the accumulated profits, losses and reserves before admission are to be distributed to the existing partners. Similarly, assets and liabilities are to be revalued and the profit or loss on revaluation is to be distributed to the existing partners. The following adjustments are necessary at the time of admission of a partner:

1. Distribution of accumulated profits, reserves and losses
2. Revaluation of assets and liabilities
3. Determination of new profit-sharing ratio and sacrificing ratio
4. Adjustment for goodwill
5. Adjustment of capital on the basis of new profit sharing ratio (if so agreed)

5.3 Distribution of accumulated profits, reserves and losses

Profits and losses of previous years which are not distributed to the partners are called accumulated profits and losses. Any reserve and accumulated profits and losses belong to the old partners and hence these should be distributed to the old partners in the old profit sharing ratio. Reserves include general reserve, reserve fund, workmen compensation fund and investment fluctuation fund. Incase of workmen compensation fund, the excess amount after providing for anticipated claim is the accumulated profit to be transferred.

Following are the journal entries to be passed:

(a) For transferring accumulated profit and reserves

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Profit and loss appropriation A/c	Dr.		xxx	
	General reserve A/c	Dr.		xxx	
	Reserve fund A/c	Dr.		xxx	
	Workmen compensation fund A/c	Dr.		xxx	
	Investment fluctuation fund A/c	Dr.		xxx	
	To Old partners' capital / current A/c (in the old ratio)				xxx

(b) For transferring accumulated loss

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Old partner's capital / current A/c	Dr.		xxx	
	ToProfit and loss A/c (in old ratio)				xxx

Investment fluctuation fund

Investment fluctuation fund is created out of profit to adjust the reduction in the market value of the investments. If the market value of the investments is greater than or equal to the book value, then, the entire investment fluctuation fund is transferred to the old partners' capital account in old profit sharing ratio. If the market value of the investments is less than the book value, then the difference is to be subtracted from the investment fluctuation fund and the balance of investment fluctuation fund is to be transferred to the old partners' capital account in old profit sharing ratio.

Illustration 1

Mala and Vimala were partners sharing profits and losses in the ratio of 3:2. On 31.3.2017, Varshini was admitted as a partner. On the date of admission, the book of the firm showed a reserve fund of ₹ 50,000. Pass the journal entry to distribute the reserve fund.

Solution

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
2017 March 31	Reserve fund A/c	Dr.		50,000	
	To Mala's capital A/c (50,000 x 3/5)				30,000
	To Vimala's capital A/c (50,000 x 2/5)				20,000
	(Reserve fund transferred to old partners' capital account in the old profit sharing ratio)				

Illustration 2

Kavitha and Radha are partners of a firm sharing profits and losses in the ratio of 4:3. They admit Deepa on 1.1.2019. On that date, their balance sheet showed debit balance of profit and loss account being accumulated loss of ₹ 70,000 on the asset side of the balance sheet. Give the journal entry to transfer the accumulated loss on admission.

Solution

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
2019	Kavitha's capital A/c	Dr.		40,000	
January 1	Radha's capital A/c	Dr.		30,000	
	To Profit and loss a/c				70,000
	(Accumulated loss transferred to old partners' capital account in the old profit sharing ratio)				

Illustration 3

Rathna Kumar and Arockia Das are partners in a firm sharing profits and losses in the ratio of 3:2. Their balance sheet as on 31st March, 2017 is as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Buildings	30,000
Rathna Kumar	30,000		Plant	60,000
Arockia Das	50,000	80,000	Furniture	20,000
Profit and loss appropriation A/c		20,000	Debtors	10,000
General reserve		5,000	Stock	15,000
Workmen compensation fund		15,000	Cash at bank	15,000
Sundry creditors		30,000		
		1,50,000		1,50,000

David was admitted into the partnership on 1.4.2017. Pass journal entry to distribute the accumulated profits and reserve on admission.

Solution

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
2017	Profit and loss appropriation A/c	Dr.		20,000	
April 1	General reserve A/c	Dr.		5,000	
	Workmen compensation fund A/c	Dr.		15,000	
	To Rathna Kumar's capital A/c (40,000 x 3/5)				24,000
	To Arockia Das's capital A/c (40,000 x 2/5)				16,000
	(Accumulated profit and reserve transferred to old partners' capital account in the old profit sharing ratio)				

5.4 Revaluation of assets and liabilities

When a partner is admitted into the partnership, the assets and liabilities are revalued as the current value may differ from the book value. Determination of current values of assets and liabilities is called revaluation of assets and liabilities. The reasons for revaluation of assets and liabilities are as follows:

(i) To give a true and fair view of the state of affairs of the firm and

(ii) To share the gain arising from the revaluation of assets and liabilities as it is due to the old partners.

There are two ways in which the revaluation of assets and liabilities may be dealt with in the accounts.

(a) Revised value of assets and liabilities are shown in the books

(b) Revised value of assets and liabilities are not shown in the books

5.4.1 When revised value of assets and liabilities are shown in the books

Under this method, the assets and liabilities are shown at their revised values in the books and in the balance sheet which is prepared immediately after the admission of a partner. A Revaluation account is opened to record the increase or decrease in assets and liabilities. Revaluation account is also called Profit and loss adjustment account. It is a nominal account. Revaluation account is credited with increase in value of assets and decrease in the value of liabilities. It is debited with decrease in value of assets and increase in the value of liabilities. Unrecorded assets if any are credited and unrecorded liabilities if any are debited to the revaluation account. The profit or loss arising therefrom is transferred to the capital accounts of the old partners in the old profit sharing ratio. If the total of the credit side of the revaluation account exceeds the total of the debit side, the difference is profit on revaluation. If the total of the debit side of the revaluation account exceeds the total of the credit side, the difference is loss on revaluation.

Following are the journal entries to be passed to record the revaluation of assets and liabilities:

Date	Particulars	L.F.	Debit ₹	Credit ₹
	1. For increase in the value of asset			
	Concerned asset A/c Dr.		xxx	
	To Revaluation A/c			xxx
	2. For decrease in the value of asset			
	Revaluation A/c Dr.		xxx	
	To Concerned asset A/c			xxx
	3. For increase in the amount of liabilities			
	Revaluation A/c Dr.		xxx	
	To Concerned liability A/c			xxx
	4. For decrease in the amount of liability			
	Concerned liability A/c Dr.		xxx	
	To Revaluation A/c			xxx
	5. For recording an unrecorded asset			
	Concerned asset A/c Dr.		xxx	
	To Revaluation A/c			xxx
	6. For recording an unrecorded liability			
	Revaluation A/c Dr.		xxx	
	To Concerned liability A/c			xxx
	7. For transferring the balance in revaluation A/c			
	(a) If there is profit on revaluation			
	Revaluation A/c Dr.		xxx	
	To Old partners' capital A/c (individually in old ratio)			xxx
	(b) If there is loss on revaluation			
	Old partners' capital A/c (individually in old ratio) Dr.		xxx	
	To Revaluation A/c			xxx

Format of Revaluation Account:

Dr. **Revaluation Account** **Cr.**

Particulars	₹	Particulars	₹
To Concerned asset A/c (net decrease)	xxx	By Concerned asset A/c (net increase)	xxx
To Concerned liability A/c (net increase)	xxx	By Concerned liability A/c (net decrease)	xxx
To Old partners' capital A/c (profit on revaluation shared in old ratio)*	xxx	By Old partners' capital A/c (loss on revaluation shared in old ratio)*	xxx
	xxx		xxx

*There will be either profit or loss on revaluation.

Illustration 4

Rajesh and Ramesh are partners sharing profits in the ratio 3:2. Raman is admitted as a new partner and the new profit sharing ratio is decided as 5:3:2. The following revaluations are made. Pass journal entries and prepare revaluation account.

(a) The value of building is increased by ₹ 15,000.

(b) The value of the machinery is decreased by ₹ 4,000.

(c) Provision for doubtful debt is made for ₹ 1,000.

Solution

Journal entries

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Buildings A/c Dr.		15,000	
	To Revaluation A/c			15,000
	(Appreciation in value of buildings recorded)			
	Revaluation A/c Dr.		5, 000	
	To Machinery A/c			4,000
	To Provision for doubtful debts A/c			1,000
	(Decrease in assets recorded and provision made)			
	Revaluation A/c Dr.		10,000	
	To Rajesh's capital A/c			6,000
	To Ramesh's capital A/c			4,000
	(Profit on revaluation transferred)			

Dr. Revaluation Account Cr.

Particulars	₹	₹	Particulars	₹
To Machinery A/c		4,000	By Buildings A/c	15,000
To Provision for doubtful debts A/c		1,000		
To Profit on revaluation transferred to				
Rajesh's capital A/c (3/5)	6,000			
Ramesh's capital A/c (2/5)	4,000	**10,000**		
		15,000		15,000

Illustration 5

Sriram and Raj are partners sharing profits and losses in the ratio of 2:1. Nelson joins as a partner on 1st April 2017. The following adjustments are to be made:

(i) Increase the value of stock by ₹ 5,000

(ii) Bring into record investment of ₹ 7,000 which had not been recorded in the books of the firm.

(iii) Reduce the value of office equipment by ₹ 10,000

(iv) A provision would also be made for outstanding wages for ₹ 9,500.

Give journal entries and prepare revaluation account.

Solution

Journal entries

Date	Particulars		L.F.	Debit ₹	Credit ₹
2017	Stock A/c	Dr.		5,000	
April 1	Investment A/c	Dr.		7,000	
	To Revaluation A/c				12,000
	(Increase in the value of stock and unrecorded investment accounted)				
,,	Revaluation A/c	Dr.		19,500	
	To Office equipment A/c				10,000
	To Outstanding wages A/c				9,500
	(Reduction in the value of office equipment and provision of outstanding wages recorded)				
,,	Sriram's capital A/c	Dr.		5,000	
	Raj's capital A/c	Dr.		2,500	
	To Revaluation A/c				7,500
	(Loss on revaluation transferred)				

Dr. **Revaluation Account** **Cr.**

Particulars	₹	Particulars	₹	₹
To Office equipment A/c	10,000	By Stock A/c		5,000
To Outstanding wages A/c	9,500	By Investment A/c		7,000
		By Loss on revaluation transferred to		
		Sriram's capital A/c (2/3)	5,000	
		Raj's capital A/c (1/3)	2,500	**7,500**
	19,500			19,500

Illustration 6

Raghu and Sam are partners in a firm sharing profits and losses in the ratio of 3:2. Their balance sheet as on 31st March, 2017 is as follows:

Liabilities	₹	₹	Assets	₹	₹
Capital accounts:			Machinery		30,000
Raghu	40,000		Furniture		10,000
Sam	30,000	70,000	Stock		10,000
Sundry creditors		30,000	Debtors	21,000	
			Less: Provision for		
			doubtful debts	1,000	20,000
			Bank		30,000
		1,00,000			1,00,000

Prakash is admitted on 1.4.2017 subject to the following conditions:

(a) He has to bring a capital of ₹ 10,000

(b) Machinery is valued at ₹ 24,000

(c) Furniture to be depreciated by ₹ 3,000

(d) Provision for doubtful debts should be increased to ₹ 3,000

(e) Unrecorded trade receivables of ₹ 1,000 would be brought into books now

Pass necessary journal entries and prepare revaluation account and capital account of partners after admission.

Solution

Journal entries

Date	Particulars	L.F.	Debit ₹	Credit ₹
2017	Bank A/c Dr.		10,000	
April 1	To Prakash's capital A.c			10,000
	(Capital brought by Prakash)			
,,	Revaluation A/c Dr.		11,000	
	To Machinery A/c			6,000
	To Furniture A/c			3,000
	To Provision for doubtful debts A/c			2,000
	(Depreciation on machinery and furniture and provision made for doubtful debts adjusted)			

,,	Trade receivables A/c To Revaluation A/c (Unrecorded trade receivables recorded)		1,000	 1,000
,,	Raghu's capital A/c Sam's capital A/c Dr. To Revaluation A/c (Loss on revaluation transferred to capital accounts)		6,000 4,000	 10,000

Dr. **Revaluation Account** **Cr.**

Particulars	₹	Particulars	₹	₹
To Machinery	6,000	By Trade receivables A/c		1,000
To Furniture	3,000	By Loss on revaluation transferred to		
To Provision for bad debts	2,000	Raghu's capital A/c (3/5)	6,000	
		Sam's capital A/c (2/5)	4,000	**10,000**
	11,000			11,000

Dr. **Capital Account** **Cr.**

Date	Particulars	Ragu ₹	Sam ₹	Prakash ₹	Date	Particulars	Ragu ₹	Sam ₹	Prakash ₹
	To Revaluation A/c	6,000	4,000	-		By Balance b/d	40,000	30,000	-
	To Balance c/d	**34,000**	**26,000**	**10,000**		By Bank	-	-	10,000
		40,000	30,000	10,000			40,000	30,000	10,000
						By Balance b/d	34,000	26,000	10,000

Illustration 7

Anand and Balu are partners in a firm sharing profits and losses in the ratio of 7:3. Their balance sheet as on 31st March, 2018 is as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Land	60,000
Anand	50,000		Stock	40,000
Balu	30,000	80,000	Debtors	20,000
Sundry creditors		20,000	Cash in hand	10,000
Profit and loss A/c		30,000		
		1,30,000		1,30,000

Chandru is admitted as a new partner on 1.4.2018 by introducing a capital of ₹ 20,000 for 1/4 share in the future profit subject to the following adjustments:

(a) Stock to be depreciated by ₹ 3,000

(b) Provision for doubtful debts to be created for ₹ 2,000.

(c) Land was to be appreciated by ₹ 10,000

Prepare revaluation account and capital account of partners after admission.

Solution

Dr. **Revaluation Account** **Cr.**

Particulars	₹	₹	Particulars	₹
To Stock		3,000	By Land A/c	10,000
To Provision for doubtful debts		2,000		
To Profit on revaluation transferred to				
Anand's capital A/c (7/10)	3,500			
Balu's capital A/c (3/10)	1,500	**5,000**		
		10,000		10,000

Dr. **Capital Account** **Cr.**

Particulars	Anand ₹	Balu ₹	Chandru ₹	Particulars	Anand ₹	Balu ₹	Chandru ₹
To Balance c/d	**74,500**	**40,500**	**20,000**	By Balance b/d	50,000	30,000	-
				By Bank A/c	-	-	20,000
				By Revaluation A/c	3,500	1,500	-
				By Profit and loss A/c	21,000	9,000	-
	74,500	40,500	20,000		74,500	40,500	20,000
				By Balance b/d	74,500	40,500	20,000

Student activity 5.2

Whole class game: Change your position

One student says a transaction. If that transaction has the effect of revaluation gain, other students should stand up and vice versa.

Examples: When one student says depreciation of buildings, others should sit down.

When one student says furniture revaluation upwards, others should stand up.

It can also be played in groups or pairs.

5.4.2 When revised values of assets and liabilities are not shown in the books

Under this method, the assets and liabilities are shown at their original values and not at the revised values in the books and in the balance sheet which is prepared immediately after the admission of a partner. The net result of revaluation is adjusted through the capital accounts of the partners. A Memorandum revaluation account which is a temporary account is opened when the revised values are not to be shown in the books of accounts.

5.5 New profit sharing ratio and sacrificing ratio

5.5.1 New profit sharing ratio

It is necessary to determine the new profit sharing ratio at the time of admission of a partner because the new partner is entitled to share the future profits of the firm. New profit sharing ratio is the agreed proportion in which future profit will be distributed to all the partners including the new partner. If the new profit sharing ratio is not agreed, the partners will share the profits and losses equally.

5.5.2 Sacrificing ratio

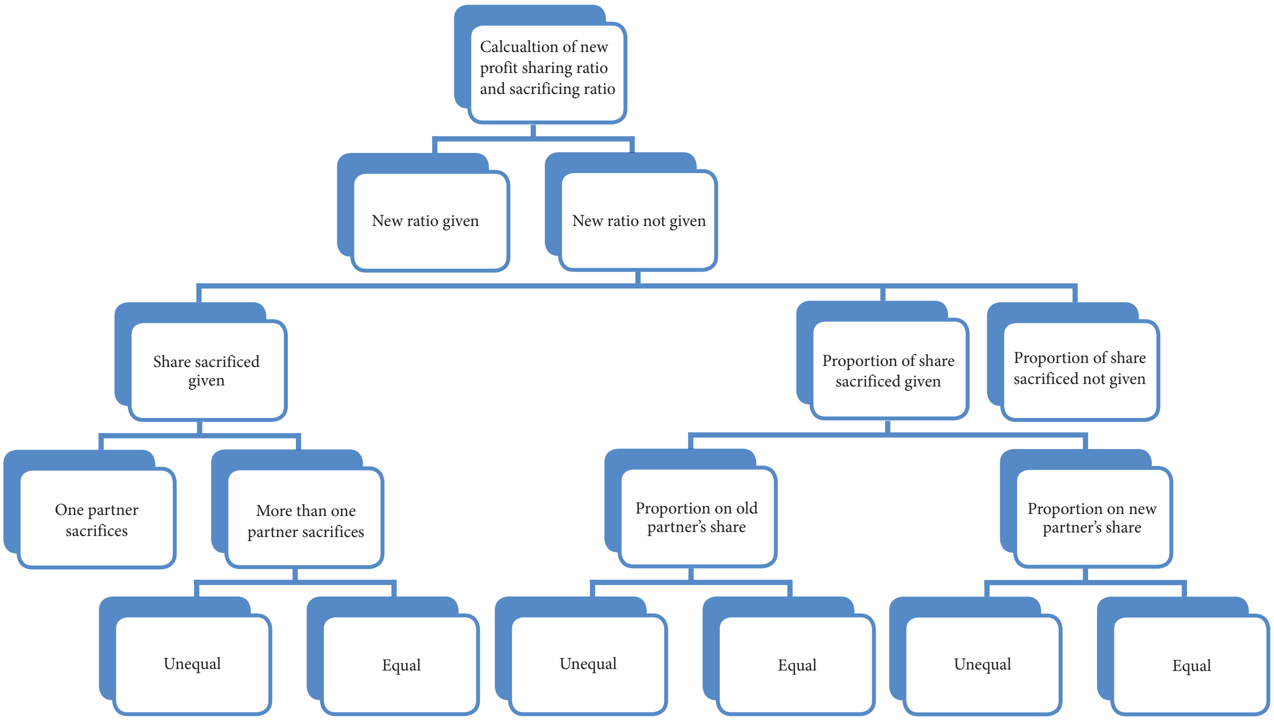
The old partners may sacrifice a portion of the share of profit to the new partner. The sacrifice may be made by all the partners or some of the partners. Sacrificing ratio is the proportion of the profit which is sacrificed or foregone by the old partners in favour of the new partner. The purpose of finding the sacrificing ratio is to share the goodwill brought in by the new partner. The share sacrificed is calculated by deducting the new share from the old share.

Share sacrificed = Old share - New share

Sacrificing ratio = Ratio of share sacrificed by the old partners

Share of the new partner is the sum of shares sacrificed by the old partners.

Tutorial note: When the new profit sharing ratio is not given in the problem, it is to be calculated based on the information given in the problem.



DO YOU KNOW?

Sometimes an existing partner may also gain in share of profit on admission of a partner when the new share is greater than the old share. In this case, the gaining partner has to compensate the sacrificing partners to the extent of his share in the total goodwill of the firm.

Calculation of sacrificing ratio and new profit sharing ratio under different situations

1. When new profit sharing ratio is given

When new profit sharing ratio is given, sacrificing ratio has to be calculated as follows:

Sacrificing ratio = Ratio of share sacrificed by the old partners

Share sacrificed = Old share - New share

Illustration 8

Anbu and Raju are partners, sharing profits in the ratio of 3:2. Akshai is admitted as a partner. The new profit sharing ratio among Anbu, Raju and Akshai is 5:3:2. Find out the sacrificing ratio.

Solution

Old ratio of Anbu and Raju $= 3:2$ that is, $\frac{3}{5}:\frac{2}{5}$

New ratio of Anbu, Raju and Akshai $= 5:3:2$ that is, $\frac{5}{10}:\frac{3}{10}:\frac{2}{10}$

Share sacrificed = Old share - New share

Anbu $= \frac{3}{5}-\frac{5}{10}=\frac{6-5}{10}=\frac{1}{10}$

Raju $= \frac{2}{5}-\frac{3}{10}=\frac{4-3}{10}=\frac{1}{10}$

Sacrificing ratio of Anbu and Raju is $\frac{1}{10}:\frac{1}{10}$ that is 1:1

2. When new profit sharing ratio is not given

(a) When share sacrificed is given

When new profit sharing ratio is not given, but the share sacrificed by the old partner(s) is given, new profit sharing ratio is calculated as follows:

New share of old partner	= Old share - Share sacrificed
Share of new partner	= Sum of shares sacrificed by old partners

Illustration 9

Hari and Saleem are partners sharing profits and losses in the ratio of 5:3. They admit Joel for 1/8 share, which he acquires entirely from Hari. Find out the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Share sacrificed by old partners

Hari $= \frac{1}{8}$

Saleem $= 0$

Sacrificing ratio $= 1:0$

Old ratio of Hari and Saleem is 5:3 that is $\frac{5}{8}:\frac{3}{8}$

New share of old partner = Old share - Share sacrificed

Hari $= \frac{5}{8} - \frac{1}{8} = \frac{5-1}{8} = \frac{4}{8}$

Saleem $= \frac{3}{8}$

Share of new partner

Joel $= \frac{1}{8}$

New profit sharing ratio of Hari, Saleem and Joel is $\frac{4}{8}:\frac{3}{8}:\frac{1}{8}$ that is, 4:3:1

Illustration 10

Ravi and Kumar share profits and losses in the ratio of 7:3. Christy is admitted as a new partner with 3/7 share which he acquires 2/7 from Ravi and 1/7 from Kumar. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Shares sacrificed $= \frac{2}{7}, \frac{1}{7}$

Sacrificing ratio of Ravi and Kumar is 2:1

Old profit sharing ratio $= 7:3$ or $\frac{7}{10}:\frac{3}{10}$

New share of old partners = Old share - Share sacrificed

Ravi $= \frac{7}{10} - \frac{2}{7} = \frac{49-20}{70} = \frac{29}{70}$

Kumar $= \frac{3}{10} - \frac{1}{7} = \frac{21-10}{70} = \frac{11}{70}$

Share of new partner

Christy $= \frac{3}{7}$

In order to equate the denominator of Christy's share, multiply and divide by 10

$$= \frac{3}{7} \times \frac{10}{10} = \frac{30}{70}$$

New profit sharing ratio of Ravi, Kumar and Christy = $\frac{29}{70} : \frac{11}{70} : \frac{30}{70} = 29 : 11 : 30$

Illustration 11

Hameed and Govind are partners sharing profits and losses in the ratio of 5:3. They admit John as a partner. John acquires his share 1/5 from Hameed and 1/5 from Govind. Find out the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Share sacrificed = $\frac{1}{5}, \frac{1}{5}$

Sacrificing ratio of Hameed and Govind is 1:1

Old ratio is 5:3 that is $\frac{5}{8} : \frac{3}{8}$

New share of old partner = Old share - Share sacrificed

Hameed $= \frac{5}{8} - \frac{1}{5} = \frac{25-8}{40} = \frac{17}{40}$

Govind $= \frac{3}{8} - \frac{1}{5} = \frac{15-8}{40} = \frac{7}{40}$

Share of new partner

John = Sum of shares sacrificed by old partners

$$= \frac{1}{5} + \frac{1}{5} = \frac{2}{5}$$

In order to equalise the denominator of John's share, multiply and divide by 8

John's share $= \frac{2}{5} \times \frac{8}{8} = \frac{16}{40}$

New profit sharing ratio of Hameed, Govind and John is $\frac{17}{40} : \frac{7}{40} : \frac{16}{40}$ or 17:7:16

(b) When proportion of share sacrificed is given

(i) When share sacrificed is given as a proportion on old partners' share

When new profit sharing ratio is not given, but the share sacrificed is given as a proportion on old partners' share, new profit sharing ratio is calculated as follows:

Share sacrificed by old partner	= Old share x Proportion of share sacrificed
New share of old partner	= Old share - Share sacrificed
w partner	= Sum of shares sacrificed by old partners

Illustration 12

Suresh and Dinesh are partners sharing profits in the ratio of 3:2. They admit Ramesh as a new partner. Suresh surrenders 1/5 of his share in favour of Ramesh. Dinesh surrenders 2/5 of his share in favour of Ramesh. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Old share = 3:2 that is, Suresh $\frac{3}{5}$ and Dinesh $\frac{2}{5}$

Share sacrificed = Old share x Proportion of share sacrificed

Suresh $= \frac{3}{5} \times \frac{1}{5} = \frac{3}{25}$

Dinesh $= \frac{2}{5} \times \frac{2}{5} = \frac{4}{25}$

Sacrificing ratio of Suresh and Dinesh is $\frac{3}{25}$ and $\frac{4}{25}$, that is, 3:4

New share = Old share - Share sacrificed

Suresh $= \frac{3}{5} - \frac{3}{25} = \frac{15-3}{25} = \frac{12}{25}$

Dinesh $= \frac{2}{5} - \frac{4}{25} = \frac{10-4}{25} = \frac{6}{25}$

Share of new partner = Sum of shares sacrificed by Suresh and Dinesh

Ramesh $= \frac{3}{25} + \frac{4}{25} = \frac{3+4}{25} = \frac{7}{25}$

New profit sharing ratio of Suresh, Dinesh and Ramesh = $\frac{12}{25} : \frac{6}{25} : \frac{7}{25}$ that is, 12:6:7

Illustration 13

Prasanth and Nisha are partners sharing profits and losses in the ratio of 3:2. They admit Ramya as a new partner. Prasanth surrenders 2/5 of his share and Nisha surrenders 2/5 of her share in favour of Ramya. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Old share = 3:2 that is, Prasanth $\frac{3}{5}$ and Nisha $\frac{2}{5}$

Share sacrificed = Old share × Proportion of share sacrificed

Prasanth $= \frac{3}{5} \times \frac{2}{5} = \frac{6}{25}$

Nisha $= \frac{2}{5} \times \frac{2}{5} = \frac{4}{25}$

Sacrificing ratio of Prasanth and Nisha is $\frac{6}{25}$ and $\frac{4}{25}$, that is, 3:2

New share = Old share - Share sacrificed

Prasanth $= \frac{3}{5} - \frac{6}{25} = \frac{15-6}{25} = \frac{9}{25}$

Nisha $= \frac{2}{5} - \frac{4}{25} = \frac{10-4}{25} = \frac{6}{25}$

Share of new partner = Sum of shares sacrificed by Prasanth and Nisha

Ramya $= \frac{6}{25} + \frac{4}{25} = \frac{6+4}{25} = \frac{10}{25}$

New profit sharing ratio of Prasanth, Nisha and Ramya $= \frac{9}{25} : \frac{6}{25} : \frac{10}{25}$ that is, 9:6:10

(ii) When proportion of share sacrificed on new partner's share is given

When new profit sharing ratio is not given, but the proportion of share sacrificed on new partner's share is given, new profit sharing ratio is calculated as follows:

New share of old partner	= Old share - Share sacrificed
Share sacrificed	= New partner's share × Proportion of share sacrificed

Illustration 14

Ramesh and Raju are partners sharing profits in the ratio of 2:1. They admit Ranjan into partnership with 1/4 share of profit. Ranjan acquired the share from old partners in the ratio of 3:2. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Ranjan's share $= \frac{1}{4}$

Old ratio = 2:1 that is, $\frac{2}{3} : \frac{1}{3}$

Proportion of share sacrificed = 3:2 that is, $\frac{3}{5} : \frac{2}{5}$

Share sacrificed = New partner's share × Proportion of share sacrificed

Ramesh $= \frac{1}{4} \times \frac{3}{5} = \frac{3}{20}$

Raju $= \frac{1}{4} \times \frac{2}{5} = \frac{2}{20}$

Sacrificing ratio of Ramesh and Raju is $\frac{3}{20}$ and $\frac{2}{20}$, that is, 3:2

New share of old partner = Old share - Share sacrificed

Ramesh $= \frac{2}{3} - \frac{3}{20} = \frac{40-9}{60} = \frac{31}{60}$

Raju $= \frac{1}{3} - \frac{2}{20} = \frac{20-6}{60} = \frac{14}{60}$

Share of new partner

Ranjan $= \frac{1}{4}$

In order to equate the denominator, multiply and divide Ranjan's share by 15

$$= \frac{1}{4} \times \frac{15}{15} = \frac{15}{60}$$

Thus, the new profit sharing ratio $= \frac{31}{60} : \frac{14}{60} : \frac{15}{60}$ = 31:14:15

Illustration 15

Mahesh and Dhanush are partners sharing profits and losses in the ratio of 2:1. Arun is admitted for 1/4 share which he acquired equally from both Mahesh and Dhanush. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Arun's share $= \frac{1}{4}$

Proportion of share sacrificed = 1:1(equally) i.e. $\frac{1}{2} : \frac{1}{2}$

Share sacrificed = New partner's share × Proportion of share sacrificed

Mahesh $= \frac{1}{4} \times \frac{1}{2} = \frac{1}{8}$

Dhanush $= \frac{1}{4} \times \frac{1}{2} = \frac{1}{8}$

Sacrificing ratio of Mahesh and Dhanush is $\frac{1}{8} : \frac{1}{8}$ that is, 1:1

New share of old partner = Old share - Share sacrificed

Mahesh $= \frac{2}{3} - \frac{1}{8} = \frac{16-3}{24} = \frac{13}{24}$

Dhanush $= \frac{1}{3} - \frac{1}{8} = \frac{8-3}{24} = \frac{5}{24}$

Share of new partner

Arun $= \frac{1}{4}$

In order to equate, multiply and divide Arun's share by 6

$= \frac{1}{4} \times \frac{6}{6} = \frac{6}{24}$

New profit sharing ratio of Mahesh, Dhanush and Arun $= \frac{13}{24} : \frac{5}{24} : \frac{6}{24}$ that is, 13:5:6.

(c) When share sacrificed and proportion of share sacrificed is not given

When new profit sharing ratio, share sacrificed and the proportion of share sacrificed is not given, but only the share of new partner is given, new profit sharing ratio is calculated by assuming that the share sacrificed is the proportion of old share. New profit sharing ratio is calculated as follows:

Share sacrificed	= New partner's share x Old share
New share of old partner	= Old share - Share sacrificed

Illustration 16

Vimal and Athi are partners sharing profits in the ratio of 2:1. Jeyam is admitted for 1/4 share in the profits. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Since share sacrificed, proportion of share sacrificed and new profit sharing ratio are not given, it is assumed that the existing partners sacrifice in their old profit sharing ratio, that is, 2:1.

Sacrificing ratio of Vimal and Athi is 2:1

Let the total share be 1

Jeyam's share $= \frac{1}{4}$

Remaining share $= 1 - \frac{1}{4} = \frac{4-1}{4}$

$= \frac{3}{4}$

New share of old partners = Remaining share × Old share

Vimal $= \frac{3}{4} \times \frac{2}{3} = \frac{6}{12}$

Athi $= \frac{3}{4} \times \frac{1}{3} = \frac{3}{12}$

Share of new partner

Jeyam $= \frac{1}{4}$

In order to equalise the denominator, multiply and divide by 3

Jeyam's share $= \frac{1}{4} \times \frac{3}{3} = \frac{3}{12}$

New profit sharing ratio of Vimal, Athi and Jeyam = $\frac{6}{12} : \frac{3}{12} : \frac{3}{12}$ that is, 2:1:1

Illustration 17

Anil, Sunil and Hari are partners in a firm sharing profits in the ratio of 4:3:3. They admit Raja for 20% profit. Calculate the new profit sharing ratio and sacrificing ratio.

Solution

Computation of sacrificing ratio and new profit sharing ratio

Old ratio of Anil, Sunil and Hari = 4:3:3 or $\frac{4}{10} : \frac{3}{10} : \frac{3}{10}$

Raja's share of profit = 20% or 20/100 or 1/5

Let the total share be 1

Remaining share $= 1 - \frac{1}{5} = \frac{5-1}{5}$

$= \frac{4}{5}$

New share of old partners = Remaining share × Old share

Anil $= \frac{4}{5} \times \frac{4}{10} = \frac{16}{50}$

Sunil $= \frac{4}{5} \times \frac{3}{10} = \frac{12}{50}$

Hari $= \frac{4}{5} \times \frac{3}{10} = \frac{12}{50}$

Share of new partner

Raja $= \frac{1}{5}$

In order to equalise the denominator, multiply and divide Raja's share by 10

Raja's share $= \frac{1}{5} \times \frac{10}{10} = \frac{10}{50}$

New profit sharing ratio of Anil, Sunil, Hari and Raja = $\frac{16}{50} : \frac{12}{50} : \frac{12}{50} : \frac{10}{50}$ that is, 8:6:6:5. Sacrificing ratio = 4:3:3

5.6 Adjustment for goodwill

Reputation built up by a firm has an impact on the present profit and future profit to be earned by the firm. At the time of admission of a partner, the existing partners sacrifice part of their share of profit in favour of the new partner. Hence, to compensate the sacrifice made by the existing partners, goodwill of the firm has to be valued and adjusted. In addition to capital, the new partner may contribute towards goodwill. This goodwill is distributed in the sacrificing ratio to the old partners who sacrifice.

5.6.1 Accounting treatment for goodwill

Accounting treatment for goodwill on admission of a partner is disccussed below:

1. When new partner brings cash towards goodwill
2. When the new partner does not bring goodwill in cash or in kind
3. When the new partner brings only a part of the goodwill in cash or in kind
4. Existing goodwill

1. When new partner brings cash towards goodwill

When the new partner brings cash towards goodwill in addition to the amount of capital, it is distributed to the existing partners in the sacrificing ratio. The following journal entries are to be made:

(i) For the goodwill brought in cash credited to old partners' capital account

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Cash / Bank A/c	Dr.		xxx	
	To Old partners' capital / current A/c (in sacrificing ratio)				xxx

(ii) For the goodwill brought in kind (in the form of assets) credited to old partners' capital account

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Respective Asset A/c	Dr.		xxx	
	To Old partners' capital / current A/c (in sacrificing ratio)				xxx

(iii) For withdrawal of cash received for goodwill by the old partners

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Old partners' capital / current A/c	Dr.		xxx	
	To Cash / Bank A/c				xxx

Illustration 18

Amudha and Bhuvana are partners who share profits and losses in the ratio of 5:3. Chithra joins the firm on 1st January, 2019 for 3/8 share of profits and brings in cash for her share of goodwill of ₹ 8,000. Pass necessary journal entry for adjusting goodwill on the assumption that the fluctuating capital method is followed and the partners withdraw the entire amount of their share of goodwill.

Solution

As the sacrifice made by the existing partners is not mentioned, it is assumed that they sacrifice in their old profit sharing ratio 5:3. Therefore, sacrificing ratio is 5:3.

Journal Entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
2019	Bank A/c Dr.		8,000	
January 1	To Amudha's capital A/c (5/8)			5,000
	To Bhuvana's capital A/c (3/8)			3,000
	(Cash brought for goodwill credited to Amudha and Bhuvana in sacrificing ratio)			
,,	Amudha's capital A/c Dr.		5,000	
	Bhuvana's capital A/c Dr.		3,000	
	To Bank A/c			8,000
	(Amount withdrawn by the partners)			

Illustration 19

Arun, Babu and Charles are partners sharing profits and losses equally. They admit Durai into partnership for 1/4 share in future profits. The goodwill of the firm is valued at ₹ 36,000 and Durai brought cash for his share of goodwill. The existing partners withdraw half of the amount of their share of goodwill. Pass necessary journal entries on the assumption that the fluctuating capital method is followed.

Solution

Durai's share of goodwill = 36,000 × 1/4 = ₹ 9,000

As the sacrifice made by the existing partners is not mentioned, it is assumed that they sacrifice in their old profit sharing ratio 1:1:1. Therefore, sacrificing ratio is 1:1:1.

Journal Entries

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank A/c Dr.		9,000	
	To Arun's capital A/c			3,000
	To Babu's capital A/c			3,000
	To Charles's capital A/c			3,000
	(Cash brought for goodwill credited to old partners' capital account in sacrificing ratio)			

	Arun's capital A/c Dr.		1,500	
	Babu's capital A/c Dr.		1,500	
	Charles's capital A/c Dr.		1,500	
	To Bank A/c			4,500
	(Cash withdrawn by the partners)			

Illustration 20

Vasu and Devi are partners sharing profits and losses in the ratio of 3:2. They admit Nila into partnership for 1/4 share of profit. Nila pays cash ₹ 3,000 towards her share of goodwill. The new ratio is 3:3:2. Pass necessary journal entry on the assumption that the fixed capital system is followed.

Solution

Calculation of sacrificing ratio

Sacrificing ratio = Old share – New share

Vasu $= \frac{3}{5} - \frac{3}{8} = \frac{24-15}{40} = \frac{9}{40}$

Devi $= \frac{2}{5} - \frac{3}{8} = \frac{16-15}{40} = \frac{1}{40}$

Therefore, sacrificing ratio is 9:1

Journal entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank A/c Dr.		3,000	
	To Vasu's current A/c (9/10)			2,700
	To Devi's current A/c (1/10)			300
	(Cash brought for goodwill credited to old partners' capital account in sacrificing ratio)			

2. When the new partner does not bring goodwill in cash or in kind

If the new partner does not bring goodwill in cash or in kind, his share of goodwill must be adjusted through the capital accounts of the partners. The following journal entry is passed.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	New partners' capital A/c Dr.		xxx	
	To Old partners' capital / current A/c (in sacrificing ratio)			xxx

Illustration 21

Ashok and Mumtaj were partners in a firm sharing profits and losses in the ratio of 5:1. They have decided to admit Tharun into the firm for 2/9 share of profits. The goodwill of the firm on the date of admission was valued at ₹ 27,000. Tharun is not able to bring in cash for his share of goodwill. Pass necessary journal entries for goodwill on the assumption that the fluctuating capital system is followed.

Solution

As the sacrifice made by the existing partners is not mentioned, it is assumed that they sacrifice in their old profit sharing ratio of 5:1. Therefore, sacrificing ratio is 5:1.

Tharun's share of goodwill = $27{,}000 \times \frac{2}{9}$ = ₹ 6,000

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Tharun's capital A/c	Dr.		6,000	
	To Ashok's capital A/c (5/6)				5,000
	To Mumtaj's capital A/c (1/6)				1,000
	(Tharun's share of goodwill credited to the old partners' capital account in the sacrificing ratio)				

3. When the new partner brings only a part of the goodwill in cash or in kind

Sometimes the new partner may bring only a part of the goodwill in cash or assets. In such a case, for the cash or the assets brought, the respective account is debited and for the amount not brought in cash or kind, the new partner's capital account is debited. The following journal entry is passed.

Journal entry

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Cash / Bank A/c	Dr.		xxx	
	New partners' capital A/c	Dr.		xxx	
	To Old partners' capital / current A/c (in sacrificing ratio)				xxx

Illustration 22

Aravind and Balaji are partners sharing profits and losses in 3:2 ratio. They admit Anirudh into partnership. The new profit sharing ratio is agreed at 1:1:1. Anirudh's share of goodwill is valued at ₹ 20,000 of which he pays ₹ 12,000 in cash. Pass necessary journal entries for goodwill on the assumption that the fluctuating capital method is followed.

Solution

Calculation of sacrificing ratio

Sacrificing ratio = Old share – New share

Aravind $= \frac{3}{5} - \frac{1}{3} = \frac{9-5}{15} = \frac{4}{15}$

Balaji $= \frac{2}{5} - \frac{1}{3} = \frac{6-5}{15} = \frac{1}{15}$

Therefore, sacrificing ratio is 4:1

Journal entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Cash A/c Dr.		12,000	
	Anirudh's capital A/c Dr.		8,000	
	To Aravind's capital A/c (4/5)			16,000
	To Balaji's capital A/c (1/5)			4,000
	(Share of goodwill of Anirudh credited to old partners' capital account)			

4. Existing goodwill

If goodwill already appears in the books of accounts, at the time of admission if the partners decide, it can be written off by transferring it to the existing partners' capital account / current account in the old profit sharing ratio. The following journal entry is to be passed:

Journal entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Old partners' capital / current A/c (in old ratio) Dr.		xxx	
	To Goodwill A/c			xxx
	(Existing goodwill written off)			

Illustration 23

Sathish and Sudhan are partners in a firm sharing profits and losses in the ratio of 4:3. On 1st April 2018, they admitted Sasi as a partner. On the date of Sasi's admission, goodwill appeared in the books of the firm at ₹ 35,000. By assuming fluctuating capital account, pass the necessary journal entry if the partners decide to

(i) write off the entire amount of existing goodwill

(ii) write off ₹ 21,000 of the existing goodwill.

Solution

(i) To write off the entire amount of existing goodwill

Journal entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
2018	Sathish's capital A/c (4/7) Dr.		20,000	
April 1	Sudhan's capital A/c (3/7) Dr.		15,000	
	To Goodwill A/c			35,000
	(Existing goodwill written off)			

(ii) To write off ₹ 21,000 of the existing goodwill

Journal entry

Date	Particulars	L.F.	Debit ₹	Credit ₹
2018	Sathish's capital A/c (21,000 x 4/7) Dr.		12,000	
April 1	Sudhan's capital A/c (21,000 x 3/7) Dr.		9,000	
	To Goodwill A/c			21,000
	(Existing goodwill written off to the extent of ₹ 21,000)			

DO YOU KNOW?

When goodwill is paid by the new partner to the old partners privately, no entry is made in the books of the partnership firm.

5.7 Adjustment of capital on the basis of new profit sharing ratio

Sometimes, it may be agreed by the partners that their capitals in the reconstituted firm be in the proportion of their new profit sharing ratio. There can be two situations.

The new partner may be required to bring proportionate capital for his share of profit. New partner's capital is calculated on the basis of the capital of the reconstituted firm or on the basis of combined capitals of the old partners for their share of profit.

The old partners may be required to make their capital in proportion to their new profit sharing ratio. Old partners' capital is calculated on the basis of the capital brought by the new partner for his share of profit. The deficiency or excess in the old partners' capital account may be adjusted through the current accounts or cash may be brought in or withdrawn by the partners.

Comprehensive problems

Illustration 24

Vetri and Ranjit are partners, sharing profits in the ratio of 3:2. Their balance sheet as on 31st December 2017 is as under:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Furniture	25,000
Vetri	30,000		Stock	20,000
Ranjit	20,000	50,000	Debtors	10,000
Reserve fund		5,000	Cash in hand	35,000
Sundry creditors		45,000	Profit and loss A/c (loss)	10,000
		1,00,000		1,00,000

On 1.1.2018, they admit Suriya into their firm as a partner on the following arrangements.

(i) Suriya brings ₹ 10,000 as capital for 1/4 share of profit.

(ii) Stock to be depreciated by 10%

(iii) Debtors to be revalued at ₹ 7,500.

(iv) Furniture to be revalued at ₹ 40,000.

(v) There is an outstanding wages of ₹ 4,500 not yet recorded.

Prepare revaluation account, partners' capital account and the balance sheet of the firm after admission.

Solution

Dr **Revaluation Account** **Cr.**

Particulars	₹	₹	Particulars	₹
To Stock A/c		2,000	By Furniture A/c	15,000
To Debtors A/c		2,500		
To Outstanding wages A/c		4,500		
To Profit on revaluation transferred to capital A/c				
Vetri (3/5)	3,600			
Ranjit (2/5)	2,400	**6,000**		
		15,000		15,000

Dr. **Capital Account** **Cr.**

Particulars	Vetri ₹	Ranjit ₹	Suriya ₹	Particulars	Vetri ₹	Ranjit ₹	Suriya ₹
To Profit and loss A/c	6,000	4,000	-	By Balance b/d	30,000	20,000	-
To Balance c/d	**30,600**	**20,400**	**10,000**	By Reserve fund A/c	3,000	2,000	-
				By Revaluation A/c	3,600	2,400	-
				By Cash A/c	-	-	10,000
	36,600	24,400	10,000		36,600	24,400	10,000
				By Balance b/d	30,600	20,400	10,000

Balance Sheet as on 1st January 2018

Liabilities	₹	₹	Assets	₹	₹
Capital accounts:			Furniture	25,000	
Vetri	30,600		Add: Appreciation	15,000	40,000
Ranjit	20,400		Stock	20,000	
Suriya	10,000	61,000	Less: Depreciation	2,000	18,000
Sundry creditors		45,000	Debtors	10,000	
Outstanding wages		4,500	Less: Decrease	2,500	7,500
			Cash in hand	35,000	
			Add: Suriya's capital	10,000	45,000
		1,10,500			1,10,500

Illustration 25

The balance sheet of Rekha and Mary on 31st March 2018 is as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Buildings	50,000
Rekha	50,000		Stock	8,000
Mary	30,000	80,000	Sundry debtors	60,000
General reserve		40,000	Cash at bank	32,000
Workmen compensation fund		10,000		
Sundry creditors		20,000		
		1,50,000		1,50,000

They share the profits and losses in the ratio of 3:1.They agreed to admit Kavitha into the partnership firm for 1/4 share of profit which she gets entirely from Rekha.

Following are the conditions:

(i) Kavitha has to bring ₹ 20,000 as capital. Her share of goodwill is valued at 4,000. She could not bring cash towards goodwill.

(ii) Depreciate buildings by 10%

(iii) Stock to be revalued at ₹ 6,000

(iv) Create provision for doubtful debts at 5% on debtors

Prepare necessary ledger accounts and the balance sheet after admission.

Solution

Dr. **Revaluation Account** **Cr.**

Particulars	₹	Particulars	₹	₹
To Buildings A/c	5,000	By Loss on revaluation transferred to		
To Stock A/c	2,000	Rekha's capital A/c (3/4)	7,500	
To Provision for bad debts A/c	3,000	Mary's capital A/c (1/4)	2,500	10,000
	10,000			10,000

Dr. **Capital Account** **Cr.**

Particulars	Rekha ₹	Mary ₹	Kavitha ₹	Particulars	Rekha ₹	Mary ₹	Kavitha ₹
To Revaluation A/c	7,500	2,500	-	By Balance b/d	50,000	30,000	-
To Rekha's capital A/c (share of goodwill)	-	-	4,000	By Bank A/c	-	-	20,000
				By General reserve A/c	30,000	10,000	-
				By Workmen compensation fund A/c	7,500	2,500	-
To Balance c/d	**84,000**	**40,000**	**16,000**	By Kavitha's capital A/c (share of goodwill)	4,000	-	-
	91,500	42,500	20,000		91,500	42,500	20,000
				By Balance b/d	84,000	40,000	16,000

Balance Sheet as on 1st April 2018

Liabilities	₹	₹	Assets	₹	₹
Capital accounts:			Buildings	50,000	
Rekha	84,000		Less: Depreciation	5,000	45,000
Mary	40,000		Stock	8,000	
Kavitha	16,000	1,40,000	Less: Decrease	2,000	6,000
Sundry creditors		20,000	Sundry debtors	60,000	
			Less: Provision for		
			doubtful debts	3,000	57,000
			Bank (32,000+20,000)		52,000
		1,60,000			1,60,000

Illustration 26

Ameer and Raja are partners sharing profits in the ratio of 3:2. Their balance sheet is shown as under on 31.12.2018.

Liabilities	₹	₹	Assets	₹
Capital accounts:			Machinery	60,000
Ameer	80,000		Furniture	40,000
Raja	70,000	1,50,000	Debtors	30,000
Reserve fund		15,000	Stock	10,000
Creditors		35,000	Prepaid insurance	40,000
			Cash at bank	20,000
		2,00,000		2,00,000

Rohit is admitted as a new partner who introduces a capital of ₹ 30,000 for his 1/5 share in future profits. He brings ₹ 10,000 for his share of goodwill.

Following revaluations are made:

(i) Stock is to be appreciated to ₹ 14,000

(ii) Furniture is to be depreciated by 5%

(iii) Machinery is to be revalued at ₹ 80,000

Prepare the necessary ledger accounts and the balance sheet after the admission.

Solution

Dr. **Revaluation Account** **Cr.**

Particulars	₹	₹	Particulars	₹
To Furniture A/c		2,000	By Stock A/c	4,000
To Profit on revaluation transferred to			By Machinery A/c	20,000
Ameer's capital A/c (3/5)	13,200			
Raja's capital A/c (2/5)	8,800	**22,000**		
		24,000		24,000

Dr. **Capital Account** **Cr.**

Particulars	Ameer ₹	Raja ₹	Rohit ₹	Particulars	Ameer ₹	Raja ₹	Rohit ₹
To Balance c/d	**1,08,200**	**88,800**	**30,000**	By Balance b/d	80,000	70,000	-
				By Bank A/c	-	-	30,000
				By Reserve fund A/c	9,000	6,000	-
				By Revaluation A/c	13,200	8,800	-
				By Bank A/c* (share of goodwill)	6,000	4,000	-
	1,08,200	88,800	30,000		1,08,200	88,800	30,000
				By Balance b/d	1,08,200	88,800	30,000

*__Note:__ Since the sacrificing ratio is not given and the new partner's share is given, it is assumed that the old profit sharing ratio (3:2) is the sacrificing ratio and the new partner's share of goodwill is distributed to the old partners accordingly.

Dr. **Cash at bank Account** **Cr.**

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	20,000		By Balance c/d	**60,000**
	To Rohit's capital A/c	30,000			
	To Ameer's capital A/c	6,000			
	To Raja's capital A/c	4,000			
		60,000			60,000

Balance Sheet as on 1st January 2019

Liabilities	₹	₹	Assets	₹	₹
Capital accounts:			Machinery	60,000	
Ameer	1,08,200		Add: Appreciation	20,000	80,000
Raja	88,800		Furniture	40,000	
Rohit	30,000	2,27,000	Less: Depreciation	2,000	38,000
Creditors		35,000	Debtors		30,000
			Stock	10,000	
			Add: Appreciation	4,000	14,000
			Prepaid insurance		40,000
			Cash at bank		60,000
		2,62,000			2,62,000

Illustration 27

Veena and Pearl are partners in a firm sharing profits and losses in the ratio of 2:1. Their balance sheet as on 31st March, 2018 is as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts			Buildings	60,000
Veena	60,000		Machinery	30,000
Pearl	40,000	1,00,000	Debtors	20,000
General reserve		30,000	Stock	10,000
Workmen compensation fund		10,000	Cash at bank	30,000
Sundry creditors		10,000		
		1,50,000		1,50,000

Deri is admitted on 1.4.2018 subject to the following conditions:

(a) The new profit sharing ratio among Veena, Pearl and Deri is 5:3:2.

(b) Deri has to bring a capital of ₹ 30,000

(c) Stock to be depreciated by 20%

(d) Anticipated claim on workmen compensation fund is ₹ 1,000

(e) Unrecorded investment of ₹ 11,000 has to be brought into books

(f) The goodwill of the firm is valued at ₹ 30,000 and Deri brought cash for his share of goodwill. The existing partners withdraw the entire amount brought by Deri towards goodwill.

Prepare the necessary ledger accounts and balance sheet after admission.

Solution

Dr. **Revaluation Account** Cr.

Particulars	₹	₹	Particulars	₹
To Stock A/c		2,000	By Investments A/c	11,000
To Profit on revaluation transferred to				
Veena's capital A/c (2/3)	6,000			
Pearl's capital A/c (1/3)	3,000	9,000		
		11,000		11,000

Old ratio of Veena and Pearl $= 2:1$ that is, $\frac{2}{3}:\frac{1}{3}$

New ratio of Veena, Pearl and Deri $= 5:3:2$ i.e. $\frac{5}{10}:\frac{3}{10}:\frac{2}{10}$

Share sacrificed = Old share - New share

Veena $= \frac{2}{3} - \frac{5}{10} = \frac{20-15}{30} = \frac{5}{30}$

Pearl $= \frac{1}{3} - \frac{3}{10} = \frac{10-9}{30} = \frac{1}{30}$

Sacrificing ratio of Veena and Pearl = 5:1

Dr. **Capital Account** Cr.

Particulars	Veena ₹	Pearl ₹	Deri ₹	Particulars	Veena ₹	Pearl ₹	Deri ₹
To Bank A/c	5,000	1,000	-	By Balance b/d	60,000	40,000	-
To Balance c/d	**92,000**	**56,000**	**30,000**	By Bank A/c	-	-	30,000
				By General reserve A/c	20,000	10,000	-
				By Workmen compensation fund A/c (10,000- 1,000)	6,000	3,000	-
				By Revaluation A/c	6,000	3,000	-
				By Bank A/c* (share of goodwill)	5,000	1,000	-
	97,000	57,000	30,000		97,000	57,000	30,000
				By Balance b/d	92,000	56,000	30,000

* Goodwill of the firm is ₹ 30,000

Deri's share of goodwill = 30,000 × 2/10 = ₹ 6,000

It is to be distributed to Veena and Pearl in their sacrificing ratio of 5:1

Dr. **Cash at bank Account** Cr.

Particulars	₹	Particulars	₹
To Balance b/d	30,000	By Veena's capital A/c	5,000
To Deri's capital A/c	30,000	By Pearl's capital A/c	1,000
To Veena's capital A/c	5,000	By Balance c/d	60,000
To Pearl's capital A/c	1,000		
	66,000		66,000

Balance Sheet as on 1st April 2018

Liabilities	₹	₹	Assets	₹	₹
Capital accounts:			Buildings		60,000
Veena	92,000		Machinery		30,000
Pearl	56,000		Investments		11,000
Deri	30,000	1,78,000	Debtors		20,000
Workmen's compensation			Stock	10,000	
fund (10,000-9,000)		1,000	Less: Decrease	2,000	8,000
Sundry creditors		10,000	Cash at bank		60,000
		1,89,000			1,89,000

Points to remember

- On admission of a new partner, the firm is reconstituted with a new agreement and the existing agreement comes to an end.
- On admission of a partner, generally there is a change in the mutual rights of the partners.The new partner acquires the right to share the future profits and share the assets of the firm.
- The new partner becomes liable for all the acts which are carried out by the firm from the date of his / her admission into the firm.
- On admission of a partner, the accumulated profits, accumulated losses and reserves before admission are to be distributed to the existing partners in the old ratio.
- When a partner is admitted into the firm, assets and liabilities are to be revalued and the profit or loss on revaluation is to be distributed to the existing partners in the old ratio.

❖ At the time of admission of a partner it is necessary to determine the new profit sharing ratio because the new partner is entitled to share the future profits of the firm.

❖ If the new profit sharing ratio is not agreed, the partners will share the profits and losses equally.

❖ The existing partners sacrifice part of their share of profit in favour of the new partner. To compensate the sacrifice made by the existing partners, goodwill brought by the new partner is distributed in the sacrificing ratio to the old partners who sacrifice.

❖ Sacrificing ratio is the proportion of the profit which is sacrificed or foregone by the old partners in favour of the new partner.

Self-examination questions

I Multiple Choice questions

Choose the correct answer

1. Revaluation A/c is a

(a) Real A/c　　(b) Nominal A/c

(c) Personal A/c　　(d) Impersonal A/c

2. On revaluation, the increase in the value of assets leads to

(a) Gain　　(b) Loss

(c) Expense　　(d) None of these

3. The profit or loss on revaluation of assets and liabilities is transferred to the capital account of

(a) The old partners　　(b) The new partner

(c) All the partners　　(d) The Sacrificing partners

4. If the old profit sharing ratio is more than the new profit sharing ratio of a partner, the difference is called

(a) Capital ratio　　(b) Sacrificing ratio

(c) Gaining ratio　　(d) None of these

5. At the time of admission, the goodwill brought by the new partner may be credited to the capital accounts of

(a) all the partners　　(b) the old partners

(c) the new partner　　(d) the sacrificing partners

6. Which of the following statements is not true in relation to admission of a partner

(a) Generally mutual rights of the partners change

(b) The profits and losses of the previous years are distributed to the old partners

(c) The firm is reconstituted under a new agreement

(d) The existing agreement does not come to an end

7. Match List I with List II and select the correct answer using the codes given below:

List I	List II
(i) Sacrificing ratio	1. Investment fluctuation fund
(ii) Old profit sharing ratio	2. Accumulated profit
(iii) Revaluation Account	3. Goodwill
(iv) Capital Account	4. Unrecorded liability

Codes:

	(i)	(ii)	(iii)	(iv)
(a)	1	2	3	4
(b)	3	2	4	1
(c)	4	3	2	1
(d)	3	1	2	4

8. Select the odd one out

(a) Revaluation profit
(b) Accumulated loss
(c) Goodwill brought by new partner
(d) Investment fluctuation fund

9. James and Kamal are sharing profits and losses in the ratio of 5:3. They admit Sunil as a partner giving him 1/5 share of profits. Find out the sacrificing ratio.

(a) 1:3
(b) 3:1
(c) 5:3
(d) 3:5

10. Balaji and Kamalesh are partners sharing profits and losses in the ratio of 2:1. They admit Yogesh into partnership. The new profit sharing ratio between Balaji, Kamalesh and Yogesh is agreed to 3:1:1. Find the sacrificing ratio between Balaji and Kamalesh.

(a) 1:3
(b) 3:1
(c) 2:1
(d) 1:2

Answer

1. (b)	**2. (a)**	**3. (a)**	**4. (b)**	**5.(d)**	**6. (d)**	**7. (b)**	**8. (c)**	**9. (c)**	**10. (d)**

II Very short answer questions

1. What is meant by revaluation of assets and liabilities?
2. How are accumulated profits and losses distributed among the partners at the time of admission of a new partner?
3. What is sacrificing ratio?
4. Give the journal entry for writing off existing goodwill at the time of admission of a new partner.
5. State whether the following will be debited or credited in the revaluation account.

   (a) Depreciation on assets
   (b) Unrecorded liability
   (c) Provision for outstanding expenses
   (d) Appreciation of assets

III Short answer questions

1. What are the adjustments required at the time of admission of a partner?
2. What are the journal entries to be passed on revaluation of assets and liabilities?
3. Write a short note on accounting treatment of goodwill.

IV Exercises

Distribution of accumulated profits, reserves and losses

1. Arul and Anitha are partners sharing profits and losses in the ratio of 4:3. On 31.3.2018, Ajay was admitted as a partner. On the date of admission, the book of the firm showed a general reserve of ₹ 42,000. Pass the journal entry to distribute the general reserve.

   (Answer: Arul: ₹ 24,000(Cr.); Anitha: ₹ 18,000 (Cr.))

2. Anjali and Nithya are partners of a firm sharing profits and losses in the ratio of 5:3. They admit Pramila on 1.1.2018. On that date, their balance sheet showed accumulated loss of ₹40,000 on the asset side of the balance sheet. Give the journal entry to transfer the accumulated loss on admission.

   (Answer: Profit and loss: Anjali: ₹ 25,000 (Dr.); Nithya: ₹ 15,000 (Dr.))

3. Oviya and Kavya are partners in a firm sharing profits and losses in the ratio of 5:3. They admit Agalya into the partnership. Their balance sheet as on 31st March, 2019 is as follows:

Balance Sheet as on 31st March 2019

Liabilities		₹	Assets	₹
Capital accounts:			Buildings	40,000
Oviya	50,000		Plant	50,000
Kavya	40,000	90,000	Furniture	30,000
Profit and loss appropriation A/c		40,000	Debtors	20,000
General reserve		8,000	Stock	10,000
Workmen's compensation fund		12,000	Cash	20,000
Sundry creditors		20,000		
		1,70,000		1,70,000

Pass journal entry to transfer the accumulated profits and reserve on admission.

(Answer: Oviya: ₹ 37,500; Kavya: ₹ 22,500)

Revaluation of assets and liabilities

4. Hari, Madhavan and Kesavan are partners, sharing profits and losses in the ratio of 5:3:2. As from 1st April 2017, Vanmathi is admitted into the partnership and the new profit sharing ratio is decided as 4:3:2:1. The following adjustments are to be made.

(a) Increase the value of premises by ₹ 60,000.

(b) Depreciate stock by ₹ 5,000, furniture by ₹ 2,000 and machinery by ₹ 2,500.

(c) Provide for an outstanding liability of ₹ 500.

Pass journal entries and prepare revaluation account.

(Answer: Revaluation profit: ₹ 50,000)

5. Seenu and Siva are partners sharing profits and losses in the ratio of 5:3. In the view of Kowsalya admission, they decided

(a) To increase the value of building by ₹ 40,000.

(b) To bring into record investments at ₹ 10,000, which have not so far been brought into account.

(c) To decrease the value of machinery by ₹ 14,000 and furniture by ₹ 12,000.

(d) To write off sundry creditors by ₹ 16,000.

Pass journal entries and prepare revaluation account.

(Answer: Revaluation profit: ₹ 40,000)

6. Sai and Shankar are partners, sharing profits and losses in the ratio of 5:3. The firm's balance sheet as on 31st December, 2017, was as follows:

Liabilities	₹	₹	Assets	₹	₹
Capital accounts:			Building		34,000
Sai	48,000		Furniture		6,000
Shankar	40,000	88,000	Investment		20,000
Creditors		37,000	Debtors	40,000	
Outstanding wages		8,000	Less: Provision for		
			bad debts	3,000	37,000
			Bills receivable		12,000
			Stock		16,000
			Bank		8,000
		1,33,000			1,33,000

On 31st December, 2017 Shanmugam was admitted into the partnership for 1/4 share of profit with ₹ 12,000 as capital subject to the following adjustments.

(a) Furniture is to be revalued at ₹ 5,000 and building is to be revalued at ₹ 50,000.

(c) Provision for doubtful debts is to be increased to ₹5,500

(d) An unrecorded investment of ₹ 6,000 is to be brought into account

(e) An unrecorded liability ₹ 2,500 has to be recorded now.

Pass journal entries and prepare Revaluation Account and capital account of partners after admission.

(Answer: Revaluation Profit: ₹ 16,000; Capital accounts: Sai: ₹ 58,000(Cr.), Shankar: ₹ 46,000(Cr.); Shanmugam: ₹ 12,000(Cr.))

7. Amal and Vimal are partners in a firm sharing profits and losses in the ratio of 7:5. Their balance sheet as on 31st March, 2019, is as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Land	80,000
Amal	70,000		Furniture	20,000
Vimal	50,000	1,20,000	Stock	25,000
Sundry creditors		30,000	Debtors	30,000
Profit and loss A/c		24,000	Bank	19,000
		1,74,000		1,74,000

Nirmal is admitted as a new partner on 1.4.2018 by introducing a capital of ₹ 30,000 for 1/3 share in the future profit subject to the following adjustments.

(a) Stock to be depreciated by ₹5,000

(b) Provision for doubtful debts to be created for ₹3,000

(c) Land to be appreciated by ₹ 20,000

Prepare revaluation account and capital account of partners after admission.

(Answer: Revaluation Profit: ₹ 12,000; Capital accounts: Amal ₹91,000(Cr.), Vimal ₹65,000(Cr.), Nirmal ₹30,000(Cr.))

Computation of sacrificing ratio and new profit sharing ratio

8. Praveena and Dhanya are partners sharing profits in the ratio of 7:3. They admit Malini into the firm. The new ratio among Praveena, Dhanya and Malini is 5:2:3. Calculate the sacrificing ratio.

(Answer: Sacrificing ratio 2:1)

9. Ananth and Suman are partners sharing profits and losses in the ratio of 3:2. They admit Saran for 1/5 share, which he acquires entirely from Ananth. Find out the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 2:2:1; Sacrificing ratio 1:0)

10. Raja and Ravi are partners, sharing profits in the ratio of 3:2. They admit Ram for 1/4 share of the profit. He takes 1/20 share from Raja and 4/20 from Ravi. Calculate the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 11:4:5; Sacrificing ratio 1:4)

11. Vimala and Kamala are partners, sharing profits and losses in the ratio of 4:3. Vinitha enters into the partnership and she acquires 1/14 from Vimala and 1/14 from Kamala. Find out the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 7:5:2; Sacrificing ratio 1:1)

12. Govind and Gopal are partners in a firm sharing profits in the ratio of 5:4. They admit Rahim as a partner. Govind surrenders 2/9 of his share in favour of Rahim. Gopal surrenders 1/9 of his share in favour of Rahim. Calculate the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 35:32:14; Sacrificing ratio 5:2)

13. Prema and Chandra share profits in the ratio of 5:3. Hema is admitted as a partner. Prema surrendered 1/8 of her share and Chandra surrendered 1/8 of her share in favour of Hema. Calculate the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 35:21:8; Sacrificing ratio 5:3)

14. Karthik and Kannan are equal partners. They admit Kailash with 1/4 share of the profit. Kailash acquired his share from old partners in the ratio of 7:3. Calculate the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 13:17:10; Sacrificing ratio 7:3)

15. Selvam and Senthil are partners sharing profit in the ratio of 2:3. Siva is admitted into the firm with 1/5 share of profit. Siva acquires equally from Selvam and Senthil. Calculate the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 3:5:2; Sacrificing ratio 1:1)

16. Mala and Anitha are partners, sharing profits and losses in the ratio of 3:2. Mercy is admitted into the partnership with 1/5 share in the profits. Calculate new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 12:8:5; Sacrificing ratio 3:2)

17. Ambika, Dharani and Padma are partners in a firm sharing profits in the ratio of 5:3:2. They admit Ramya for 25% profit. Calculate the new profit sharing ratio and sacrificing ratio.

(Answer: New profit sharing ratio 15:9:6:10; Sacrificing ratio 5:3:2)

Adjustment for goodwill

18. Aparna and Priya are partners who share profits and losses in the ratio of 3:2. Brindha joins the firm for 1/5 share of profits and brings in cash for her share of goodwill of ₹ 10,000. Pass necessary journal entry for adjusting goodwill on the assumption that the fluctuating capital method is followed and the partners withdraw the entire amount of their share of goodwill.

(Answer: Share of goodwill: Aparna: ₹ 6,000; Priya: ₹ 4,000)

19. Deepak, Senthil and Santhosh are partners sharing profits and losses equally. They admit Jerald into partnership for 1/3 share in future profits. The goodwill of the firm is valued at ₹ 45,000 and Jerald brought cash for his share of goodwill. The existing partners withdraw half of the amount of their share of goodwill. Pass necessary journal entries for adjusting goodwill on the assumption that the fluctuating capital method is followed.

(Answer: Share of goodwill: Deepak: ₹ 5,000; Senthil: ₹5,000; Santhosh: ₹5,000)

20. Malathi and Shobana are partners sharing profits and losses in the ratio of 5:4. They admit Jayasri into partnership for 1/3 share of profit. Jayasri pays cash ₹ 6,000 towards her share of goodwill. The new ratio is 3:2:1. Pass necessary journal entry for adjusting goodwill on the assumption that the fixed capital method is followed.

**(Answer: Share of goodwill: Malathi's current account: ₹2,000;
Shobana's current account ₹4,000)**

21. Anu and Arul were partners in a firm sharing profits and losses in the ratio of 4:1. They have decided to admit Mano into the firm for 2/5 share of profits. The goodwill of the firm on the date of admission was valued at ₹ 25,000. Mano is not able to bring in cash for his share of goodwill. Pass necessary journal entry for goodwill on the assumption that the fluctuating capital method is followed.

(Answer: Share of goodwill: Anu: ₹ 8,000; Arul: ₹ 2,000)

22. Varun and Barath are partners sharing profits and losses 5:4. They admit Dhamu into partnership. The new profit sharing ratio is agreed at 1:1:1. Dhamu's share of goodwill is valued at ₹ 15,000 of which he pays ₹10,000 in cash. Pass necessary journal entries for adjustment of goodwill on the assumption that the fluctuating capital method is followed.

(Answer: Share of goodwill: Varun: ₹10,000; Barath ₹ 5,000)

23. Sam and Jose are partners in a firm sharing profits and losses in the ratio of 3:2. On 1st April 2018, they admitted Joel as a partner. On the date of Joel's admission, goodwill appeared in the books of the firm at ₹ 30,000. By assuming fluctuating capital method, pass the necessary journal entry if the partners decide to

(a) write off the entire amount of existing goodwill

(b) write off ₹ 20,000 of the existing goodwill.

(Answer: Goodwill: (a) Sam ₹ 18,000(Dr.); Jose ₹ 12,000(Dr.)
(b) Sam ₹ 12,000(Dr.); Jose ₹ 8,000(Dr.))

Comprehensive problems

24. Rajan and Selva are partners sharing profits and losses in the ratio of 3:1. Their balance sheet as on 31st March 2017 is as under:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Building	25,000
Rajan	30,000		Furniture	1,000
Selva	16,000	46,000	Stock	20,000
General reserve		4,000	Debtors	16,000
Creditors		37,500	Bills receivable	3,000
			Cash at bank	12,500
			Profit and loss account	10,000
		87,500		87,500

On 1.4.2017, they admit Ganesan as a new partner on the following arrangements:

(i) Ganesan brings ₹10,000 as capital for 1/5 share of profit.

(ii) Stock and furniture is to be reduced by 10%, a reserve of 5% on debtors for doubtful debts is to be created.

(iii) Appreciate buildings by 20%.

Prepare revaluation account, partners' capital account and the balance sheet of the firm after admission.

(Answer: Revaluation profit: ₹ 2,100; Capital accounts: Rajan: ₹ 27,075;
Selva: ₹ 15,025; Ganesan: ₹ 10,000; Balance sheet total: ₹ 89,600)

25. Sundar and Suresh are partners sharing profits in the ratio of 3:2. Their balance sheet as on 1st January, 2017 was as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Buildings	40,000
Sundar	30,000		Furniture	13,000
Suresh	20,000	50,000	Stock	25,000
Creditors		50,000	Debtors	15,000
General reserve		10,000	Bills receivable	14,000
Workmen compensation fund		15,000	Bank	18,000
		1,25,000		1,25,000

They decided to admit Sugumar into partnership for 1/4 share in the profits on the following terms:

(a) Sugumar has to bring in ₹ 30,000 as capital. His share of goodwill is valued at ₹ 5,000. He could not bring cash towards goodwill.
(b) That the stock be valued at ₹ 20, 000.
(c) That the furniture be depreciated by ₹ 2,000.
(d) That the value of building be depreciated by 20%.

Prepare necessary ledger accounts and the balance sheet after admission.

(Answer; Revaluation loss: ₹ 15,000; Capital accounts: Sundar: ₹ 39,000, Suresh ₹ 26,000, Sugumar ₹ 25,000; Balance sheet total: ₹ 1,40, 000)

26. The following is the balance sheet of James and Justina as on 1.1.2017. They share the profits and losses equally.

Liabilities	₹	₹	Assets	₹
Capital accounts:			Building	70,000
James	40,000		Stock	30,000
Justina	50,000	90,000	Debtors	20,000
Creditors		35,000	Bank	15,000
Reserve fund		15,000	Prepaid insurance	5,000
		1,40,000		1,40,000

On the above date, Balan is admitted as a partner with 1/5 share in future profits. Following are the terms for his admission:

(i) Balan brings ₹ 25,000 as capital.

(ii) His share of goodwill is ₹10, 000 and he brings cash for it.

(iii) The assets are to be valued as under:

Building ₹ 80, 000; Debtors ₹ 18,000; Stock ₹ 33,000

Prepare necessary ledger accounts and the balance sheet after admission.

(Answer: Revaluation profit: ₹ 11, 000; Capital accounts: James: ₹ 58, 000; Justina: ₹ 68, 000; Balan: ₹ 25,000; Balance sheet total: ₹ 1,86,000)

27. Anbu and Shankar are partners in a business sharing profits and losses in the ratio of 3:2. The balance sheet of the partners on 31.03.2018 is as follows:

Liabilities	₹	₹	Assets	₹
Capital accounts:			Computer	40,000
Anbu	4,00,000		Motor car	1,60,000
Shankar	3,00,000	7,00,000	Stock	4,00,000
Profit and loss		1,20,000	Debtors	3,60,000
Creditors		1,20,000	Bank	40,000
Workmen compensation fund		60,000		
		10,00,000		10,00,000

Rajesh is admitted for 1/5 share on the following terms:

(i) Goodwill of the firm is valued at ₹ 75,000 and Rajesh brought cash for his share of goodwill.

(ii) Rajesh is to bring ₹ 1,50,000 as his capital.

(iii) Motor car is valued at ₹ 2,00,000; stock at ₹ 3,80,000 and debtors at ₹ 3,50,000.

(iv) Anticipated claim on workmen compensation fund is ₹10,000

(v) Unrecorded investment of ₹ 5,000 has to be brought into account.

Prepare revaluation account, capital accounts and balance sheet after Rajesh's admission.

(Answer: Revaluation profit: ₹15,000; Capital accounts: Anbu: ₹ 5,20,000; Shankar: ₹ 3,80,000; Rajesh: ₹ 1,50,000; Balance sheet total: ₹ 11,80,000)

Student activity 5.3

Read and analyse the following transactions. Fill in the following table by writing asset or liability and put a ✓ in the appropriate column. The first two transactions are done as examples.

(1) The value of inventory should be revalued from ₹ 2,500 to ₹ 3,000.

(2) Building revalued from ₹ 2,00,000 to ₹ 1,60,000

(3) Creditors revalued from ₹ 2,000 to ₹ 1,800, as discount can be availed from creditors.

(4) The value of furniture decreased by ₹ 2,000

(5) A provision for outstanding wages would be created for ₹ 1,000

(6) Vehicle revalued to ₹ 20,000 from ₹ 28,000

(7) Outstanding salary would be created for ₹ 10,000

(8) Provision for doubtful debts is to be created for ₹ 1,000

(9) Land revalued from ₹ 2,00,000 to ₹ 2,50,000

(10) Fixtures revalued from ₹ 20,000 to ₹ 22,000

Transaction number	Asset/liability	Increase	Decrease	Debit revaluation account	Credit revaluation account
1	Asset	✓			✓
2	Asset		✓	✓	
3					
4					
5					
6					
7					
8					
9					
10					

What do you conclude from the above activity? Show your understanding by filling in the table below. Write increase or decrease in the appropriate box. One box is filled in as an example.

Revaluation account	Debit	Credit
Asset	Decrease	?
Liability	?	?

CASE STUDY

Sita and Sumathy started a restaurant in a busy area by forming a partnership business .The restaurant attracted many customers due to its quality of food and customer service. By the end of second year, the restaurant started making profit. After five years, they had a plan to expand the restaurant by opening one more branch. One of their friends, Susan, has good marketing skills. So, Sita and Sumathy mutually agreed to admit Susan into the firm. But, the firm did not have any partnership deed. On admission, the assets and liabilities were revalued. The partners generated goodwill internally. Very soon, Susan with her marketing skills got a contract with a nearby office to supply food for all their employees. It resulted in more profit to the firm.

Discuss on the following:

1. Do you think Sita and Sumathy should have a partnership deed?
2. In the absence of a partnership deed, what is to be done?
3. What are the accounting adjustments to be made when Susan joins in an existing firm?
4. Can the firm record the internally generated goodwill?
5. Susan expects a share on the gain on revaluation. Is it possible for her to get a share?
6. Susan claims a commission on the new contract. Do you agree on this?

To explore further

Is it compulsory for the partners to continue in the business forever? What will happen if any one of the partners leaves the firm? Will the partnership cease to operate?

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