

(13) X and Y are the partners sharing profit and loss in the ratio of 2:3. They admitted Z as a new partner for $\frac{1}{5}$ th share. Goodwill is valued at ₹ 20,000. Balance of goodwill appeared at ₹ 15,000 in the balance sheet. Z brought ₹ 50,000 as his capital and 80 % of his share of goodwill in cash. Old partners withdrew 40 % amount of goodwill in cash which is credited to their capital account. After the admission of Z the profit of the first year of the new firm was ₹ 60,000. Pass necessary journal entries.

5. R and J are the partners sharing profit and loss in the ratio of 2:3. They admitted B as a new partner for $\frac{1}{6}$ th share of profit. Following balances appeared in the books of R and J at the time of the admission of B :

General reserve ₹ 7000	Contingency reserve ₹ 5100
Workmen compensation reserve ₹ 6000	Bad debt reserve ₹ 4200
Investment fluctuation reserve ₹ 1900	Advertisement campaign expenditure ₹ 3400
Profit-loss A/c (Debit balance) ₹ 1600	

Pass necessary journal entries.

6. K and R are the partners sharing profit and loss in the ratio of 4:1. They admitted P as a new partner for $\frac{1}{5}$ th share. Following balances were appearing in the books of K and R at the time of admission of P.

Investment fluctuation reserve ₹ 2500	Workmen compensation reserve ₹ 7000
Bad debt reserve ₹ 3000	Investment ₹ 20,000
Debtors ₹ 70,000	

Pass necessary journal entries in the following cases :

- (1) If market value of investment is as under :
 - (i) ₹ 19,500
 - (ii) ₹ 22,000
 - (2) If following claim of workmen compensation is accepted :
 - (i) ₹ 6000
 - (ii) ₹ 8500
 - (3) If bad debt reserve is to be maintained on debtors :
 - (i) ₹ 4000
 - (ii) ₹ 2500
 - (iii) 10 % bad debt reserve is to be maintained after writting off bad debt ₹ 2000.
7. A and B are the partners sharing profit and loss in equal proportion. They admitted C as a new partner for $\frac{1}{4}$ th share. Following balances were appearing in the balance sheet of A and B at the time of the admission of C.

Patents	₹	30,000	Goodwill	₹	20,000
Land-Building	₹	1,80,000	Machinery	₹	60,000
Stock	₹	35,000	Creditors	₹	40,000

On C's admission, they decided that,

- (i) Patents are to be written off fully.
- (ii) Value of land and building is to be increased by 20 %.
- (iii) Value of machinery is to be decreased upto 60 %.
- (iv) Stock was overvalued by ₹ 4000 than its cost price.
- (v) Creditors of ₹ 6000 are not to be paid.

Pass necessary journal entries and prepare the revaluation account.

8. Aabha and Beena are partners in a firm sharing profit and loss in the ratio of 2:1. Their balance sheet as on 31-3-2017 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital account :		Goodwill	18,000
Aabha 80,000		Land-building	72,000
Beena 60,000	1,40,000	Machinery	40,000
General reserve	18,000	Stock	36,000
Workmen compensation reserve	4500	Debtors 24,000	
Investment fluctuation reserve	1500	– Bad debt reserve 2000	22,000
Creditors	28,000	Investment	8000
Bills payable	12,000	Cash-Bank	2000
		Advertisement campaign expenditure	6000
	2,04,000		2,04,000

They admitted Rushil as a new partner from 1-4-2017 on the following conditions :

- (1) Rushil will bring ₹ 1,00,000 as his capital and ₹ 24,000 as goodwill in cash.
- (2) Value of land and building is to be increased by ₹ 17,000.
- (3) Value of machinery is to be decreased upto ₹ 32,000.
- (4) Provision for bad debt is to be kept at 10 % on debtors.
- (5) Provision for outstanding electricity bill is to be made at ₹ 1100.
- (6) New profit sharing ratio of all three partners is to be kept at 2:1:2.

Pass necessary journal entries and prepare revaluation account, partners' capital account, cash-bank account and balance sheet after admission.

9. Aashtha and Aahna are partners in a firm. The balance sheet of the firm as on 31-3-2017 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital account :		Goodwill	8400
Aashtha 76,000		Land-Building	40,000
Aahna 48,400	1,24,400	Machinery	32,000
Workmen compensation fund	4800	Investment	20,000
Investment fluctuation fund	1600	Debtors	25,200
Provident fund	6400	Stock	14,400
Bad debt reserve	8000	Cash	16,000
Creditors	12,000	Advertisement campaign expenditure	3200
Bills payable	6000	Profit-loss A/c	4000
	1,63,200		1,63,200

The admitted Sonu as a new partner as on 1-4-2017 on the following condition :

- (1) Sonu will bring ₹ 80,000 as her capital and ₹ 7200 as her share of goodwill in cash.
- (2) New profit and loss sharing ratio will be 4:3:3.
- (3) Goodwill is to be valued at ₹ 40,000.
- (4) The claim of workmen compensaiton is accepted at ₹ 3200.
- (5) Aahna will take over investments at ₹ 19,200.
- (6) Accrued interest on investment ₹ 2400 is not recorded.
- (7) Accepted bills payable of ₹ 2000 which was drawn by creditors is not recorded.
- (8) Book value of land-building is 20 % less then its market value.
- (9) Out of insurance premium paid, ₹ 4800 is for next year.

Prepare necessary accounts and balance sheet after admission.

10. Vidit and Vishal are partners sharing profit and loss in the ratio of 2:3. The balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital :		Building	66,000
Vidit 48,000		Machinery	30,000
Vishal 60,000	1,08,000	Stock	18,000
Contingency reserve	9000	Debtors	39,600
Workmen compensation reserve	24,000	Bank	8400
Investment reserve	7200	Investment	18,000
Creditors	30,000		
Bad debt reserve	1800		
	1,80,000		1,80,000

They admitted Bunty on 1-4-2016 as a new partner on the following terms :

- (1) Vidit will sacrifice $\frac{1}{4}$ th from his share and Vishal will sacrifice $\frac{1}{8}$ th from his share in the favour of Bunty.
- (2) Bunty will bring ₹ 72,000 as capital and his share of goodwill in cash.
- (3) Goodwill of the firm is valued at ₹ 32,000.
- (4) Vidit and Vishal withdrew 50 % of goodwill received by them in cash.
- (5) Provision for depreciation on machinery is to be made at 10 %.
- (6) Write off ₹ 3600 as bad debt from debtors and provision for bad debt is to be maintained at 15 %.
- (7) Market value of investment is ₹ 9000 which is to be recorded in the books.
- (8) Claim of workmen compensation is accepted at ₹ 30,000.
- (9) 10 % of creditors are now not to be paid.

Prepare necessary account and balance sheet of new firm.

11. Prerna and Piyush are partners in a firm sharing profit and loss in the ratio of their capital. Balance sheet of their firm was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital account :		Building	90,000
Prerna 50,000		Furniture	17,500
Piyush 1,50,000	2,00,000	Machinery	1,07,500
Reserve fund	30,000	Stock	17,500
Creditors	40,000	Debtors	30,000
Outstanding expenses	1500	Cash-Bank	8250
		Accrued income	750
	2,71,500		2,71,500

They admitted Poyani as a new partner for $\frac{1}{5}$ th share of profit on 31-3-2016 on following terms :

- (1) Poyani brought ₹ 62,500 as capital and ₹ 24,000 as her share of goodwill in cash. 60 % amount of goodwill is withdrawn by the old partners.
- (2) Market value of stock and machinery is ₹ 20,000 and ₹ 1,20,000 respectively.
- (3) Provision for bad debt at 10 % and 2 % discount reserve on debtors is to be made.
- (4) Creditors are to be paid ₹ 30,000.
- (5) Value of building is to be increased by 15 % and value of furniture is to be increased by 20 %.
- (6) Outstanding wages of ₹ 460 is not recorded in the books.

From the above information prepare necessary accounts and new balance sheet of the firm.

12. P and Q are partners sharing profit and loss in the ratio of 3:2. Balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital account :		Land-Building	80,000
P 70,000		Debtors 22,000	
Q 50,000	1,20,000	— Bad debt reserve 2000	20,000
Provident fund	18,000	Stock	36,000
Creditors	22,000	Cash	4000
		Goodwill	20,000
	1,60,000		1,60,000

On above date they admitted R as a new partner on the following terms :

- (1) R will bring ₹ 60,000 as capital in cash.
- (2) Goodwill is valued at ₹ 30,000.
- (3) R can not bring his share of goodwill in cash.

- (4) Value of land and building is ₹ 90,000.
- (5) Bad debt reserve is to be provided at 5 % on debtors.
- (6) Value of stock is to be reduced by ₹ 400.
- (7) Creditors of ₹ 500 are not to be paid.
- (8) New profit and loss sharing ratio of all partners is decided at 5:2:3.

From the above information prepare necessary accounts and balance sheet after admission. Give necessary journal entries for goodwill.

13. A and B are partners in a firm sharing profit and loss in the ratio of 4:1. Balance sheet of their firm on 31-3-2017 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital account :		Land-Building	35,000
A 75,000		Furniture	30,000
B 25,000	1,00,000	Investments	25,000
Current account :		Stock	15,000
A 8000		Debtors 5500	
B 2000	10,000	– Bad debt reserve 500	5000
Workmen accident compensation fund	5000	Bills receivable	2000
Creditors	4000	Cash-Bank	3000
Bills payable	1000	Goodwill	5000
	1,20,000		1,20,000

They admitted C as a new partner on above date on the following conditions. They decided to keep their new profit-loss sharing ratio at 3:1:1 :

- (1) C will bring ₹ 20,000 as capital for his $\frac{1}{5}$ th share of profit and ₹ 5000 as his share of goodwill in cash. Out of goodwill half amount is to be withdrawn by the old partners.
- (2) Value of land and building is to be increased by 10 %. While value of furniture and stock is to be decreased by 5 %.
- (3) Market value of investment is ₹ 35,000. Which is to be shown in the books.
- (4) Provision for doubtful debt is to be made at 10 % on debtors.
- (5) Workmen accident compensation claim is accepted ₹ 1000.
- (6) Dishonour expense of bills receivable ₹ 150 and bank charges ₹ 300 which are paid but not recorded in the books.

Prepare necessary accounts and balance sheet after admission of partners.

14. Rutvi and Princy are partners sharing profit and loss in the ratio of 5:3. The balance sheet of their firm as on 31-3-2017 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Workmen's profit sharing fund	30,000	Bank	60,000
Creditors	1,20,000	Debtors	90,000
Workmen compensation reserve	60,000	Stock	60,000
Current account :		Building	4,50,000
Rutvi	1,50,000	Investments	1,05,000
Princy	1,95,000		
	3,45,000		
Capital account :			
Rutvi	1,20,000		
Princy	90,000		
	2,10,000		
	7,65,000		7,65,000

They admitted Manan as a partner on 1-4-2017 on the following terms :

- (1) Manan will bring his personal furniture of ₹ 75,000 as capital.
- (2) Out of creditors ₹ 60,000 are payable to Manan which is to be transferred to his capital account.
- (3) Manan will be given $\frac{1}{5}$ th share in future.
- (4) Manan will bring ₹ 45,000 as goodwill in cash.
- (5) Goodwill of firm is valued at ₹ 3,00,000.
- (6) Credit purchase of ₹ 15,000 which was not recorded in creditors account and purchase account but it is included in closing stock.
- (7) Market value of stock of ₹ 45,000 is ₹ 36,000.
- (8) Liability of workmen compensation is ₹ 28,000.
- (9) Accrued interest on investment ₹ 24,000 is not recorded.

Prepare new balance sheet after admission.

15. Riya and Gauri are the partners sharing profit and loss in the ratio of 1:2. They admitted Sanju as a new partner for $\frac{1}{5}$ th share on 1-4-2017. Sanju brings ₹ 90,000 as capital in cash. After the adjustment of reserves, profit of revaluation and goodwill the capital of Riya and Gauri was ₹ 1,50,000 and ₹ 2,00,000 respectively. Partners decided to maintain new firms' total capital at ₹ 4,50,000 in their new profit and loss ratio. Necessary amount is to be brought or withdrawn in cash. Prepare partners' capital account.
16. Parshvi and Aneri are the partners sharing profit and loss in the ratio of 2:1. Balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital :		Goodwill	21,000
Parshvi 91,000		Building	1,40,000
Aneri 84,000	1,75,000	Furniture	28,000
Capital reserve	14,700	Stock	18,200
Workmen saving account	7000	Debtors	16,800
Workmen profit sharing fund	8400	Cash	56,000
10 % Loan from bank	35,000		
Creditors	39,900		
	2,80,000		2,80,000

On 1-4-2016 they admitted Henshi as a new partner on the following conditions :

- (1) New profit and loss sharing ratio is to be kept at 3:4:2.
- (2) Henshi brings ₹ 40,000 as capital.
- (3) Interest on bank loan is outstanding for one year.
- (4) Personal expense of Parshvi paid by the firm is debited to the profit and loss account ₹ 5600.
- (5) Reconstruction expense is paid by Aneri ₹ 8400.
- (6) Goodwill is valued at ₹ 90,000.
- (7) Parshvi and Aneri will maintain their capital in the new firm in their new profit and loss sharing ratio by taking Henshi's capital as base. For this purpose necessary adjustments should be made in partners' current account.

Prepare necessary accounts and balance sheet after admission.

17. Ankita and Esha are the partners sharing profit and loss in the ratio of 2:1. Balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital :		Machinery	64,000
Ankita 64,000		Furniture	40,000
Esha 32,000	96,000	Stock	13,600
General reserve	16,800	Debtors 40,000	
Creditors	60,000	– Bad debt reserve 3200	36,800
Bills payable	8000	Cash-Bank	26,400
	1,80,800		1,80,800

They admitted Arpita as a new partner on 1-4-2016 on the following conditions :

- (1) Ankita sacrificed $\frac{1}{12}$ th from her share and Esha sacrificed $\frac{1}{6}$ th from her share in favour of Arpita.
- (2) Arpita is to bring proportionate capital.

- (3) Arpita is to bring her share of goodwill in cash. Goodwill of the firm is valued at ₹ 90,000.
- (4) Fixed assets are to be depreciated by 10 %.
- (5) All debtors are good.
- (6) Insurance premium of ₹ 2400 out of ₹ 12,000 is to be carried forward to next year.

Prepare necessary accounts and balance sheet.

18. Jaini and Aanya are the partners sharing profit and loss in the ratio of 3:2. The balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital :		Building	42,000
Jaini 70,000		Machinery	17,500
Aanya 56,000	1,26,000	Investment	63,000
General reserve	8400	Debtors 56,000	
Investment reserve	4200	– Bad debt reserve 2800	53,200
Workmen profit sharing fund	31,500	Bank	39,200
Creditors	44,800		
	2,14,900		2,14,900

They admitted Priyanka as a partner on 1-4-2016 on the following terms :

- (1) Priyanka will bring ₹ 14,000 as goodwill in cash.
- (2) Priyanka will bring her capital equal to 20 % of new total capital of Jaini and Aanya.
- (3) New profit and loss sharing ratio is to be kept at 2:2:1.
- (4) Provision for bad debt is not required.
- (5) Machinery is to be reduced by 10 %.
- (6) Market value of building is ₹ 70,000.
- (7) Market value of investments is ₹ 68,950.
- (8) Total capital of the old partners Jaini and Aanya after all adjustments will be maintained in their relative new ratio. For this purpose necessary adjustments will be made through bank.

Prepare necessary accounts and balance sheet.

19. Tapu and Sonu are the partners sharing profit and loss in the ratio of 1:2. The balance sheet of their firm as on 31-3-2016 was as under :

Balance Sheet

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capital account :		Goodwill	54,000
Tapu 2,00,000		Land-Building	3,00,000
Sonu 3,00,000	5,00,000	Machinery	1,00,000
Profit-loss A/c	48,000	Stock	40,000
Creditors	50,000	Debtors	80,000
Bad debt reserve	16,000	Cash	40,000
	6,14,000		6,14,000

They admitted Goli as a new partner on the following terms :

- (1) Goodwill is valued at ₹ 54,000.
- (2) Bad debt reserve on debtors to be maintained at ₹ 10,000.
- (3) Land-building is to be increased by 10 %.
- (4) Book value of machinery is 25 % more than its market value.
- (5) Value of stock is to be reduced by 10 %.
- (6) Goli will bring his capital equal to 50 % of net assets of the new firm.
- (7) Goli will bring his share of goodwill in cash.
- (8) Tapu sacrifices $\frac{1}{3}$ rd of his profit share and Sonu sacrifices $\frac{1}{6}$ share for Goli.

Prepare the necessary accounts and balance sheet. Also determine new profit-loss sharing ratio of all the three partners.

20. Meet, Jeet and Neel are the partners sharing profit and loss in the ratio of 3:2:1. The balance sheet of their firm as on 31-3-2017 was as under :

Balance Sheet

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Capital account :			Building		1,00,000
Meet	1,00,000		Machinery		80,000
Jeet	75,000		Investment		60,000
Neel	50,000	2,25,000	Debtors		40,000
General reserve		12,000	Stock		64,000
Investment fluctuation reserve		20,000	Cash		26,000
Workmen compensation reserve		15,000			
Workmen profit sharing fund		35,000			
Workmen saving account		40,000			
Creditors		23,000			
		3,70,000			3,70,000

On the above date they admitted Heer as a new partner on the following conditions :

- (1) Meet sacrificed $\frac{1}{8}$ th share and Neel sacrificed $\frac{1}{24}$ th share from their profit in favour of Heer.
- (2) Goodwill is valued at ₹ 60,000. Heer will bring her share of goodwill in cash.
- (3) Market value of investment is ₹ 52,000, which is to be shown in books.
- (4) Claim for workmen compensation is accepted at ₹ 18,000.
- (5) Market value of machinery is ₹ 60,000 and market value of building is ₹ 1,26,000 which are to be brought in the books.
- (6) Heer will bring ₹ 50,000 as her capital in cash.
- (7) Capital of the partners shall be proportionate to their new profit sharing ratio, taking Heer's capital as base. Necessary effect is to be given in cash.

Prepare the necessary account and balance sheet after admission of Heer.

Retirement / Death of a Partner

1. Introduction	7. Distribution of Reserves and Accumulated Profit-Losses
2. Circumstances of Retirement of a Partner	8. Determination of Amount Payable to the Retiring Partner
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4. Calculation of New Profit and Loss Sharing Ratio and Gaining Ratio	— Exercise
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1. Introduction

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

2. Circumstances of Retirement of a Partner

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

(A) As per Indian Partnership Act

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

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

- (1) Unanimously : Any partner can retire by unanimous consent of all the partners.
- (2) By notice : A partner has right to retire from the firm by giving notice to other partners in writing indicating his intention of retirement from the firm.
- (3) By contract : Any partner can retire as per the conditions of the partnership deed.
- (4) Insolvency of a partner : A partnership of any partner ends from the date from which he is declared insolvent.
- (5) Death of a partner : Partnership ends automatically due to the death of a partner.
- (6) Expulsion by other partners : Subject to provision in partnership deed, a partner can be expelled by other partners.

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

3. Important Accounting Aspects and Accounting Treatments

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

- (1) Calculation of new profit-loss sharing ratio and calculation of gaining share of continuing partners.
- (2) Valuation of goodwill and its accounting treatment.
- (3) Revaluation of assets and liabilities.
- (4) Distribution of accumulated reserves and balances of undistributed profits and losses.
- (5) Determination of amount payable to the retiring or deceased partner.
- (6) Payment of amount due to the retiring or deceased partner.

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

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

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

$$\therefore \text{New share} = \text{Old share} + \text{Gain and}$$

$$\text{Gain} = \text{New share} - \text{Old share}$$

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

- (1) When gaining ratio or gain is not given, means old ratio is continued
- (2) When gaining share of continuing partners is given
- (3) When gaining ratio of continuing partners is given
- (4) When old and new profit and loss sharing ratios are given

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

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

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

- if
- (i) M retires
 - (ii) N retires
 - (iii) O retires

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

- (i) If M retires new profit and loss sharing ratio between N and O will be 3:2.
- (ii) If N retires then new profit and loss sharing ratio of M and O will be 4:2 that is 2:1.
- (iii) If O retires then new profit and loss sharing ratio of M and N will be 4:3.

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

Gain = New share – Old share

When M retires :

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

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

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

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

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

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

- if
- (i) M retires
 - (ii) N retires
 - (iii) O retires

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

- (i) If M retires then new profit and loss sharing ratio of N and O = 3:2.
- (ii) If N retires then new profit and loss sharing ratio of M and O = 4:2 means 2:1.
- (iii) If O retires then new profit and loss sharing ratio of M and N = 4:3.

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

$$\text{Gain} = \text{New share} - \text{Old share}$$

Under circumstances (i) if M retires,

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

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

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

∴ Gain = New share – Old share

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

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

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

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

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

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

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

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

$$\text{New share} = \text{Old share} + \text{Gain}$$

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

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

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

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

$$\text{New share} = \text{Old share} + \text{Gain}$$

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

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

∴ New profit and loss sharing ratio of X and Z = 11:7

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

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

Gaining share of continuing partner = Share of the retiring partner ×

gaining share given to the respective partners

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

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

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

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

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

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

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

New share = Old share + gain

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

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

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

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

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

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

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

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

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

New share = Old share + Gain

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

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

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

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

New share = Old share + Gain

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

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

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

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

Illustration 5 : P, Q and R are the partners sharing profit and loss in the ratio of $\frac{1}{4}$, $\frac{1}{3}$ and $\frac{5}{12}$.

Q retires. P and R decided to distribute Q's share in the ratio of 2:1. Calculate profit-loss sharing ratio of P and R.

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

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

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

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

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

Now, New share = Old share + Gain

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

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

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

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

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

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

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

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

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

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

\therefore Gaining ratio is 1:3.

New share = Old share + Gain

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

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

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

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

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

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

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

$$\text{New share} = \text{Old share} + \text{Gain}$$

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

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

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

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

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

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

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

$$\text{New share} = \text{Old share} + \text{Gain}$$

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

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

$$\begin{aligned} \therefore \text{New share of profit and loss sharing ratio} &= \frac{6}{10} : \frac{4}{10} \\ &= 6:4 \text{ means } 3:2 \end{aligned}$$

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

$$\text{Gain} = \text{New share} - \text{Old share}$$

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

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

U retires.

New sharing ratio of P and A = 2:1

$$\text{Gain} = \text{New share} - \text{Old share}$$

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

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

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

5. Accounting Treatment of Goodwill

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

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

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

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

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

To goodwill A/c

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

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

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

To retiring/deceased partners' capital A/c

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

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

Ans. :

Journal Entries

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

Explanation (1) : Gaining ratio :

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

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

Gain = New share – Old share

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

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

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

∴ Gaining ratio of C, W and A = 1:2:1

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

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

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

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

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

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

Ans. :

Journal Entries

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

Calculation 1 : Gaining ratio :

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

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

Gain = New share – Old share

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

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

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

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

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

Goodwill receivable by A :

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

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

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

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

T and S will give in their gaining ratio

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

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

∴ Gaining ratio of T and S = 3:2

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

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

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

Ans. :

Journal Entries

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

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

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

Goodwill payable to B = ₹ 30,000

(2) : Gaining ratio :

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

New ratio of R and T = 3:2

Gain = New share — Old share

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

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

∴ Gaining ratio of R and T = 8:7

6. Revaluation of Assets and Liabilities

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

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

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

7. Distribution of Reserves and Accumulated Profit-Losses

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

8. Determination of Amount Payable to the Retiring Partner

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

- (1) Following amounts are credited to the retiring partners' capital account :
 - (i) Opening balance of capital account and credit balance of current account on the date of retirement.
 - (ii) Share in profit of revaluation account

- (iii) Share in reserves and undistributed profit
 - (iv) Share in new value of goodwill
 - (v) Share in profit of the firm from the date of last balance sheet to the date of retirement.
 - (vi) Salary, commission, interest on capital, interest on loan given to the firm from the date of last balance sheet to the date of retirement. (If rate of interest on the partners' loan is not given; interest is payable on the partner's loan at the rate of 6 % p.a. till the date of retirement.)
- (2) Following balances reduce capital, therefore they are debited to his capital account :
- (i) Debit balance of current account
 - (ii) Drawings
 - (iii) Interest on drawings till the date of retirement
 - (iv) Share in undistributed loss and deferred revenue expenditure (fictitious assets)
 - (v) Share in old goodwill appearing in the books of the firm
 - (vi) Share in loss of revaluation account
 - (vii) Loan given by the firm to the retiring partner

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

Retiring partners' capital A/c...Dr

To cash A/c

To retiring partners' loan A/c

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

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

Balance Sheet

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

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

- (1) Land and Building is to be valued at ₹ 2,20,000.
- (2) Value of machinery is to be reduced by ₹ 30,000.
- (3) The provision for doubtful debts is to be kept at 10 %.
- (4) Liability for workmen compensation is accepted at ₹ 15,000.
- (5) Goodwill of the firm is valued at ₹ 1,60,000. Y's share in goodwill is to be adjusted through the capital account of X and Z.
- (6) The new ratio of profit and loss sharing of X and Z is decided at 1:1. From the above information pass necessary journal entries and prepare revaluation account, partners' capital account and balance sheet after the retirement of Y.

Ans. :

Journal Entries

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

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

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

Revaluation Account

Dr

Cr

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

Partners' Capital Accounts

Dr

Cr

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

Balance Sheet as on 1-4-2016 After Retirement

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

Explanation : (1) Gaining ratio of continuing ratio

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

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

$$\text{Gain} = \text{New share} - \text{Old share}$$

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

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

\therefore Gaining ratio of X and Z = 1:2

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

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

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

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

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

Journal Entry

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

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

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

Revaluation A/c Dr...	5000
-----------------------	------

To Workmen compensation claim A/c	15,000
-----------------------------------	--------

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

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

Balance Sheet

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

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

- (1) The claim of workmen compensation is accepted at ₹ 20,000.
- (2) The market value of investment is ₹ 45,000.
- (3) Bad debts on debtors ₹ 2000 is to be written off and the provision for doubtful debts is to be kept at 5 %
- (4) Fixed assets to be appreciated by 20 %.
- (5) The book value of stock is over valued by ₹ 600 compared to its cost. The cost of stock is to be recorded.
- (6) The value of goodwill of the firm is ₹ 1,00,000.
- (7) Ajay is to be paid ₹ 10,000 in cash.
- (8) The new profit and loss sharing ratio of Alpa and Amay is 1:4.

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

Ans. :

Revaluation Account

Dr

Cr

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

Partners' Capital Accounts

Dr

Cr

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

Balance Sheet as on 1-4-2017 After Retirement

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

Explanation (1) : Gaining ratio :

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

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

Gain = New share – Old share

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

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

(2) : Calculation of goodwill :

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

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

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

Journal Entries

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

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

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

Investment fluctuation fund A/c Dr... 20,000

To Investments A/c 15,000
To Ajay's capital A/c 2500
To Alpa's capital A/c 1500
To Amay's capital A/c 1000

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

Workmen compensation reserve A/c Dr... 30,000

To workmen compensation claim A/c 20,000
To Ajay's capital A/c 5000
To Alpa's capital A/c 3000
To Amay's capital A/c 2000

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

Balance Sheet

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

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

- (1) The value of machinery is to be increased by 10 %.
- (2) The value of trademark is to be reduced upto 40 %.
- (3) Bad debt reserve on debtors is to be kept at 15 %.
- (4) Discounted bills receivable of ₹ 1300 which is dishonoured on due date, 31-3-2017. No amount is received from the debtors.
- (5) Goodwill of the firm is valued at ₹ 60,000.
- (6) The new profit-loss sharing ratio of Gopi and Krishna is 2:1.

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

Ans. :

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

Current Accounts of Partners

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

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

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

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

$$\text{Gain} = \text{New share} - \text{Old share}$$

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

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

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

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

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

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

Revaluation A/c Dr...	1300	
To Bank A/c		1300

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

Complete amount means, reduce upto 60 %.

9800 10,800 7200

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

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

Ans. :

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

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

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

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

$$\begin{aligned}
 \text{P's new capital} &= ₹ 1,40,000 \times \frac{3}{5} \\
 &= ₹ 84,000
 \end{aligned}$$

$$\begin{aligned}
 \text{V's new capital} &= ₹ 1,40,000 \times \frac{2}{5} \\
 &= ₹ 56,000
 \end{aligned}$$

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

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

Capital brought Capital paid

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

Journal Entries

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

Capital Accounts of Partners

Dr

Cr

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

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

Illustration 18 : A, B and C are the partners sharing profit and loss in the ratio of 4:3:2 respectively.

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

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

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

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

Total capital of new firm : B's capital = ₹ 80,000

C's capital = ₹ 90,000

Additional capital (Payable to A) = ₹ 30,000

Total capital of new firm = ₹ 2,00,000

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

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

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

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

Journal Entries

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

Dr **Capital Accounts of Partners** Cr

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

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

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

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

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

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

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

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

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

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

To make payment to A = ₹ 60,000

Less : Available cash for payment to A = ₹ 10,000

(₹ 30,000 – ₹ 20,000 cash to be maintained)

Cash brought in by B and C	₹ 50,000
----------------------------	----------

Total capital of new firm of B and C :

B's capital =	₹ 50,000	
+ C's capital =	₹ 70,000	
+ Additional capital =	₹ 50,000	(Necessary cash balance to maintain minimum cash balance and to pay dues of 'A')
Total capital of B and C =	₹ 1,70,000	

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

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

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

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

Journal Entries

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

Capital Accounts of Partners

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

Cash Account

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

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

Balance Sheet

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

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

- (1) The new profit-loss sharing ratio of Karan and Fenil is to be kept at 2:3.
- (2) Goodwill of the firm is to be valued at ₹ 80,000.
- (3) Paid ₹ 60,000 for patents during current year which is for total 4 years.
- (4) Machinery is to be depreciated by 10 %.
- (5) Bad debt on debtors is to be written off ₹ 3,000.
- (6) ₹ 20,000 is to be paid to Farshid.
- (7) Market value of stock is ₹ 54,000.

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

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

Ans. :

Revaluation Account

Dr

Cr

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

Capital Accounts of Partners

Dr

Cr

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

Bank Account

Dr

Cr

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

Balance Sheet as on 1-4-2017 After Retirement

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

Explanation : (1) Distribution of goodwill

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

Gain = New share – Old share

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

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

$$\therefore \text{Goodwill payable by Fenil} = ₹ 80,000 \times \frac{3}{10} = ₹ 24,000$$

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

$$\text{Goodwill receivable by Karan} = \frac{1}{10} \times 80,000 = ₹ 8,000$$

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

Journal Entries : Fenil's capital A/c...Dr 24,000

To Karan's capital A/c 8,000

To Farshid's capital A/c 16,000

(2) Distribution of capital of new firm

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

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

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

Balance Sheet

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

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

- (1) M's share is to be distributed between L and N in the ratio of 3:2.
- (2) Bad debt of ₹ 8000 is to be written off and provision for bad debt is to be kept at 10 % and provision for discount reserve is to be kept at 5 % on debtors.
- (3) Market value of investment is ₹ 50,000.
- (4) Market value of building is ₹ 2,50,000.
- (5) Write off ₹ 1560 from furniture.
- (6) The capital of L and N is to be kept in their new profit and loss sharing ratio and all necessary adjustments to be made through their current account.
- (7) The value of goodwill of the firm is ₹ 50,000.
- (8) N accepts creditors of ₹ 5500 to pay.

Prepare necessary accounts and prepare balance sheet after retirement also :

Ans. :

Revaluation Account

Dr

Cr

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

Capital Accounts of Partners

Dr

Cr

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

Balance Sheet as on 1-4-2016 After Retirement

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

Explanation : (1) Distribution of goodwill

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

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

∴ Gaining ratio of L and N = 3:2

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

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

Journal Entries :

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

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

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

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

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

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

New share = Old share + Gain

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

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

∴ New ratio = 29:21

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

Capital of L (₹ 1,90,000 – ₹ 17,000) = ₹ 1,73,000

Capital of N (₹ 1,03,000 – ₹ 12,000) = ₹ 91,000

Total capital of new firm = ₹ 2,64,000

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

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

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

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

Balance Sheet

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

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

- (1) Goodwill is to be valued at 3 times the average profit of last five years.
- (2) Value of land and building is ₹ 15,000.
- (3) Market value of X Ltd.'s share is ₹ 1200.
- (4) All debtors are good.
- (5) A provision of ₹ 2000 for outstanding salary is to be made.
- (6) Last four years profit of the firm was as under :

2011-12	₹ 6000
2012-13	₹ 2000
2013-14	₹ 3000
2014-15	₹ 2000
- (7) Share of R will be gained by P.
- (8) Amount due to R is to be paid in cash which is brought in by P and Q in such a way as to make their capitals in proportionate to their new profit and loss sharing ratio.

Prepare necessary accounts and new balance sheet.

Ans. :

Revaluation Account

Dr

Cr

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

Capital Accounts of Partners

Dr

Cr

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

Cash-Bank Account

Dr

Cr

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

Balance Sheet as on 1-4-2016 After Retirement

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

Explanation : (1) Valuation and distribution of goodwill

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

$$\text{Goodwill} = ₹ 2000 \times 3 = ₹ 6000$$

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

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

∴ P gives goodwill to R.

Journal Entries :

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

(2) New profit-loss sharing ratio

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

R retires and his share is gained by P.

New share = Old share + Gain

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

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

∴ New profit-loss sharing ratio = 2:1

(3) New capital of P and Q

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

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

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

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

Balance Sheet

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