CA FOUNDATION

MARATHON

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Accounting: Part 3

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CA FOUNDATION MARATHON (SUPER REVISION/ONE SHOT)

ACCOUNTING

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Partnership:

Introduction

INTRODUCTION TO PARTNERSHIP ACCOUNTS

DEFINITIONS

Partnership	Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all.
Partners	Persons who have entered into Partnership with one another are individually called Partners.
Firm	Persons who have entered into Partnership with one another are collectively called firm
Firm Name	The name under which their business is carried on is called the Firm Name

FEATURES OF PARTNERSHIP

Persons	It requires at least two persons to form a Partnership.
Agreement	An agreement is entered by all the persons concerned, setting out the terms and conditions under which the Partnership is based. When this agreement is set out in writing, it is called the "Partnership Deed".
Business	A partnership can exist only in business. Thus, it is not the agreement alone which creates a partnership. A partnership comes into existence only when partners begin to carry on business in accordance with their agreement
Mutual Agency	The activities of the business will be carried on/managed by all or any one of them acting for all. This principle of mutuality is the essence of Partnership agreement
Sharing of Profit/loss	The Partners share the profits and losses of the business in the agreed ratio.
Minor as a Partner	A minor can be added in partnership firm. But the condition is that he can be admitted to share profit only. He cannot be made to share losses of the firm.

Number of Partners:

Minimum Partners: Two

Maximum Partners: As per Section 464 of Companies Act, 2013, no association or partnership consisting of more than such number of persons as may be prescribed shall be formed for the purpose of carrying on any business which shall not exceed 100. Prescribed limit is 50. Thus, maximum number of members in a partnership firm are 50.

PARTNERSHIP DEED & CONTENTS

Meaning	Partnership Deed is the written agreement containing the terms and conditions under which the Partnership will sustain or exist.
Contents of Partnership Deed	❖ Name of the firm and the nature of the Partnership Business. ❖ Commencement and Tenure of the Business (e.g. Partnership at Will, etc.) ❖ Amount of Capital to be contributed by each Partner. ❖ Ratio for sharing the Profit/Loss of Partnership business. ❖ Arrangement in respects of Drawings by Partners and limits thereon.

	❖ Interest to be credited on the Capital Account of Partners. ❖ Interest to be charged on Drawings of Partners ❖ Remuneration to Partners & the basis of determining such remuneration e.g. Commission as a percentage of Firm's Turnover, other conditions etc. ❖ Process of setting disputes that may arises among the Partners. ❖ Procedure for maintenance of Books of Accounts ❖ Audit of Books of Accounts ❖ Manner of valuation of Goodwill in case of admission of new partners, retirement of existing partners and death of a Partner. ❖ Procedure for settlement of Partners' claims in case of retirement/death ❖ Procedure for dissolution of Partnership
Notes	❖ When partnership deed is not registered a partnership firm is allowed to carry on business subject to certain disabilities. ❖ It is not mandatory to have a written agreement in all cases. Further, even in cases where there is a written Partnership Deed, it is not compulsory to have it registered.

DISTINCTION BETWEEN PARTNERSHIP & LIMITED LIABILITY PARTNERSHIP

BASIS	PARTNERSHIP	LIMITED LIABILITY PARTNERSHIP
Applicable Law	Indian Partnership Act 1932	The Limited Liability Partnerships Act, 2008
Registration	Optional	Compulsory
Creation	Created by an Agreement	Created by Legal process
Separate Legal Entity	No	Yes
Name	No guidelines. The partners can have any name as per their choice	Name of LLP to contain word limited liability partners (LLP) as suffix.
Perpetual Succession	Partnerships do not have perpetual succession	It has perpetual succession and individual partners may come and go
Number of Partners	Minimum 2 and Maximum 50	Minimum 2 but no maximum limit
Designated Partners	There is no provision for such partners under the Partnership Act, 1932.	At least two designated partners and atleast one of them shall be resident in India.
Legal compliances	All partners are responsible for all the compliances and penalties under the Act.	Only designated partners are responsible for all the compliances and penalties under this Act
Liability of Partners / Members	Liability of each partner is unlimited. It can be extended upto the personal assets of the partners.	Liability of each partner limited to the extent to agreed contribution except in case of willful fraud.

REMUNERATION, INTEREST ON CAPITAL, LOAN, DRAWINGS, PROFIT SHARING RATIO

1. Governing Statute: The law governing Partnership in India is the Partnership Act, 1932.
2. Conditions not covered by Partnership Deed: Where any situation or circumstance is not covered by the Partnership Deed or is not adequately provided for in the Partnership Deed, the Provision of the Partnership Act, 1932 will apply.

If the Deed is silent on-	Provisions of the Partnership Act
Partners' Remuneration/ Salary/Commission	No Remuneration will be allowed.
Interest on Partners' Capital	No IOC will be allowed to any Partner.
Interest on loan given by Partner to Firm	Maximum 6% p.a. can be allowed on loan.
Interest on Partners' Drawings	No interest will be charged.
Profit Sharing Ratio	Profits and Losses will be shared equally.

PARTNER'S CAPITAL ACCOUNTS

Aspects	Fluctuating Capital Method	Fixed Capital Method
Ledger A/cs prepared	Partner's Capital Account.	1. Partner's Capital Account, and 2. Partner's Current Account.
Initial Capital contribution	Amount brought in or contribution is credited to Partner's Capital A/c	Amount brought in or contributed is credited to Partners' Capital A/c
Subsequent transactions	Subsequent transactions are accounted in Partner's Capital A/c	Subsequent transactions are accounted in Partner's Current A/c

FORMAT OF PARTNER'S CAPITAL ACCOUNT

Particulars	A	B	C	Particulars	A	B	C
To Cash/Bank (Withdrawal of capital, if any) To Balance c/d				By Balance b/d By Cash/ Bank/ Assets (Capital Contribution)			
Total				Total			

FORMAT OF PARTNER'S CURRENT ACCOUNT

Particulars	A	B	C	Particulars	A	B	C
To Balance b/d To Drawings A/c To P&L A/c - Share of Loss To P&L Appropriation -Interest on Drawings To Balance c/d				By Balance b/d By P&L Appropriation -Remuneration/ Salary etc. -Interest on Capital -Share of Profit By Balance c/d			
Total				Total			

Note: If Capital Accounts are maintained on Fluctuating basis, all the above entries will be made in one single Capital Account only. There will not be any Current Account.

PROFIT & LOSS APPROPRIATION ACCOUNT

1. Purpose: Profit & Loss A/c of firm will show the profit earned or loss suffered by the firm. To distribute the Profit properly to the Partners, the Profit & Loss Appropriation A/c is used
2. Features:
   (a) It is an extension of P&L Account.
   (b) It is applicable only for Partnership Firm, and not Sole Proprietary Concerns.
   (c) It provides details of how Net Profit for the period has been distributed to the Partners.
   (d) The entries in P&L Appropriation A/c are governed by the Partnership Deed.

Note: Interest on Partners' Loan, Rent for use of Partners' premises, if any, etc. are debited to P&L A/c itself. Net Profit after charging & debiting these items, is only tfd. to P&L App. A/c.

3. Format:

Dr. Profit & Loss Appropriation A/c Cr.

Particulars	Amount ₹	Particulars	Amount ₹
To Interest on partner's capital A --- B ---	XX	By P&L A/c balance (Profit)	XX
To Partner's Salary A --- B ---	XX	By Interest on partner'sdrawings A --- B ---	XX
To Partner's Commission/Bonus A --- B ---	XX		
To Reserves (Amount transferred)	XX		
To Profits transferred in PSR: A --- B ---	XX		
Total	XXXX	Total	XXXX

CALCULATION OF REMUNERATION / SALARY / COMMISSION TO PARTNERS

Remuneration/ Salary/ Commission to Partners, can be provided to Partners, only if the Partnership Deed so provides. The calculations are as under:-

Type of Capital	Computation
1. Remuneration/ Salary	Remuneration / Salary p.a. = Monthly Amount x No. of months
2. Commission as x % of Turnover	Commission p.a. = Sales Turnover of the Firm x Rate of Commission
3. Commission as x % of Net Profit (a) Before Commission (b) After Commission	 Net Profit before Commission x Rate of Commission /100 Net Profit before Commission x $\frac{\text{Rate of Commission}}{(100+\text{Rate of Commission})}$

INTEREST ON PARTNERS' CAPITAL

Type of Capital	Computation of Interest on Capital (IOC)
1. Opening Capital	IOC= Opening Capital x Rate of Interest
2. Additional Capital	IOC= Additional Capital x Rate of Interest x Period of use

Example:

Ramesh & Naresh are partners in a firm. Their Capitals as on 1st April of a financial year were ₹ 3,00,000 and ₹ 1,20,000 respectively. They share profits equally. On 1st July, they decided that their Capitals should be ₹ 2,00,000 each. The necessary adjustment in the capitals was made by introducing or withdrawing cash. Interest on Capital is allowed at 8% p.a.
Compute the interest on capital for both Partners for the year ending 31st March.

1/4 —— 3M —— 1/7 —— 9M —— 31/3

R: 300000
N: 120000

1/7: 200000, (100000), + 80000

Ramesh

$(300000 \times 8\% \times \frac{3}{12}) + (200000 \times 8\% \times \frac{9}{12})$
$6000 + 12000 = 18000$

$(300000 \times 8\%) - (100000 \times 8\% \times 9/12)$
$24000 - 6000 = 18000$

Naresh

$(120000 \times 8\% \times \frac{3}{12}) + (200000 \times 8\% \times \frac{9}{12})$
$= 2400 + 12000 = 14400$

$(120000 \times 8\%) + (80000 \times 8\% \times \frac{9}{12})$
$9600 + 4800 = 14400$

Interest on Capital in case of Insufficient Profits or Loss

It is an appropriation. It will be paid to the partners if provided for in the agreement but only from profits. The treatment in different situations is as under-

Interest on Capital

- Deed is silent or No Deed → No IOC
- Deed provides for IOC
  - In case of loss → No IOC
  - In case of Profit
    - Sufficient Profits (Profits ≥ IOC) → Full IOC
    - Insufficient Profits (Profits < IOC) → Profits distributed in ratio of capital
- Deed provides for IOC & specifically states it to be charge against profit → Full IOC even if there is loss.

Example:

X and Y are Partners sharing profits and losses in the ratio of 2:3 with a capital of ₹ 2,00,000 and ₹ 1,00,000 respectively. Show the distribution of profits/losses for the year ended 31st March, in each of the following cases-

Case 1: If Partnership Deed provides for IOC at 6% p.a. and profits for year is ₹ 21,000.

Case 2: If Partnership Deed provides for IOC at 6% p.a. and profits for year is ₹ 15,000.

Interest on capital:
X = 2L × 6% = 12000
Y = 1L × 6% = 6000
2:1

Case 1: Profits = 21000

IOC X 12000
Y 6000
18000

Remaining Profit 3000
X 2/5: 1200
Y 3/5: 1800

Case 2: Profits 15000

18000	15000
	Loss 3000

15000 divided in ~~IOC~~ Capital Ratio 2:1
X 10000
Y 5000

Effective Capital

Partners may agree to share profits and losses in the capital ratio. When capitals are fixed, profits will be shared in the ratio of given capitals. But if capitals are fluctuating and partners introduce or withdraw capitals during the year, the capitals for the purpose of ratio would be determined with reference to time on the basis of weighted average method.

Example:

A and B formed a partnership with a capital contribution of ₹ 1,00,000 & ₹ 80,000 respectively on 1st January 2023. The profits were to be shared in the Capital /Effective Capital ratio. Calculate effective capital, profit sharing ratio & Interest on capital @ 6% p.a.

Date	Capital Introduced		Capital Withdrawn	
	A	B	A	B
1st April	2,00,000			
1st July		40,000	1,00,000	

A

1/1 $100000 \times \frac{12}{12} = 100000$

1/4 $200000 \times \frac{9}{12} = 150000$

1/7 $(100000) \times \frac{6}{12} = (50000)$

200000

B

1/1 $80000 \times \frac{12}{12} = 80000$

1/7 $40000 \times \frac{6}{12} = 20000$

100000

Effective cap. = 200000 & 100000

Ratio = 2:1

IOC A = 2L × 6% = 12000

B = 1L × 6% = 6000

INTEREST ON PARTNERS' DRAWINGS

- Drawings refers to amount withdrawn by Partners, in cash or kind, for their personal use.
- Partners are supposed to pay interest on drawings only when provided by the agreement or agreed by the partners.
- Interest on drawings is gain for the business. It is recorded on credit side of P&L Appropriation A/c.
- Partner's Drawings A/c & interest on drawings is closed by transferring to debit side of Capital or Current A/c.

Interest on Drawings

- Dates of Drawings not given
  - P.a. → $IOD = Drawings \times \frac{Rate}{100} \times \frac{6}{12}$
  - ~~P.a.~~ → $IOD = Drawings \times \frac{Rate}{100}$
- Dates of Drawings given
  - Amount of each drawing same $\boxed{\text{and}}$ Time interval b/w 2 drawings same
    - Direct Method
    - Product Method
    - Shortcut Method (Preferable)
  - Either amount not same $\boxed{\text{or}}$ Time interval not same
    - Direct Method
    - Product Method (Preferable)
    - Shortcut Method (x)

Short Cut Method

$$IOD = Total\ Drawings \times \frac{Rate}{100} \times \frac{Average\ Time\ Period^{*}}{12}$$

* Average Time Period

TTP = Total Time Period

TI = Time Interval

Beginning	Middle	End
$\frac{TTP+TI}{2}$	$\frac{TTP}{2}$	$\frac{TTP-TI}{2}$

A) 12 Months Period

	Beginning	Middle	End
a) Monthly	$\frac{12+1}{2} = 6.5$	$\frac{12}{2} = 6$	$\frac{12-1}{2} = 5.5$
b) Quarterly	$\frac{12+3}{2} = 7.5$	$\frac{12}{2} = 6$	$\frac{12-3}{2} = 4.5$

Example:

Compute interest on partners' Drawings in the following situations, if interest rate is 6% p.a. (Financial year of the firm ends on 31st December)

Date of withdrawal	Feb 1	May 1	June 30	Oct 31st
Amt. withdrawn (₹)	20,000	50,000	40,000	60,000

$\boxed{\text{Direct}}$ | **Product Method**

Date	Amount	Interest on drawings	Product
1/2	20,000	$20000 \times 6\% \times \frac{11}{12} = 1100$	$20000 \times 11 = 220000$
1/5	50,000	$50000 \times 6\% \times \frac{8}{12} = 2000$	$50000 \times 8 = 400000$
30/6	40,000	$40000 \times 6\% \times \frac{6}{12} = 1200$	$40000 \times 6 = 240000$
31/10	60000	$60000 \times 6\% \times \frac{2}{12} = 600$	$60000 \times 2 = 120000$
		4900	980000

$IOD = 980000 \times 6\% \times \frac{1}{12}$

$= 4900$

Example:

Compute interest on partners' Drawings if interest rate is 10% p.a.-

a) • Drawings during the entire year ₹ 2,50,000 (details of withdrawal not available)

b) • Drawings during the entire year ₹ 2,50,000, & interest is to be calculated without reference to time factor (i.e., interest on drawing at 10% and not 10% p.a.)

a) $IOD = 250000 \times \frac{10}{100} \times \frac{6}{12} = 12500$

b) $IOD = 250000 \times \frac{10}{100} = 25000$

Example:

Compute interest on partners' Drawings if interest rate is 10% p.a.-

• ₹ 10,000 withdrawn per month, throughout the year, at – (a) beginning of each month, (b) middle of each month, and (c) end of each month.

Beginning $(10000 \times 12) \times 10\% \times \frac{6.5}{12} \Rightarrow 6500$ $\rightarrow \frac{12+1}{2}$

Middle $120000 \times 10\% \times \frac{6}{12} = 6000$ $\rightarrow 12/2$

End $120000 \times 10\% \times \frac{5.5}{12} = 5500$ $\rightarrow \frac{12-1}{2}$

PAST ADJUSTMENTS IN CAPITAL ACCOUNTS OF PARTNERS

Sometimes few errors & omissions in recording of transactions or the preparation of financial statements are found after final accounts have been prepared & profits distributed among partners. These omissions and errors may be in respect of:

- Interest on capitals,
- Interest on drawings,
- Partner's salary, partner's commission or
- There may also be some changes in the provisions of partnership deed or system of accounting having impact with retrospective effect.

All these acts of omission and commission need adjustments for correction.

Now instead of altering all the old accounts, necessary adjustments can be made either;

- ❖ Through Profit and Loss Adjustment Account, or
- ❖ Directly in the Capital Accounts of the concerned partners.

Journal entry for adjustment is:

Gaining partner capital/current A/c Dr.

To Sacrificing Partner capital/current A/c

TABLE

	A	B	Total
Items to be Recorded			
IOC	✓	✓	✓
Salary, Commission, etc.	✓	✓	✓
Share of Profit	✓	✓	✓
IOD	(✓)	(✓)	(✓)
CR.	✓	✓	✓
Items to be Reversed			
IOC	✓	✓	✓
Salary, Commission, etc.	✓	✓	✓
Share of Profit	✓	✓	✓
IOD	(✓)	(✓)	(✓)
DR.	✓	✓	✓
Difference	✓	✓	

Example:

A, B and C are partners in a firm sharing profits and losses in the ratio of 2:3:5. Their fixed capitals were ₹ 15,00,000, ₹ 30,00,000 and ₹ 60,00,000 respectively.

Case 1: For the year 2023 interest on capital @ 10% was not provided.

Case 2: For the year 2023 interest on capital was credited to them @ 12% instead of 10%.

Pass entry to rectify the error.

Case 1

	A	B	C
IOC to be credited	150000	300000	600000
Share of Profit to be reversed (1050000 in 2:3:5)	(210000)	(315000)	(525000)
	60000 Dr	15000 Dr	75000 Cr.

A's current A/c - Dr 60000

B's current A/c - Dr 15000

To C's current A/c 75000

Case 2

	A	B	C
IOC to be debited @ 2%	(30000)	(60000)	(120000)
Profit to be credited (210000 in 2:3:5)	42000	63000	105000
	12000 Cr.	3000 Cr.	15000 Dr.

C's curr. A/c - Dr 15000

To A's curr. A/c 12000

To B's curr. A/c 3000

GUARANTEE OF MINIMUM PROFIT TO A PARTNER

1. Meaning: Sometimes, Partners may mutually agree that certain Partner (s) has the right to have minimum amount of profit. Such profit is called Guaranteed Profit or Guaranteed Minimum Profit.

Example: Guarantee given to a partner 'X' by the other partners 'Y & Z' means in case of loss or insufficient profits 'X' will withdraw the minimum guaranteed amount.

2. Treatment:

Situation	Steps in Computation/ Treatment
(a) If Profit Share > Guaranteed Profit	Distribute the Total Available Profit in the agreed profit sharing ratio, in the usual manner.
(b) If Profit Share < Guaranteed Profit	• Distribute the Total Available Profit in the agreed profit sharing ratio, in the usual manner. • Compute the shortfall in Guaranteed Profit, and add that to the share of the Partner entitled to the same. • Deduct the shortfall from the Profit shares of the Other Partners, as described below

Burden of Shortfall:

Guarantee given by	Shortfall to be reduced from
(a) One of the remaining partners	That Remaining Partner's Share of Profit
(b) Remaining 2 or all Partners in agreed ratio	Two or all Partners, in agreed ratio
(c) Remaining Partners in their mutual PSR	All remaining Partners in mutual PSR

Note: If the question is silent about nature of guarantee, situation (c) given above is assumed

Example

A, B & C partners with PSR 5:3:2. Guarantee given to Partner C of amount 50,000.
Guarantee given by:

1) A and Profits for the year 3,00,000
2) A and Profits for the year 2,00,000
3) A & B (Deficiency to be shared in mutual PSR) and Profits for the year 2,00,000
4) A & B (Deficiency to be shared in 3:2) and Profits for the year 2,00,000

(1) P = 300000

5:3:2	A	B	C
	150000	90000	60000

(2) P = 200000

5:3:2	A	B	C
	100000	60000	40000
	(10000)		+10000
	90000	60000	50000

(3) P = 300000

5:3:2	A	B	C
	100000	60000	40000
	(6250)	(3750)	10000 → A&B 5:3
	93750	56250	50000

(4) P = 300000

5:3:2	A	B	C
	100000	60000	40000
	(6000)	(4000)	10000 → A&B 3:2
	94000	56000	50000

LIMITED LIABILITY PARTNERSHIPS (LLP Act, 2008)

DEFINITIONS

LLP	a partnership formed and registered under this Act
LLP agreement	any written agreement between the partners of the LLP or between the LLP and its partners which determines the mutual rights & duties of the partners and their rights and duties in relation to that limited liability partnership.
Small LLP	Means a limited liability partnership— • the contribution of which, does not exceed 25 lakh rupees or such higher amount, not exceeding 5 crore rupees, as may be prescribed; and • the turnover of which, as per Statement of Accounts and Solvency for the immediately preceding financial year, does not exceed 40 lakh rupees or such higher amount, not exceeding 50 crore rupees, as may be prescribed

NATURE OF LIMITED LIABILITY PARTNERSHIP

1) A LLP is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.
2) A LLP shall have perpetual succession.
3) Any change in the partners of LLP shall not affect the existence, rights or liabilities of LLP

NON-APPLICABILITY OF THE INDIAN PARTNERSHIP ACT, 1932

Save as otherwise provided, the provisions of the Indian Partnership Act, 1932 shall not apply to a LLP.

MINIMUM NUMBER OF PARTNERS

Any individual or body corporate may be a partner in a LLP.
Provided that an individual shall not be capable of becoming a partner of a LLP, if

a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;
b) he is an undischarged insolvent; or
c) he has applied to be adjudicated as an insolvent and his application is pending

Every LLP shall have at least two partners.
If at any time the number of partners of a LLP is reduced below two and the LLP carries on business for more than six months while the number is so reduced, the person, who is the only partner of the LLP during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the LLP incurred during that period

DESIGNATED PARTNERS

Section 7

Every LLP shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

Provided that in case of a LLP in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such LLP or nominees of such bodies corporate shall act as designated partners.

Explanation- For the purposes of this section, the term "*resident in India*" means a person who has stayed in India for a period of not less 120 days during the immediately preceding one year.

Subject to the provisions of sub-section (1),
1) if the incorporation document-
   a) specifies who are to be designated partners, such persons shall be designated partners on incorporation; or
   b) states that each of the partners from time to time of LLP is to be designated partner, every such partner shall be a designated partner;
2) any partner may become a designated partner by and in accordance with the LLP agreement and a partner may cease to be a designated partner in accordance with LLP agreement.
3) An individual shall not become a designated partner in any LLP unless he has given his prior consent to act as such to the LLP in such form and manner as may be prescribed.
4) Every LLP shall file with the registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.
5) An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed

LIABILITIES OF DESIGNATED PARTNERS

Unless expressly provided otherwise in this Act, a designated partner shall be-
a) responsible for the doing of all acts, matters and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement and the like report pursuant to the provisions of this Act and as may be specified in the LLP agreement; and .
b) liable to all penalties imposed on the LLP for any contravention of those provisions.

LIMITATION OF LIABILITY OF AN LLP AND ITS PARTNERS

An obligation of an LLP arising out of a contract or otherwise, shall be solely the obligation of the LLP. The Liabilities of LLP shall be met out of the properties of the LLP
A partner is not personally liable, directly or indirectly, for an obligation referred to above, solely by reason of being a partner in the LLP
An LLP is not bound by anything done by a partner in dealing with a person, if: ❖ The partner does not have authority to act on behalf of LLP in doing a particular act & ❖ The other person knows that the partner has no authority or does not know or believe him to be a partner in the LLP
The liability of the LLP and the partners perpetrating fraudulent dealings shall be unlimited for all or any of the debts or other liabilities of the LLP
LLP is liable if a partner of LLP is liable to any person as a result of wrongful acts or omission on his part in the course of business of the LLP or with his authority

FINANCIAL DISCLOSURES AND RETURNS

Every LLP shall maintain such proper books of accounts as may be prescribed relating to its affairs for each year of its existence on cash basis or accrual basis and according to the double entry system of accounting and shall maintain the same at its registered office for such period as may be prescribed.
Every LLP shall within six months of the end of each financial year prepare a Statement of Account and Solvency for the said financial year as at the last day of the said financial year, in such form as may be prescribed, and such statement shall be signed by the designated partners of the LLP.
Every LLP shall file within the prescribed time, the Statement of Account and Solvency with the Registrar every year in such form and manner and accompanied by such fee as may be prescribed.
The accounts of an LLP must be audited in accordance with rules as prescribed. Provided that the Central Government may, by notification in the Official Gazette, exempt any class or classes of limited liability partnerships from the requirements of this sub-section

Question 1: (ICAI Study Material)

Ram and Rahim started business with capital of ₹ 50,000 and ₹ 30,000 on 1st January, 2023. Rahim is entitled to a salary of ₹ 400 per month. Interest is allowed on capitals and is charged on drawings at 6% per annum. Profits are to be distributed equally after the above noted adjustments. During the year Ram withdrew ₹ 8,000 and Rahim withdrew ₹ 10,000. The profit for the year before allowing for the terms of the Partnership Deed came to ₹ 30,000. Assuming Fixed capitals, Prepare Profit & Loss Appropriation Account and Capital & Current Accounts of the partners

Solution

P&L Appropriation Account

Particulars	Amount	Particulars	Amount
To Rahim's Current A/c Salary – 400*12	4,800	By P&L A/c (Net Profit)	30,000
To Interest on Capital Ram Current (50,000*6%)3,000 Rahim Current (30,000*6%)1,800	4,800	By Interest on Drawings Ram Current (8,000*6%*6/12) 240 Rahim Current(10,000*6%*6/12) 300	540
To Share of Profit (1:1) (Bal. Fig.) Ram Current 10,470 Rahim Current 10,470	20,940		
	30,540		**30,540**

Capital Accounts

Particulars	Ram	Rahim	Particulars	Ram	Rahim
To Balance c/d	50,000	30,000	By Bank A/c	50,000	30,000
	50,000	**30,000**		**50,000**	**30,000**

Current Accounts

Particulars	Ram	Rahim	Particulars	Ram	Rahim
To Drawings	8,000	10,000	By Interest on Capital	3,000	1,800
To Interest on Drawings	240	300	By Salary	-	4,800
To Balance c/d	5,230	6,770	By P&L Appropriation (Share of Profit)	10,470	10,470
	13,470	**17,070**		**13,470**	**17,070**

Question 2: (CA Foundation Dec 2021) (5 Marks)

A, B and C are partners in a firm. On 1st April 2019 their fixed capital stood at ₹ 50,000, ₹ 25,000 and ₹ 25,000 respectively. As per the provision of partnership deed:

(1) C was entitled for a salary of 5,000 p.a.

(2) All the partners were entitled to interest on capital at 5% p.a.

(3) Profits and losses were to be shared in the ratio of Capitals of the partners.

Net Profit for the year ended 31st March, 2020 of ₹ 33,000 and 31st March,2021 of ₹ 45,000 was divided equally without providing for the above adjustments.

You are required to pass an adjustment journal entry to rectify the above errors.

	A	B	C	Total
Salary to C (5000x2)			10000	10000
Int-on cap. (Capital x 5% x 2)	5000	2500	2500	10000
Share of Profit 2:1:1 (78000 - 10000 - 10000)	29000	14500	14500	58000
	34000	17000	27000	78000
Share of Profit to be debited [78000 in 1:1:1]	(26000)	(26000)	(26000)	(78000)
	8000 Cr.	9000 Dr.	1000 Cr.	

B's curr. A/c - Dr 9000
To A's curr. 8000
To C's curr. 1000

Question 3: (ICAI Study Material)

A and B are partners sharing profits and losses in the ratio of their effective capital.

They had ₹ 1,00,000 and ₹ 60,000 respectively in their Capital Accounts as on 1st January, 2023. A introduced a further capital of ₹ 10,000 on 1st April, 2023 and another ₹ 5,000 on 1st July, 2023. On 30th September, 2023 A withdrew ₹ 40,000.

On 1st July, 2023, B introduced further capital of ₹ 30,000.

The partners drew the following amounts in anticipation of profit.

A drew ₹ 1,000 per month at the end of each month beginning from January, 2023. B drew ₹ 1,000 on 30th June, and ₹ 5,000 on 30th September, 2023.

12% p.a. interest on capital is allowable and 10% p.a. interest on drawings is chargeable. Date of closing 31.12.2023.

Calculate: (a) Profit-sharing ratio; (b) Interest on capital; and (c) Interest on drawings.

Solution

Effective Capital

A = (1,00,000*12/12)+(10,000*9/12)+(5,000*6/12)- (40,000*3/12)
= 1,00,000+7,500+2,500-10,000 = 1,00,000

B = (60,000*12/12)+(30,000*6/12)
= 60,000+15,000 = 75,000

PSR = 1,00,000:75,000 = 4:3 (ratio of Effective capital)

Interest on Capital

A = 1,00,000*12%= 12,000 B = 75,000*12% = 9,000

Interest on Drawings

A = 12,000*10%*5.5/12 = 550

B = (1,000*10%*6/12)+ (5,000*10%*3/12) = 50 + 125 = 175

Question 4: (ICAI Study Material)

Weak, Able and Lazy are in partnership sharing profits and losses in the ratio of 2:1:1. It is agreed that interest on capital will be allowed @ 10% per annum and interest on drawings will be charged @ 8 % per annum. (No interest will be charged/allowed on Current Accounts).

The following are the particulars of the Capital and Drawings Accounts of the partners:

	Weak	Able	Lazy
Capital (1.1.2023)	75,000	40,000	30,000
Current Account (1.1.2023)	10,000	5,000	5,000 (Dr.)
Drawings	15,000	10,000	10,000

The draft accounts for 2023 showed a net profit of ₹ 60,000 before taking into account interest on capitals and drawings and subject to following rectification of errors:

(a) Life Insurance premium of Weak amounting to ₹ 750 paid by the firm on 30th June, 2023 has been charged to Miscellaneous Expenditure A/c.

(b) Repairs of Machinery amounting to ₹ 10,000 has been debited to Plant Account and depreciation thereon charged @ 20%.

(c) Travelling expenses of ₹ 3,000 of Able for a pleasure trip to U.K. paid by the firm on 30th June, 2023 has been debited to Travelling Expenses Account.

You are required to prepare the Profit and Loss Appropriation Account, Current Accounts of partners Weak, Able and Lazy for the year ended 31st December, 2023.

P&L A/c ✓ 10000

X 10000 X 20% = 2000

Question 5: (CA Foundation June 2023) (5 Marks)

X and Y were partners in a firm, sharing profit and losses in the ratio of 3: 2. They admit Z for 1/6th share in profits and guaranteed that his share of profits will not be less than 50,00,000. Total profits of the firm for the year ended 31st March, 2022 were 1,80,00,000. Calculate share of profit for each partner when:

(i) Guarantee is given by firm

(ii) Guarantee is given by X and Y equally.

	X	Y	Z
	90	60	30
20 in 3:2	(12)	(8)	20
	78	52	50

Solution

(i)

If Guarantee is given by firm

Profit and Loss Appropriation Account for the year ending on 31st March, 2022

Particulars	₹	Particulars	₹
To X's Capital A/c (3/5 of ₹ 1,30,00,000)	78,00,000	By Profit and Loss, A/c	1,80,00,000
To Y's Capital A/c (2/5 of ₹ 1,30,00,000)	52,00,000		
To Z's Capital A/c (1/6 of ₹1,80,00,000 or ₹ 50,00,000 whichever is more	50,00,000		
	1,80,00,000		**1,80,00,000**

(ii)

If Guarantee is given by X and Y equally

Profit and Loss Appropriation Account for the year ending on 31st March, 2022

Particulars		₹	Particulars	₹
To X's Capital A/c (3/6 of ₹ 1,80,00,000)	90,00,000		By Profit and Loss, A/c (net profits)	1,80,00,000
Less: Deficiency Borne for Z (1/2 of 20,00,000)	(10,00,000)	80,00,000		
To Y's Capital A/c (2/6 of ₹ 1,80,00,000)	60,00,000			
Less: Deficiency borne for Z (1/2 of 20,00,000)	(10,00,000)	50,00,000		
To Z's Capital A/c (1/6 of 1,80,00,000)	30,00,000			
Add: Def. Recovery from X	10,00,000			
Add: Def. Recovery from Y	10,00,000	50,00,000		
		1,80,00,000		**1,80,00,000**

OR = 3:2

Z = 1/6

Total = 1 Rem. = $1 - \frac{1}{6} = \frac{5}{6}$

$X = \frac{5}{6} \times \frac{3}{5} = \frac{3}{6}$

$Y = \frac{5}{6} \times \frac{2}{5} = \frac{2}{6}$

NR = $\boxed{3:2:1}$

Sol. 4

Computation of corrected Profit

	Net Profit (given)	60000
+	Insurance premium of partner wrongly charged to Misc. Exp. A/c	750
-	Repairs wrongly capitalised (10000 - 2000)	(8000)
+	Personal travelling exp. of partner wrongly charged to Trav. Exp. A/c	3000
		55750

P&L Appropriation A/c

To Interest on capital		By Net Profit	55750
Weak 7500		By Interest on drawings	
Able 4000		Weak 630 (15750 x 8% x 6/12)	
Lazy 3000	14500	Able 520 (13000 x 8% x 6/12)	
To Profit trf. to current A/c 2:1:1		Lazy 400 (10000 x 8% x 6/12)	1550
Weak 21400			
Able 10700			
Lazy 10700	42800		

Current A/cs

	Weak	Able	Lazy		Weak	Able	Lazy
To Bal b/d			5000	By Bal b/d	10000	5000	
To Int. on draw.	630	520	400	By Int. on cap.	7500	4000	3000
To Drawings	15000	10000	10000	By P&L App. (Share of Profit)	21400	10700	10700
To Misc. Exp.	750	–	–				
To Trav. Exp.	–	3000	–	By Bal c/d (B.f.)			1700
To Bal c/d (B.f.)	22520	6180					

Partnership:

Treatment of Goodwill

TREATMENT OF GOODWILL

1. Goodwill is the value of reputation of a Firm in respect of profits expected in future over and above the normal rate of profits earned by similar Firms in the same locality.
2. Goodwill is the benefits & advantages of good name, reputation & connections of a business firm. It is that attractive force which brings in customers & enhances the revenues of firm.

TYPES OF GOODWILL

A. Purchased Goodwill	B. Self-Generated Goodwill
1. Purchased Goodwill arises when a business is purchased, & the consideration paid therefore is more than the value of assets taken over. 2. Purchased Goodwill= Purchase Consideration Less Net Assets taken over 3. Purchased Goodwill is recorded in books of accounts & is shown in balance sheet. 4. The firm may write off purchased Goodwill over a period of time.	1. It refers to internally generated goodwill, that arises to the special advantages possessed by the Firm. 2. Internally Generated Goodwill is not recorded in the books of account, since Accounting Standard 26 issued by ICAI specifically provides so.

Situations which may involve valuation of Goodwill in case of Firms:

Following are the situations warranting Valuation of Goodwill in case of Partnership Firms-

- Change in Profit Sharing Ratio amongst the Partners,
- Admission of a new Partner,
- Retirement or Death of a Partner

METHODS OF VALUATION OF GOODWILL

METHOD 1: AVERAGE PROFITS METHOD

Average Profits Method

Simple Average

$$\text{Average Profits} = \frac{\text{Profits of 'n' years}}{\text{No. of years}}$$

$$\text{Goodwill} = \text{Avg. Profits} \times \text{No. of years of Purchase}$$

Weighted Average

$$\text{Weighted Average Profits} = \frac{\text{Total weighted Profits}}{\text{Total of weights}}$$

$$\text{Goodwill} = \text{Weighted Avg. Profits} \times \text{No. of years of Purchase}$$

Example: Profits: 9000, 18000, 12000
2 years purchase

$$\text{Avg. Profit} = \frac{9000 + 18000 + 12000}{3} = 13000$$

$$G/W = 13000 \times 2 = 26000$$

Example: Profits 9000, 12000, 18000
2 years purchase.

Profits	Weights	Product
9000	1	9000
12000	2	24000
18000	3	54000
	6	87000

$$WAP = \frac{87000}{6} = 14500$$

$$G/W = 14500 \times 2 = 29000$$

Computation of Adjusted Profits

Profits	xx
+ Abnormal loss	xx
− Abnormal Gain	(xx)
− Omission of Expense	(xx)
+ Omission of Income	xx
± Rectification of Errors	xx/(xx)
	xx

METHOD 2: SUPER PROFITS METHOD

Super Profits Method

Goodwill = Super Profits (SP) × No. of Years of Purchase

SP = Average Profits (AP) − Normal Profits (NP)

NP = Capital Employed (CE) × Rate of Return (r%)

CE = Total Assets − Outsider Liabilities
(excl. Fictitious assets & Non Trade Investments)

Example:

A firm earned Net Profits during the last three years as follows-

Year	I	II	III
Profit	₹ 24,000	₹ 20,000	₹ 22,000

The capital investment of the Firm is ₹ 60,000. A fair return on the capital having regard to the risk involved is 10%. Compute the value of Goodwill based on three years purchase of the Super Profits for the last three years.

Avg. Profits: $\frac{24000 + 20000 + 22000}{3} = 22000$

Normal Profits = $60000 \times 10\% = 6000$

Super Profit = $22000 - 6000 = 16000$

G/W = $16000 \times 3 = 48000$

METHOD 3: ANNUITY METHOD

100 + 10% 110 + 10% 121

$\frac{1}{1.10} = 0.909$ 10% 1 1

$(1.10)^2 = 0.826$

Annuity Method

Goodwill = Super Profits × Annuity Factor (A.F.)

A.F. = $\sum$ PVF (r%, n)

PVF = Present value Factor

r% = Rate of Return / Discounted Rate

n = No. of years

Example:

Calculate the goodwill by annuity method of super profit:

(a) Annual maintainable profit after tax is ₹ 65,000. (b) Capital employed is ₹ 4,00,000.

(c) Normal rate of return is expected at 12% p.a.

(d) Present value of an annuity of ₹ 1 for five years @ 12% interest is 3.604776.

AP = 65000 NP = 4L × 12% = 48000 $\frac{1}{1.12}$ = 0.8928

Super Profit = 65000 − 48000 = 17000

G/W = 17000 × 3.604776 = 61281

METHOD 4: CAPITALISATION METHOD

Capitalisation Method

- Capitalisation of Average Profits
  - Goodwill = Capitalised value of Business (CVB) − Capital Employed
  - CVB = $\frac{\text{Average Profits}}{r\%}$
- Capitalisation of Super Profits
  - Goodwill = $\frac{\text{Super Profits}}{r\%}$

Sometimes Question specifies to apply Average Capital Employed

Average Capital Employed = Opening Capital Employed + Closing Capital Employed

2

Example:

The net tangible assets of a firm are worth ₹ 4,10,000 and the average profit of last four years amounts to ₹ 60,000. Find out the value of goodwill under capitalization method if the reasonable return on capital invested is 12%.

Capitalisation of Avg. Profits $= \frac{AP}{R\%} - \text{Cap. Emp.}$

$= \frac{60000}{12\%} - 410000 = 500000 - 410000$

$= 90000$

Capitalisation of super Profits $= \frac{SP}{R\%} = \frac{10800}{12\%} = 90000$

$SP = 60000 - (410000 \times 12\%)$

$= 60000 - 49200 = 10800$

Question 1: (CA Foundation Dec 2022) (5 Marks)

R and S are partners in a firm with a capital of 14,00,000 and 12,00,000 respectively. During the year ended on 31st March, 2022 firm earned a profit of ₹ 6,50,000. Assuming that the normal rate of return is 20%. Calculate the amount of Goodwill of the firm by using

a. Capitalization method
b. Super Profit method, if the goodwill is valued at 6 years purchase of super profits.

Solution

i. **Capitalization Method:**

Total Capitalised Value of the firm = [(Average Profit *100)/(Normal Rate of Return)
= 6,50,000 x 100/20 = ₹ 32,50,000
Goodwill = Total Capitalised Value of Business – Capital Employed
= ₹ 32,50,000 – ₹ 26,00,000 [i.e., ₹ 14,00,000 (R) + ₹ 12,00,000 (S)]
Goodwill = ₹ 6,50,000

ii. **Super Profit Method:**

Normal Profit = Capital Employed x Normal rate of return
i.e. ₹ 26,00,000 x 20/100 = ₹ 5,20,000
Average Profit = ₹ 6,50,000
Super Profit = Average profit – Normal Profit
= ₹ 6,50,000 – ₹ 5,20,000 = ₹ 1,30,000
Goodwill = Super Profit x Number of years' purchase
= ₹ 1,30,000 x 6 = ₹ 7,80,000

Question 2: (RTP Nov 2018)/(Nov 2019)/(Nov 2021)/(Nov 2023) (Similar)

Vasudevan, Sunderarajan and Agrawal are in partnership sharing profit and losses at the ratio of 2:5:3. The Balance Sheet of the partnership as on 31.12.2021 was as follows:

Balance Sheet of M/s Vasudevan, Sunderarajan & Agrawal

Liabilities	₹	Assets	₹
Capital A/cs		Sundry fixed assets	5,00,000
Vasudevan	85,000	Stock	1,00,000
Sunderarajan	3,15,000	Debtors	50,000
Agrawal	2,25,000	Bank	5,000
Sundry Creditors	30,000		
	6,55,000		6,55,000

The partnership earned profit ₹ 2,00,000 in 2021 & the partners withdrew ₹ 1,50,000 during the year. Normal rate of return 30%. Find out the value of goodwill on the basis of 5 years' purchase of super profit. Calculate super profit using average capital employed

Super Profit = Avg. Profit − Normal Profit
= 200000 − 180000 = 20000

G/W = 20000 × 5 = 100000

Avg. Profit = 200000

Normal Profit = Avg. Cap. Emp. × 30%
= 600000 × 30% = 180000

Avg. Cap. Emp. = $\frac{\text{Op.} + \text{Cl.}}{2}$ = $\frac{575000 + 625000}{2}$ = 600000

Closing Cap. Emp. = 655000 − 30000 = 625000

Opening Cap. Emp. = 625000 + 150000 − 200000 = 575000

Cap. A/c (Combined)

Drawings	150000	b/d (B.f.)	575000
c/d	625000	Profit	200000

Question 3: (CA Foundation June 2022) (5 Marks)

Mr. X gives the following particulars in respect of business carried on by him:

Particulars	Amount (₹)
Capital Invested in business	9,00,000
Market rate of interest on investment	8%
Rate of risk return on capital invested in business	3%
Remuneration per annum from alternative employment of proprietor if he was not engaged in business	36,000

The business earned profits of ₹ 2,40,000, ₹ 2,16,000 and ₹ 3,00,000 in the years 2018, 2019 and 2021 respectively but made a loss of ₹ 36,000 in the year 2020.

Compute the value of Goodwill on the basis of 6 years' purchase of super profits of the business, calculated on the basis of average profit of last four years.

Solution

Computation of Goodwill of Mr. X

Average maintainable profits:		₹
Trading profit during	2018	2,40,000
	2019	2,16,000
	2021	3,00,000
		7,56,000
Less: Loss during	2020	(36,000)
Total		**7,20,000**
Average Profits (₹ 7,20,000 / 4)		1,80,000
Less: Remuneration for the proprietor		(36,000)
Average maintainable Profit		1,44,000
Less: Normal Profit (11% on capital employed of ₹ 9,00,000)		(99,000)
Super Profit		45,000
Goodwill at 6 year's purchase of Super Profit		**2,70,000**

Alternative: ₹

Total profit (₹ 2,40,000 + ₹ 2,16,000 + ₹ 3,00,000 - ₹ 36,000) = ₹ 7,20,000

Normal Profit (11% on capital employed of ₹ 9,00,000)	99,000
Remuneration for the proprietor	36,000
	1,35,000
Average Profits (₹ 7,20,000 / 4)	1,80,000
Super Profit (1,80,000 – 1,35,000)	45,000
Goodwill at 6 year's purchase of Super Profit	2,70,000

TREATMENT OF GOODWILL IN CASE OF CHANGE IN PSR

Accounting Issue involved	Journal Entry
1. Writing off Goodwill existing in books	All Partner's Capital A/c (individually) Dr. (in old ratio) To Goodwill A/c
2. Adjusting Goodwill on change in PSR	Gaining Partner's Capital A/c Dr. (in Gain ratio) To Sacrificing Partners' Capital A/c (in Sacrifice Ratio)

Sacrifice	Gain
Partners whose shares in Profit have deceased as a result of change in PSR, are known as Sacrificing Partners.	Partners whose shares in profits have increased as a result of change in PSR, are known as Gaining Partners
The ratio in which Partners have agreed to reduce their profits in favour of the other Partner(s) is called Sacrifice Ratio or Sacrificing Ratio.	The ratio in which Partners have agreed to gain their profits from the other Partner (s) is called Gain Ratio or Gaining Ratio
Sacrifice Ratio = Old Ratio less New Ratio	Gain Ratio = New Ratio less Old Ratio

Example:

P, Q and R are partners sharing profits and losses in the ratio of 3:2:1. The goodwill of the firm is valued at ₹ 12,000. They have decided to change the profit-sharing ratio to 2:2:1. Pass Journal Entry for goodwill adjustment.

Alt-1

OR = 3:2:1 NR = 2:2:1

$P = \frac{2}{5} - \frac{3}{6} = \frac{12-15}{30} = -\frac{3}{30}$ (S)

$Q = \frac{2}{5} - \frac{2}{6} = \frac{12-10}{30} = \frac{2}{30}$ (G)

$R = \frac{1}{5} - \frac{1}{6} = \frac{6-5}{30} = \frac{1}{30}$ (G)

Q's Cap. A/c - Dr 800
R's Cap. A/c - Dr 400
To P's Cap. A/c 1200

Alt-2

G/W = 12000

	P	Q	R
Cr. in OR (3:2:1)	6000	4000	2000
Dr in NR (2:2:1)	(4800)	(4800)	(2400)
	1200 Cr.	800 Dr.	400 Dr.

Question 4: (ICAI Study Material)

Antoo, Bantoo and Chintoo were in partnership sharing profits and losses 3:4:3 respectively. The accounts of the firm are made up to 31st March every year. The partnership provided, interalia, that: On the retirement of a partner the goodwill was to be valued at three years' purchase of average profits of the past four years up to the date of the retirement after deducting interest @12%p.a. on capital employed and remuneration of ₹ 2,000 p.m.to each partner. On 1st April 2023, Antoo retired and it was agreed on his retirement to adjust goodwill in the capital accounts without showing any amount of goodwill in the Balance Sheet. It was agreed that the capital employed would be ₹6,50,000. Bantoo and Chintoo were to continue the partnership, sharing profits and losses equally after the retirement of Antoo.

The following were the amounts of profits of earlier years before charging salary to partners and interest on capital employed.

Year	Profit
2019-20	2,60,000
2020-21	2,75,000
2021-22	2,65,000
2022-23	2,80,000

You are required to compute the value of goodwill & show the adjustment there of in the books of firm.

Solution

Calculation of Goodwill

	₹
2019-20	2,60,000
2020-21	2,75,000
2021-22	2,65,000
2022-23	2,80,000
Total profit of 4 years	**10,80,000**

Average Profit =10,80,000/4 = 2,70,000
Less: Interest on capital @ 12%p.a. = (78,000) [6,50,000*12%]
Less: Salaries of partners' 3 x 12 x 2,000 = (72,000)
Adjusted Average profit = 1,20,000
Goodwill = 3 years purchase = 3 x 1,20,000 = 3,60,000

Particulars	Antoo	Bantoo	Chintoo
Credit in Old Ratio (3:4:3)	1,08,000	1,44,000	1,08,000
Debit in New Ratio (1:1)		(1,80,000)	(1,80,000)
	1,08,000 Cr.	**36,000 Dr.**	**72,000 Dr.**

Journal Entry

Particulars	L.F.	Dr.	Cr.
Bantoo's Capital A/c Dr.		36,000	
Chintoo's Capital A/c Dr.		72,000	
To Antoo's Capital A/c			1,08,000
(Being the adjusting entry for goodwill through capital accounts of partners)			

Partnership:

Admission of New Partner

ADMISSION OF NEW PARTNER

CONCEPT

New partners are admitted for the benefit of the partnership firm. New partner is admitted either for increasing the partnership capital or for strengthening the management of the firm.

Points to Note:

1) Calculation of New Ratio & Sacrificing Ratio
2) Revaluation of Assets & Liabilities
3) Treatment of Reserves
4) Treatment of Goodwill
5) Adjustment of Partners capital Accounts

Example 1

X and Y share profits in the ratio 5:3. Z is admitted for 1/4th Share in Profits. Compute New PSR

Let total share = 1 $\quad Z = 1/4$

Remaining share $= 1 - \frac{1}{4} = \frac{3}{4}$

$X = \frac{3}{4} \times \frac{5}{8} = \frac{15}{32}$

$Y = \frac{3}{4} \times \frac{3}{8} = \frac{9}{32}$

SR = 5:3

NR = $\frac{15}{32} : \frac{9}{32} : \frac{1}{4} = 15:9:8$

Example 2

X & Y share profits in the ratio 5:3. Z is admitted for 1/5th Share in Profits, which he takes as 1/10th each from X & Y. Compute New PSR.

X's new share $= \frac{5}{8} - \frac{1}{10} = \frac{25-4}{40} = \frac{21}{40}$

Y's new share $= \frac{3}{8} - \frac{1}{10} = \frac{15-4}{40} = \frac{11}{40}$

$Z = \frac{1}{5} = \frac{8}{40}$

NR = 21:11:8

Example 3

X & Y share profits in the ratio 3:2. Z is admitted and for which X surrenders 1/5th of his share in favour of Z & Y surrenders 2/5th of his share in favour of Z. Compute New PSR.

Surrender by X $= \frac{3}{5} \times \frac{1}{5} = \frac{3}{25}$

Surrender by Y $= \frac{2}{5} \times \frac{2}{5} = \frac{4}{25}$

X's new share $= \frac{3}{5} - \frac{3}{25} = \frac{15-3}{25} = \frac{12}{25}$

Y's new share $= \frac{2}{5} - \frac{4}{25} = \frac{10-4}{25} = \frac{6}{25}$

Z's new share $= \frac{3}{25} + \frac{4}{25} = \frac{7}{25}$

NR = 12:6:7

Example 4

A,B & C share profits in the ratio 3:2:5. D is admitted for 1/4th share which is contributed in the ratio of 1 : 1 : 3. Compute New PSR.

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

$A = \frac{1}{4} \times \frac{1}{5} = \frac{1}{20}$

$B = \frac{1}{4} \times \frac{1}{5} = \frac{1}{20}$

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

New Shares

$A = \frac{3}{10} - \frac{1}{20} = \frac{6-1}{20} = \frac{5}{20}$

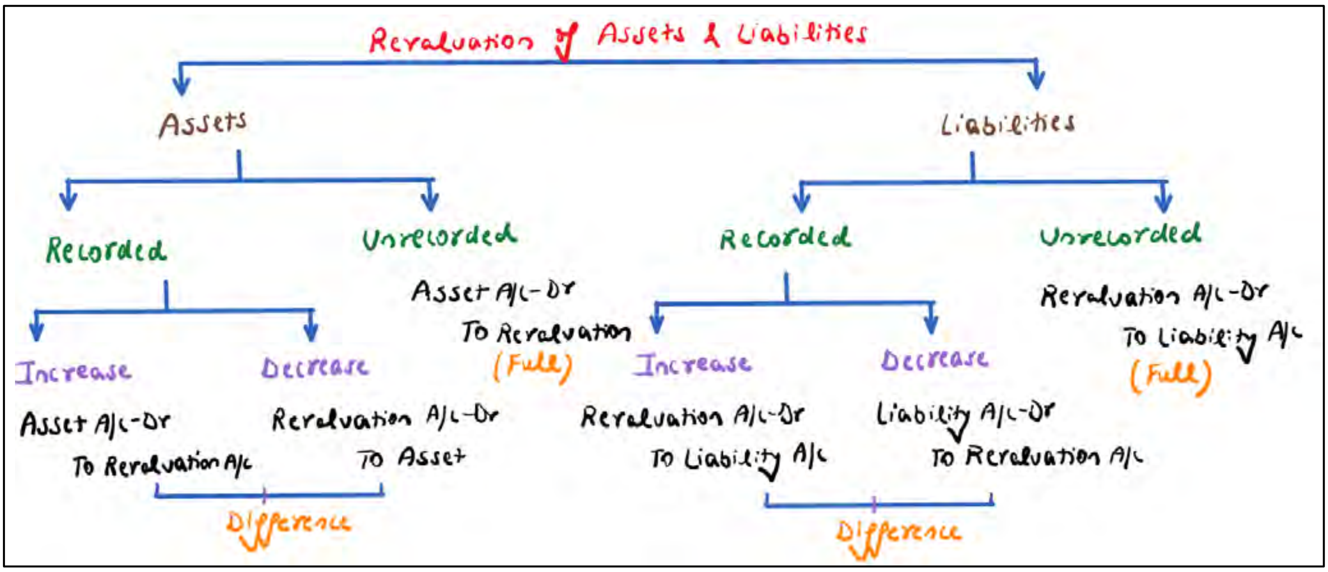
$B = \frac{2}{10} - \frac{1}{20} = \frac{4-1}{20} = \frac{3}{20}$

$C = \frac{5}{10} - \frac{3}{20} = \frac{10-3}{20} = \frac{7}{20}$

$D = \frac{1}{4} = \frac{5}{20}$

NR = 5:3:7:5

REVALUATION OF ASSETS & LIABILITIES



Revaluation A/c

Particulars	Amount	Particulars	Amount
To Asset (Decrease)		By Asset (Increase)	
To Liabilities (Increase)		By Assets unrecorded	
To Liabilities unrecorded		By Liabilities (Decrease)	
To Revaluation profit (old partners in old ratio)		By Revaluation Loss (old partners in old ratio)	

Passing the entry through Capital A/c of Partners (Preparing Memorandum Revaluation Account)

1. Find the net gain or loss on Revaluation as follows
2. Entry:

    Gaining partners capital A/c (in case of profits)
        To Sacrificing partners capital A/c
    Sacrificing partners capital A/c (in case of losses)
        To Gaining partners capital A/c

Profit → Cr in OR
Dr in NR

Note: When profit/loss on revaluation of assets and liabilities is adjusted through capital accounts only then the assets & liabilities appear in B/sheet of new firm at their old figures.

Difference Between Revaluation Account and Memorandum Revaluation Account

- Revaluation account is prepared to find out the profit or loss on revaluation of assets and liabilities which appear in the new balance sheet at the new or revalued figures. Memorandum revaluation account is also prepared to record the effect of revaluation of assets & liabilities which of course are recorded at their old figures in new balance sheet.
- Revaluation account is not divided into two parts. But the memorandum revaluation account has two parts: first part for old partners and second part for all partners including the new partner.

TREATMENT OF RESERVES

Reserves

- **General Reserve** (P&L A/c, etc.)

  General Reserve / P&L A/c - Dr
  To Partner's capital A/cs
  (OLD RATIO)

- **Specific Reserve** [Investment Fluctuation Fund, Workmen Compensation Reserve, etc.]
  - If no other information given

    Reserve A/c - Dr
    To Partner's capital A/cs
  - If Ques. specifics Liability against it
    - Reserve > Liability

      Reserve A/c - Dr
      To Liability A/c
      To Partner's cap. A/cs
    - Reserve = Liability

      Reserve A/c - Dr
      To Liability A/c
    - Reserve < Liability

      Reserve A/c - Dr
      Revaluation A/c - Dr
      To Liability A/c

Note: Sometimes the partner may decide not to close the Reserves / P& L A/c but to record the adjustment entry.

Gaining Partners' capital A/c Dr.
To Sacrificing Partners capital A/c

TREATMENT OF GOODWILL

Treatment of Goodwill

- **Old G/w** (Appearing in B/S)

  Old Partner's Capital A/c - Dr
  To Goodwill A/c

- **G/w Valued**
  1. Bring

     Cash / Bank / Asset A/c - Dr
     To New Partner's cap. A/c
     To Premium for G/w
  2. G/w Adjustment

     Premium for G/w A/c - Dr
     New Partner's cap. A/c - Dr
     To Sacrificing Partners cap. A/c
  3. Withdrawal of G/w

     Sacrificing Partner's cap. A/c - Dv
     To Cash / Bank A/c

Example:

A & B are partners with PSR of 3:2.

C is admitted into the firm for 1/5th share. His share of capital is 50,000. Goodwill of firm valued at 1,00,000. Pass entries in the following cases:

a) C brings his share of capital & goodwill
b) C brings his share of capital & 60% share of goodwill
c) C brings his share of capital only & nothing for goodwill

$1L \times \frac{1}{5} = 20000$ ↓ SR 3:2

Let total share = 1 $C = \frac{1}{5}$

Remaining share = $1 - \frac{1}{5} = \frac{4}{5}$

$A = \frac{4}{5} \times \frac{3}{5} = \frac{12}{25}$ $B = \frac{4}{5} \times \frac{2}{5} = \frac{8}{25}$

NR = 12 : 8 : 5

G/w = 100000

	A	B	C
Cr in OR (3:2)	60000	40000	
Dr in NR (12:8:5)	(48000)	(32000)	(20000)
	12000 Cr.	8000 Cr.	20000 Dr.

	(50000 + 20000) (a)		(50000 + 12000) (b)		(50000 + Nil) (c)	
Bank A/c - Dr	70000		62000		50000	
To C's capital A/c		70000		62000		50000
C's capital A/c - Dr	20000		20000		20000	
To A's cap. A/c		12000		12000		12000
To B's cap. A/c		8000		8000		8000
Balance in C's cap.	50000 (70000 - 20000)		42000 (62000 - 20000)		30000 (50000 - 20000)	

HIDDEN GOODWILL

Net worth (including goodwill) on the basis of capital brought by an incoming partner (Incoming partners capital A/c x Reciprocal of his share)

Less: Net worth (excluding G/w of the firm)

Where, *Net worth* is Total Assets – Outsiders' Liabilities

OR

Capital of partners including new + Reserves + P & L (Cr. Bal.) - Miscellaneous expenditure

Example

A & B having PSR 3 : 2 are partners with capitals of ₹ 30,000 & ₹ 20,000 on date of C's admission for 1/5th share who brings ₹ 40,000. Following are the balances:

P & L (Cr.) = 6,000 Reserves = 55,000 Deferred Revenue Expenditure = 1,000

Find Goodwill.

Net worth (incl. G/w) = $40000 \times \frac{5}{1}$ = 200000

− Net worth (excl. G/w) = = (150000)

(30000 + 20000 + 6000 + 55000 − 1000 + 40000)

Goodwill 50000

C's sh. = $50000 \times \frac{1}{5} = 10000$

ADJUSTMENT OF CAPITAL

Example 1

A & B. Ratio = 3 : 2. C is admitted 1/4th share & brings ₹ 1,00,000 as capital. Capital of new firm is to be ₹ 4,00,000. Actual capital after all adjustments of A & B are ₹ 2,00,000 & ₹ 1,00,000. New capital will be shared in their new PSR.

Total Sh. = 1 $\quad C = \frac{1}{4}$

Rem. Sh. = $1 - \frac{1}{4} = \frac{3}{4}$

$A = \frac{3}{4} \times \frac{3}{5} = \frac{9}{20}$

$B = \frac{3}{4} \times \frac{2}{5} = \frac{6}{20}$

NR = 9 : 6 : 5

Total capital = 400000

	A	B	C
Should be (9:6:5)	180000	120000	100000
Existing cap.	200000	100000	100000
	20000 withdraw	20000 Bring	-

Example 2

A & B = 3 : 2. Capital of A & B after adjustments are ₹ 80,000 & ₹ 60,000 respectively C is admitted who brings ₹35,000 as capital for 1/5th share of profit to be acquired equally from A & B. Capital of A & B are to be adjusted on the basis of C's capital.

$A = \frac{3}{5} - \frac{1}{10} = \frac{5}{10}$

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

NR = 5 : 3 : 2

C's capital = 35000 (For 1/5th share)

Total capital = $35000 \times \frac{5}{1} = 175000$

	A	B	C
Should be (5:3:2)	87500	52500	35000
Existing	80000	60000	35000
	7500 Bring	7500 Withdraw	-

Example 3

A & B = 3 : 2

Capitals of A & B after adjustments are ₹ 90,000 & ₹ 70,000. Calculate incoming partners proportionate capitals & surplus/shortage of existing capitals of old partners.

a) If C is to contribute proportionate capital for his 1/5th share

b) If C is to contribute 1/4th of the combined capitals of the existing partners.

c) If C is to contribute proportionate capital for his 1/5th share & capitals of all the partners are to be adjusted in new PSR 3:1:1

Capital of A & B = 90000 + 70000 = 160000

a) C's sh. = $\frac{1}{5}$ $\quad$ Rem. share = 4/5 $\quad$ For $\frac{4}{5}$th share, Capital = 160000

Total capital = $160000 \times \frac{5}{4} = 200000$

C's capital = $200000 \times \frac{1}{5} = 40000$

b) C's share = $160000 \times \frac{1}{4} = 40000$

c) Total capital = 200000

	A	B	C
Should be (3:1:1)	120000	40000	40000
Existing	90000	70000	40000
	30000 Bring	30000 withdraw	-

Question 1: (ICAI Study Material)

Alpha & Beeta were partners in LLP namely Meta-Chem LLP sharing profits & losses equally.

BALANCE SHEET of Meta-Chem as on 31st March 2023

Liabilities	₹	Assets	₹
Capital Accounts:		Factory Building	4,78,000
Alpha	3,00,000	Plant & Machinery	3,41,000
Beeta	2,00,000	Office Furniture	55,850
General Reserve	1,80,000	Inventory	77,740
Workmen Compensation Fund	60,000	Trade Receivables	1,43,210
Term Loan from IDFC Bank	2,78,000	Bank	44,200
Trade Payables	1,22,000		
	11,40,000		11,40,000

They agreed to admit Gyama as partner from 1st April 2023 on the following terms:

1. He shall have one-sixth share in future profits.
2. New profit sharing ratio would be 3:2:1
3. He shall bring ₹ 2,50,000 as his capital.
4. Goodwill of the firm is valued at ₹ 3,00,000
5. Factory Building is to be appreciated by 20% and inventory is revalued at ₹ 70,000.
6. Machinery to be appreciated by 20%.and Office furniture to be revalued at ₹ 50,000
7. Of the trade receivables ₹ 3,210 are bad and 5% be provided for bad & doubtful debts.
8. There is no actual liability towards workman.

You are required to prepare:

1. Revaluation account
2. Partners' capital accounts.
3. Bank Account
4. Balance Sheet after admission.

Question 2: (CA Foundation Nov 2018)(15 Marks)/(RTP May 20)/(May 23)(Sim.)

Dinesh, Ramesh and Naresh is a firm sharing profits and losses in the ratio 3:2:1. Their Balance Sheet as on 31st March, 2021 is as below:

Liabilities		₹	Assets	₹
Trade Payables		22,500	Land and Buildings	37,000
Outstanding liabilities		2,200	Furniture & Fixtures	7,200
General reserve		7,800	Stock	12,600
Capital Account :			Trade Receivables	10,700
Dinesh	15,000		Cash in hand	2,800
Ramesh	15,000		Cash at bank	2,200
Naresh	10,000	40,000		
		72,500		72,500

The partners have agreed to take Suresh as a partner with effect from 1st April, 2021 on the following terms:

(1) Suresh shall bring 8,000 towards his capital.
(2) The value of stock to be increased to ₹ 14,000 & Furniture & Fixtures to be depreciated by 10%
(3) Reserve for bad and doubtful debts should be provided at 5% of the Trade Receivables.
(4) The value of land and buildings to be increased by 5,600 and the value of the goodwill be fixed at ₹ 18,000.
(5) The new profit sharing ratio shall be divided equally among the partners

The outstanding liabilities include ₹ 700 due to Ram which has been paid by Dinesh. Necessary entries were not made in the books. Prepare

(i) Revaluation Account, and
(ii) The Capital Accounts of the partners, and
(iii) Balance Sheet of the firm after admission of Suresh

Solution

Revaluation A/c

Particulars	₹	Particulars	₹
To Furniture & Fixtures	720	By Stock	1,400
To Provision for Doubtful Debts	535	By Land & Building	5,600
To Profit transferred to			
Dinesh's Capital A/c	2,872.50		
Ramesh's Capital A/c	1,915		
Naresh's Capital A/c	957.50		
	7,000		**7,000**

Capital Accounts

	Dinesh	Ramesh	Naresh	Suresh		Dinesh	Ramesh	Naresh	Suresh
To Dinesh & Ramesh Cap. A/cs			1,500	4,500	By Bal b/d	15,000	15,000	10,000	-
To Bal c/d	26,972.5	21,015	10,757.5	3,500	By Rev. A/c	2,872.5	1,915	957.50	-
					By Gen. Reserve	3,900	2,600	1,300	-
					By Naresh & Suresh Cap. A/cs	4,500	1,500	-	-
					By Bank	-	-	-	8,000
					By O/s Liability	700	-	-	-
	26,972.5	**21,015**	**12,257.5**	**8,000**		**26,972.5**	**21,015**	**12,257.5**	**8,000**

Balance Sheet

Liabilities	Amount	Assets		Amount
Capital Account		Land & Building (37000 + 5600)		42,600
Dinesh	26,972.50	Furniture & Fixtures (7200 - 720)		6,480
Ramesh	21,015	Stock		14,000
Naresh	10,757.50	Trade Receivables	10,700	
Suresh	3,500	Less Prov. for Doubtful Debts	(535)	10,165
Trade Payables	22,500	Cash in Hand		2,800
Outstanding Liabilities (2200-700)	1,500	Cash at Bank (2200 + 8000)		10,200
	86,245			**86,245**

Working Notes:

1. Adjustment for goodwill G/W = 18000

	Dinesh	Ramesh	Naresh	Suresh
Cr. in Old Ratio (3:2:1)	9,000	6,000	3,000	-
Dr. in New Ratio (1:1:1:1)	(4,500)	(4,500)	(4,500)	(4,500)
	4,500 Cr.	**1,500 Cr.**	**1,500 Dr.**	**4,500 Dr.**

Question 3: (ICAI Study Material)

A and B are in the partnership sharing profits and losses in the proportion of three-fourth and one-fourth respectively. Their balance sheet as on 31st March, 2023 was as follows:
Cash ₹1,000; trade receivables ₹25,000; Inventory ₹22,000; plant and machinery ₹4,000; trade payables ₹12,000; bank overdraft ₹15,000; A's capital ₹15,000; B's capital ₹10,000.
On 1st April, 2023, they admitted C into partnership on the following terms:

a) C to purchase one-third of the goodwill for ₹2,000 and provide ₹10,000 as capital. Goodwill not to appear in books.
b) Further profits and losses are to be shared by A, B and C equally.
c) Plant and machinery is to be reduced by 10% and ₹500 is to be provided for estimated bad debts. Inventory is to be taken at a valuation of ₹24,940.
d) By bringing in or withdrawing cash and capitals of A and B are to be made proportionate to that of C on their profit-sharing basis.

Set out entries to the above arrangement in firm's journal & give partners' capital accounts.

OR = 3:1 C = 1/3

NR = 1:1:1

Question 4: (CA Foundation Dec 2022) (10 Marks)

X and Y are in partnership business sharing profits and losses in the ratio of 2:3. Their Balance Sheet as at 31st March, 2022 is as follows:

Liabilities	Amount (₹)	Assets	Amount (₹)
Capital Accounts:		Building	60,000
X	60,000	Plant	45,000
Y	1,40,000	Furniture	23,500
General Reserve	40,000	Debtors	38,400
Creditors	42,600	Bills receivable	12,500
Bills payable	15,400	Stock	42,600
Salary payable	2,000	Bank	78,000
	3,00,000		3,00,000

On 1st April, 2022 they decided to admit Z into the partnership giving him 1/5th share in the future profits. He brings in ₹ 1,00,000 as his share of capital. Goodwill was valued at ₹ 1,20,000 at the time of admission of Z. The partners decided to revalue assets & liabilities as follows:

a. Plant ₹ 40,000, Stock ₹ 42,000, Furniture ₹ 20,000 and Bills Receivable ₹ 12,000.
b. Out of total Debtors, ₹ 2,400 is bad and 5% provision is to be provided for bad and doubtful debts.
c. Building is to be appreciated by 75%.
d. Actual liability towards salary payable is ₹ 1,200 only.

You are required to show the following accounts in the books of the firm:

1. Revaluation Account
2. Partner's Capital Accounts
3. Balance sheet of the Firm after Admission of Z.

Solution

In the books of X, Y and Z

Revaluation Account

Particulars	₹	Particulars	₹
To Plant	5,000	By Building (60000 X 75%)	45,000
To Bad Debts	2,400	By Salary Payable	800
To Provision for Doubtful Debts (38400 - 2400) X 5%	1,800		
To Stock	600		
To Furniture	3,500		
To Bills receivable	500		
To Profit on revaluation			
- X	12,800		
- Y 2:3 Profit = 32000	19,200		
	45,800		**45,800**

Partners' Capital A/c's

Particulars	X	Y	Z	Particulars	X	Y	Z
To X and Y (G/w Adj.)	-	-	24,000	By Balance b/d	60,000	1,40,000	-
To Balance c/d	98,400	1,97,600	76,000	By Bank	-	-	1,00,000
				By Z	9,600	14,400	-
				By Gen. Reserve	16,000	24,000	-
				By Revaluation	12,800	19,200	-
	98,400	**1,97,600**	**1,00,000**		**98,400**	**1,97,600**	**1,00,000**

Balance Sheet as on 1st April, 2022 (after admission)

Liabilities	₹	Assets	₹
Capital Accounts:		Building (60000 + 45000)	1,05,000
- X	98,400	Plant	40,000
- Y	1,97,600	Furniture	20,000
- Z	76,000	Debtors*	34,200
Creditors	42,600	Bills Receivable	12,000
Bills Payable	15,400	Stock	42,000
Salary Payable	1,200	Bank (78000 + 100000)	1,78,000
	4,31,200		**4,31,200**

* Debtors: (38,400 – 2,400 – 1,800) = ₹ 34,200

Debtors 36000
- PDD (1800) 34200

Question 5: (ICAI Study Material)

A and B are partners sharing profits and losses in the ratio of 3:2. Their Balance Sheet as on 31.3.2023 is given below:

Liabilities	₹	Assets	₹
Trade payables	50,000	Freehold premises	2,00,000
Capital Accounts:		Plant	40,000
A	2,00,000	Furniture	20,000
B	1,00,000	Office equipment	25,000
		Inventories	30,000
		Trade receivables	25,000
		Bank	10,000
	3,50,000		3,50,000

On 1.4.2023 they admit C on the following terms:

(1) C will bring ₹ 50,000 as a capital and ₹ 10,000 for goodwill for 1/5 share;
(2) Provision for doubtful debts is to be made on Trade receivables @ 2%
(3) Inventory to be written down by 10%.
(4) Freehold premises is to be revalued at ₹2,40,000, plant at ₹ 35,000, furniture ₹ 25,000 and office equipment ₹ 27,500.
(5) Partners agreed that the values of the assets and liabilities remain the same and, as such, there should not be any change in their book values as a result of the above mentioned adjustments.

You are required to make necessary adjustment in the Capital Accounts of the partners and show the Balance Sheet of the New Firm

$1 - \frac{1}{5} = \frac{4}{5} < \frac{3}{5}, \frac{2}{5}$ $\frac{12}{25}$ $\frac{8}{25}$ $\boxed{12:8:5}$

Solution

Memorandum Revaluation A/c

Particulars	₹	Particulars	₹
To Provision for doubtful debts	500	By Freehold Premises	40,000
To Inventory	3,000	By Furniture	5,000
To Plant A/c	5,000	By Office Equipment	2,500
To Profit transferred to (3:2)			
A's Capital A/c	23,400		
B's Capital A/c	15,600		
	47,500		**47,500**
To Freehold Premises	40,000	By Provision for doubtful debts	500
To Furniture	5,000	By Inventory	3,000
To Office Equipment	2,500	By Plant A/c	5,000
		By Loss transferred to (12:8:5)	
		A's Capital A/c	18,720
		B's Capital A/c	12,480
		C's Capital A/c	7,800
	47,500		**47,500**

Partner's Capital Accounts

Particulars	A	B	C	Particulars	A	B	C
To A's Capital A/c	-	-	6,000	By Balance b/d	2,00,000	1,00,000	-
To B's Capital A/c	-	-	4,000	By Bank A/c	-	-	60,000

To Revaluation A/c	18,720	12,480	7,800	By C's Capital A/c	6,000	4,000	--
To Balance c/d	2,10,680	1,07,120	42,200	By Revaluation A/c	23,400	15,600	-
	2,29,400	**1,19,600**	**60,000**		**2,29,400**	**1,19,600**	**60,000**

Balance Sheet

Liabilities	Amount	Assets	Amount
Capital Account		Freehold Premises	2,00,000
A	2,10,680	Plant	40,000
B	1,07,120	Furniture	20,000
C	42,200	Office Equipment	25,000
Trade Payables	50,000	Inventories	30,000
		Trade receivables	25,000
		Bank (10000 + 60000)	70,000
	4,10,000		**4,10,000**

Question 6: (ICAI Study Material)

The Balance Sheet of Amit, Bhushan and Charan, who share profits and losses as 3 : 2 : 1 respectively, as on 01.04.2021 is as follows:

Liabilities	₹	Assets		₹
Capital Accounts :		Machinery		1,50,000
Amit	1,80,000	Furniture		1,50,000
Bhushan	1,60,000	Stock		2,10,000
Charan	1,40,000	Debtors	80,000	
Current Accounts: Bhushan	16,000	Less: Provision for Bad Debts	(4,000)	76,000
Creditors	1,20,000	Cash		20,000
		Current Account: Charan		10,000
	6,16,000			6,16,000

Dev is admitted as a partner on the above date for 1/5th share in the profit and loss. Following are agreed upon:

1) The profit and loss sharing ratio among the old partners will be equal.
2) Dev brings in ₹ 1,50,000 as capital but is unable to bring required amount of premium for goodwill.
3) The goodwill of the firm is valued at ₹ 60,000.
4) Assets and liabilities are to be valued as follows: Machinery ₹ 2,06,000 : Furniture ₹ 1,28,000 : Provision for doubtful debts @ 10% on debtors.
5) Necessary adjustments regarding goodwill and Profit / loss on revaluation are to made through the Partner's Current Accounts.
6) It is decided that the revalued figures of assets and liabilities will not appear in the Balance Sheet of the new firm.
7) Capital Accounts of the old partners in the new firm should be proportionate to the new profit and loss sharing ratio, taking Dev's Capital as base. The existing partners will not bring cash for further capital. The necessary adjustments are to be made through the partner's Current Account.

Prepare Partner's Capital & Current Account, & Balance Sheet of the new firm after admission

Question 7: (ICAI Study Material)

Cu and Au were in partnership sharing profits and losses in the ratio 5:3. On 1st April 2023, they decided to admit Ag in the partnership on the following terms:

1. Ag will bring ₹ 2,00,000/- as capital for ¼ share.
2. New profit sharing ratio shall be 2:1:1 among Cu, Au and Ag.
3. Cu was entitled to salary of ₹ 2,000/- p.m., it was revised to ₹ 3,000 p.m. from 1st October 2021.
4. Interest on capital was paid at 8% p.a.
5. Capitals as on 31st March 2023 were Cu ₹ 4,00,000 Au ₹ 3,00,000, which had remained unchanged since last four years.
6. Goodwill was to be valued on the basis of 3 years purchase of average adjusted weighted average profits of past 4 years. The profits of previous four years, before charging interest on capital and salary to Cu were as follows:

Year	Profit
2019-20	2,10,000
2020-21	2,60,000
2021-22	2,10,000
2022-23	3,05,000

These profits were subject to following rectification

(a) A machine costing ₹ 40,000 purchased on 1st October 2021 was wrongly charged to revenue. The machinery was depreciated at 20% p.a. on w.d.v. method

(b) Stock on 31st March 2021 was over valued by ₹ 20,000/-

(c) There was a loss by fire amounting to ₹ 10,000/- in the year 2019-20 which was not considered in trading account but correctly debited in the P&L Acc for that year.

(d) Debtors as on 31st March 2023 included bad debts of ₹ 5,800/-

7. Ag shall bring his share of goodwill in cash.

You are required to calculate amount of goodwill Ag is supposed to bring and journal entry for the same.

Solution

Calculation of Goodwill

	2019-20	2020-21	2021-22	2022-23
Given Profits	2,10,000	2,60,000	2,10,000	3,05,000
Less: Salary to Cu	(24,000)	(24,000)	(30,000)	(36,000)
Less: Interest on Capital [7,00,000*8%]	(56,000)	(56,000)	(56,000)	(56,000)
Add: Machine to be capitalised	-	-	40,000	-
Less: Depreciation on Machinery	-	-	(4,000) [40,000*20%*6/12]	(7,200) [36,000*20%]
Less: Overvaluation of Closing Stock	-	(20,000)	-	-
Add: Overvaluation of Opening Stock	-	-	20,000	-
Add: Loss by Fire (Abnormal Item)	10,000	-	-	-
Less: Bad Debts to be w/off	-	-	-	(5,800)
Adjusted Profits	1,40,000	1,60,000	1,80,000	2,00,000
Weights	1	2	3	4
Weighted Profits i.e. Product	1,40,000	3,20,000	5,40,000	8,00,000

Weighted Average Profits = Total Product / Total of Weights
= 18,00,000 / 10
= 1,80,000

Goodwill = 3 year purchase = 1,80,000 * 3
= 5,40,000
Share of Ag = 5,40,000 * ¼ = 1,35,000

Journal Entries

Particulars	**L.F.**	**Dr.**	**Cr**
Bank A/c Dr. (200000 + 135000)		3,35,000	
To Ag's Capital A/c			3,35,000
[Being Capital of 2,00,000 & G/w Share 1,35,000 Brought by Ag]			
Ag's Capital A/c Dr.		1,35,000	
To Cu's Capital A/c			67,500
To Au's Capital A/c			67,500
(Being the adjusting entry for goodwill through capital accounts of partners)			

Working Note:

Particulars	**Cu**	**Au**	**Ag**
Credit in Old Ratio (5:3)	3,37,500	2,02,500	
Debit in New Ratio (2:1:1)	(2,70,000)	(1,35,000)	(1,35,000)
	67,500 Cr.	**67,500 Cr.**	**1,35,000 Dr.**

Revaluation

B/S

	Machinery 100000

Cases

1) Machinery valued at 90000
2) Machinery valued at 120000
3) Machinery is increased by 15%
4) Machinery is decreased by 10%
5) Machinery is decreased to 88000
6) Machinery is increased to 125000

Revaluation A/c

To Mach. 10,000	
	By Mach. 20,000
	By Mach. 15000
To Mach. 10,000	
To Mach. 12000	
	By Mach. 25000

B/S

	Debtor 50000
	− PDD 10% (5000) 45000

1) Provision is increased by 5%

$50000 \times 5\% = 2500$

2) Provision is to be 4000

3) Provision is to be 6500

4) Provision is to be decreased by 3%

$50000 \times 3\% = 1500$ Dec

Revaluation A/c

To PDD 2500	

	By PDD 1000

To PDD 1500	

	By PDD 1500

B/s

		Debtors	50000

1) Of the total debtors 2000 are bad

Revaluation A/c

To Debtors (Bad debts)	2000		

B/s

		Debtors (50000 - 2000)	48000

2) Of the total debtors 3000 are bad & 5% provision is to be made

Revaluation A/c

To Debtors	3000		
To PDD (47000 x 5%)	2350		

B/s

		Debtors (50000 - 3000)	47000
		- PDD	(2350)
			44650

Solution 1

Revaluation A/c

To Inventory	7740	By Factory Building (478000 × 20%)	95600
To Office Furniture	5850	By Machinery (341000 × 20%)	68200
To Debtors (Bad debts)	3210		
To Prov. for Doubtful debts (143210 − 3210) × 5%	7000		
To Profit trd. to Cap. A/cs (B.f.) Alpha 70000 Beeta 70000	140000		

Capital Accounts

	Alpha	Beeta	Gyama		Alpha	Beeta	Gyama
To Beeta's cap.			50000	By Bal b/d	300000	200000	-
				By General Res.	90000	90000	-
				By workmen comp. Fund	30000	30000	-
				By Revaluation A/c	70000	70000	-
To Bal c/d (B.F)	4,90,000	4,40,000	200000	By Bank A/c			2,50,000
				By Gyama's cap. A/c		50000	

Bank A/c

To Bal b/d	44200	By Bal c/d	294200
To Gyama's cap.	250000		

Balance sheet

Liabilities			Assets		
Capital A/cs:			Factory Building		573600
Alpha	490000		Plant & Machinery		409200
Beeta	440000		Office Furniture		50000
Gyana	200000	11,30,000	Inventory		70000
Term Loan from Bank		278000	Trade Rec.	140000	
Trade Payables		122000	- PDD	(7000)	133000
			Bank		294200
		15,30,000			1530000

W.N: 1

Adjustment of Goodwill

G/W = 300000

	Alpha	Beeta	Gyama
Cr. in OR (1:1)	150000	150000	–
Dr in NR (3:2:1)	(150000)	(100000)	(50000)
	–	50000 Cr.	50000 Dr.

Sol.-3

Journal Entries

	Particulars		Dr.	Cr.
1)	Revaluation A/c – Dr		900	
	(4000 x 10%) To Plant & Mach. A/c			400
	To Prov. for Doubtful debts			500
2)	Inventory A/c – Dr (24940 – 22000)		2940	
	To Revaluation A/c			2940
3)	Revaluation A/c – Dr		2040	
	To A's capital A/c			1530
	To B's capital A/c			510
	(Being revaluation profit trf. to old partners in OR 3:1)			
	[2940 - 900 = 2040]			

4)	Bank A/c -Dr	12000	
	To C's capital A/c		12000
5)	B's Capital A/c -Dr	500	
	C's Capital A/c -Dr	2000	
	To A's capital A/c		2500
	(Being adjustment entry passed for G/W)		
6)	A's capital A/c -Dr	9030	
	B's capital A/c -Dr	10	
	To Bank A/c		9040
	(Being capital withdrawn)		

Capital A/cs

	A	B	C		A	B	C
To A's capital A/c		500	2000	By Bal b/d	15,000	10,000	
To Bank (B.f.)	9030	10	–	By Revaluation A/c	1530	510	
				By Bank A/c			12000
				By B's cap. & C's cap. A/c	2500		
To Bal c/d	10,000	10,000	10,000				

W.N:

C's share = 1/3 C's share of G/w = 2000

Total G/w = 2000 × 3/1 = 6000

	A	B	C
Cr in OR (3:1)	4500	1500	
Dr in NR (1:1:1)	(2000)	(2000)	(2000)
	2500 Cr.	500 Dr.	2000 Dr.

WN

Capital Adjustment

C's share of capital = 10000 for $\frac{1}{3}$rd share

Total capital = $10000 \times \frac{3}{1} = 30,000$

Divide / distribute in New Ratio 1:1:1

i.e. 10000 each.

Memo-Rev

	A	B
OR =	3 :	2

Building = 100000

Revalued at 120000

C = 1/6   NR = 3:2:1

Revaluation A/c

Profit (OR 3:2)	20000	By Building	20000

B/S

		Building	120000

Building to be shown at same value

Rev-A/c (Memo-Rev- A/c)

P = 20000 (3:2)		By Building	20000
To Building	20000	By Loss (3:2:1)	20000

B/S

		Building	100000

Solution 6

Capital A/cs

	Amit	Bhushan	Charan	Dev		Amit	Bhushan	Charan	Dev
					By Bal b/d	180000	160000	140000	
					By Cash				150000
To Bal c/d (750000 in NR)	200000	200000	200000	150000	By Current A/c (B.f)	20000	40000	60000	

Current A/cs

	Amit	Bhushan	Charan	Dev		Amit	Bhushan	Charan	Dev
To Bal b/d			10000		By Bal b/d		16000		
To Amit & Bhushan Curr. A/c			3000	6000	By Charan & Dev Curr. A/c	7000	2000		
To Amit & Bhushan Curr - A/c			6000	12000	By Charan & Dev Curr - A/c	14000	4000		
To Capital A/c	20000	40000	60000	–	By Bal c/d (B.f)		18000	79000	18000
To Bal c/d (B.f)	1000								

Balance sheet

Liabilities			Assets		
Capital A/cs			Machinery		150000
Amit	200000		Furniture		150000
Bhushan	200000		Stock		210000
Charan	200000		Debtors	80000	
Dev	150000	750000	− PDD	(4000)	76000
Current A/c: Amit		1000	Cash (20000 + 150000)		170000
Creditors		120000	**Current A/c**		
			Bhushan	18000	
			Charan	79000	
			Dev	18000	115000
		871000			871000

Working Notes

1) New Ratio

OR = 3 : 2 : 1

Dev = $\frac{1}{5}$ Total share = 1

Remaining share = $1 - \frac{1}{5} = \frac{4}{5} \rightarrow$ 1 : 1 : 1

Amit = Bhushan = Charan = $\frac{4}{5} \times \frac{1}{3} = \frac{4}{15}$

NR = 4 : 4 : 4 : 3

2) Revaluation

Inc. in Machinery	56000
Dec. in Furniture	(22000)
Inc. in PDD	(4000)
(8000 - 4000)	
Profit	30000

	Amit	Bhushan	Charan	Dev
Cr in OR (3:2:1)	15000	10000	5000	
Dr in NR (4:4:4:3)	(8000)	(8000)	(8000)	(6000)
	7000 Cr.	2000 Cr.	3000 Dr.	6000 Dr.

3) G/W = 60000

	Amit	Bhushan	Charan	Dev
Cr in OR (3:2:1)	30000	20000	10000	-
Dr in NR (4:4:4:3)	(16000)	(16000)	(16000)	(12000)
	14000 Cr.	4000 Cr.	6000 Dr.	12000 Dr.

4) Capital Adjustment

Dev capital for $\frac{1}{5}$ share = 150000

Total capital = $150000 \times \frac{5}{1}$ = 750000

Divide in NR 4:4:4:3

Partnership:

Retirement & Death of Partner

RETIREMENT & DEATH OF PARTNER

CONCEPT OF RETIREMENT

- Whenever a partner retires, the continuing partners gain. So they arrange for the amount to be paid to discharge the claims of the retiring partners.
- On retirement of a partner, it is required to revalue assets and liabilities just as in the case of admission of a partner. If there is revaluation profit/loss, then such profit/loss should be distributed amongst the existing partners including the retiring partner at the existing profit sharing ratio (i.e. Old PSR)
- On the retirement of a partner any undistributed profit or reserve standing at the Balance Sheet is to be credited to the Partners' Capital Accounts in the old profit sharing ratio.

Example 1

A, B & C having PSR 3 : 2 : 1 . B retires and his share is taken by A & C in 2 : 1. Find new ratio.

$B = 2/6$

Share given to A $= \frac{2}{6} \times \frac{2}{3} = \frac{4}{18}$

Share given to C $= \frac{2}{6} \times \frac{1}{3} = \frac{2}{18}$

New share

$A = \frac{3}{6} + \frac{4}{18} = \frac{9+4}{18} = \frac{13}{18}$

$C = \frac{1}{6} + \frac{2}{18} = \frac{3+2}{18} = \frac{5}{18}$

New Ratio = 13 : 5

Example 2

P, Q & R having PSR 4 : 3 : 2 . Q retires & surrenders 1/9th of his share in favour of P & remaining in favour of R.

$Q = \frac{3}{9}$

P: $\frac{3}{9} \times \frac{1}{9} = \frac{3}{81}$

R: $\frac{3}{9} \times \frac{8}{9} = \frac{24}{81}$

New share

$P = \frac{4}{9} + \frac{3}{81} = \frac{36+3}{81} = \frac{39}{81}$

$R = \frac{2}{9} + \frac{24}{81} = \frac{18+24}{81} = \frac{42}{81}$

New Ratio = 39 : 42 = 13 : 14

Example 3

X, Y, Z having PSR 4 : 3: 2, Y retires & surrender 1/9 from his share in favour of X & remaining in favour of Z.

$Y = \frac{3}{9}$

X: $\frac{1}{9}$

Z: $\frac{2}{9}$

New share

$X = \frac{4}{9} + \frac{1}{9} = \frac{5}{9}$

$Z = \frac{2}{9} + \frac{2}{9} = \frac{4}{9}$

New Ratio = 5 : 4

TREATMENT OF GOODWILL

Old goodwill

↓

Already appearing in B/sheet

↓

W/off in Old Ratio

Goodwill arising at the time of retirement

↓

Gaining Partner's capital A/c - Dr

To Sacrificing Partner's Cap. A/c

[Cr. in OR
Dr in NR]

Example

X, Y & Z having PSR 2 : 3 : 5. Goodwill appearing in the books ₹ 50,000. X retires & Goodwill valued at ₹ 45,000. Y & Z decided to share equally.

1) X's cap. A/c - Dr 10000
Y's cap. A/c - Dr 15000
Z's cap. A/c - Dr 25000
To Goodwill 50000

2) Y's cap. A/c - Dr 9000
To X's cap. A/c 9000

G/w = 45000

	X	Y	Z
Cr in OR (2:3:5)	9000	13500	22500
Dr in NR (1:1)	-	(22500)	(22500)
	9000 Cr.	9000 Dr.	-

Gain

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

$Z = \frac{1}{2} - \frac{5}{10} = \frac{5-5}{10} = 0$

FINAL PAYMENT TO RETIRING PARTNER

The following adjustments are necessary in the Capital A/c:

(i) Transfer of Profit/Loss on Revaluation.
(ii) Transfer of Reserve
(iii) Transfer of Goodwill

After adjustment of the above-mentioned items, the Capital Account balance standing to the credit of the retiring partner represents amount to be paid to him.

Claim of the retiring partner is payable in the following forms:

- Fully in cash
- Fully transferred to loan account to be paid later with some interest on it.
- Partly in cash and partly as loan repayable later with agreed interest.

Question 1: (ICAI Study Material)

On 31st March, 2023, the balance sheet of M/s Ram, Rahul and Rohit sharing profits and losses in proportion to their capital, stood as follows:

Liabilities		₹	Assets	₹
Capital Accounts:			Land & building	2,00,000
Ram	3,00,000		Machinery	2,00,000
Rahul	2,00,000		Closing stock	1,00,000
Rohit	1,00,000	6,00,000	Sundry debtors	2,00,000
Sundry creditors		2,00,000	Cash and bank balances	1,00,000
		8,00,000		8,00,000

On 31st March, 2023, Ram desired to retire from the firm and the remaining partners decided to carry on. It was agreed to revalue the assets and liabilities on that date on the following basis:

1. Land and buildings be appreciated by 30%.
2. Machinery be depreciated by 20%.
3. Closing stock to be valued at ₹ 80,000.
4. Provision for bad debts be made at 5%.
5. Old credit balances of sundry creditors ₹ 10,000 be written off.
6. Joint life policy of the partners surrendered and cash obtained ₹ 60,000.
7. Goodwill of the entire firm be valued at ₹1,80,000 and Ram's share of the goodwill be adjusted in the accounts of Rahul and Rohit who share the future profits equally. No goodwill account being raised.
8. The total capital of the firm is to be the same as before retirement. Individual capital be in their profit sharing ratio.
9. Amount due to Ram is to be settled on the following basis:50% on retirement and the balance 50% within one year

Prepare revaluation account, capital account of partners: Rahul & Rohit, loan account of Ram, cash account and balance sheet as on 1.4.2023 of M/s Rahul and Rohit.

Solution

Revaluation Account

Particulars	₹	Particulars	₹
To Machinery	40,000	By Land & Buildings	60,000
To Stock	20,000	By Creditors	10,000
To Provision for Bad Debts	10,000	By Cash & Bank-Joint Life Policy	60,000
To Profit on revaluation t/f to			
Ram's capital A/c	30,000		
Rahul's capital A/c	20,000		
Rohit's capital A/c	10,000		
	1,30,000		**1,30,000**

Partners' Capital Accounts

	Ram	Rahul	Rohit		Ram	Rahul	Rohit
To Ram's Capital	-	30,000	60,000	By Balance b/d	3,00,000	2,00,000	1,00,000
To Cash &Bank	2,10,000			By Revaluation	30,000	20,000	10,000
To Ram's Loan	2,10,000			By Rahul's Capital	30,000		

To Balance c/d	-	3,00,000	3,00,000	By Rohit's Capital	60,000		
				By Cash & Bank	-	1,10,000	2,50,000
	4,20,000	**3,30,000**	**3,60,000**		**4,20,000**	**3,30,000**	**3,60,000**

Ram's Loan Account

Particulars	₹	Particulars	₹
To Balance c/d	2,10,000	By Ram's Capital A/c	2,10,000
	2,10,000		**2,10,000**

Cash & Bank Account

Particulars	₹	Particulars	₹
To Balance b/d	1,00,000	By Ram's Capital	2,10,000
To Revaluation A/c-JLP	60,000	By Balance c/d	3,10,000
To Rahul's Capital	1,10,000		
To Rohit's Capital	2,50,000		
	5,20,000		**5,20,000**

Balance Sheet

Liabilities	Amount	Assets	Amount
Capital Account		Land & Building	2,60,000
Rahul 3,00,000		Machinery	1,60,000
Rohit 3,00,000	6,00,000	Stock	80,000
Ram's Loan Account	2,10,000	Debtors 2,00,000	
Creditors	1,90,000	Less:Provision for Bad Debts(10,000)	1,90,000
		Cash & Bank	3,10,000
	10,00,000		**10,00,000**

Working Notes:

1. Gaining ratio of existing partners:
   Rahul 1/2-1/3=1/6 Rohit 1/2-1/6=2/6
2. Total goodwill of firm is ₹ 1,80,000
   Ram's share (1/2 x ₹ 1,80,000)=₹ 90,000
   Ram's share of goodwill is to be borne by Rahul and Rohit in their gaining ratios i.e.
   Rahul=1/3 x ₹ 90,000= ₹ 30,000 Rohit = 2/3 x ₹ 90,000=₹ 60,000

G/w = 180000

	Ram	Rahul	Rohit
Cr in OR (3:2:1)	90000	60000	30000
Dr in NR (1:1)	-	(90000)	(90000)
	90000 Cr.	30000 Dr.	60000 Dr.

Question 2: (CA Foundation May 2018) (10 Marks) / (RTP Nov 2023)

A, B & C are partners sharing profits in ratio of 3:2:1. Their Balance Sheet as at 31st March, 2021

Liabilities		Amount	Assets		Amount
Capital Accounts			Building		10,00,000
A	8,00,000		Furniture		2,40,000
B	4,20,000		Office equipments		2,80,000
C	4,00,000	16,20,000	Stock		2,50,000
Sundry Creditors		3,70,000	Sundry debtors	3,00,000	
General Reserves		3,60,000	Less: Provision for Doubtful debts	(30,000)	2,70,000
			Joint life policy		1,60,000
			Cash at Bank		1,50,000
		23,50,000			23,50,000

B retired on 1st April, 2021 subject to the following conditions:

(i) Office Equipments revalued at ₹ 3,27,000.

(ii) Building revalued at ₹ 15,00,000. Furniture is written down by ₹ 40,000 and Stock is reduced to ₹ 2,00,000 .

(iii) Provision for Doubtful Debts is to be created @ 5% on Debtors.

(iv) Joint Life Policy will appear in the Balance Sheet at surrender value after B's retirement. The surrender value is ₹ 1,50,000

(v) Goodwill was to be valued at 3 years purchase of average 4 years profit which were:

2017 90,000 2018 1,40,000 2019 1,20,000 2020 1,30,000

(vi) Amount due to B is to be transferred to his Loan Account.

Prepare the Revaluation Account, Partners' Capital Accounts and the Balance Sheet immediately after B's retirement.

Solution

Revaluation Account

Particulars	Amount	Particulars	Amount
To Furniture	40,000	By Office Equipment	47,000
To Stock	50,000	By Building	5,00,000
To Joint Life Policy	10,000	By Provision for doubtful debts	15,000
To Profit Transferred to		(30000 - 15000)	
A's Capital	2,31,000		
B's Capital	1,54,000		
C's Capital	77,000		
	5,62,000		**5,62,000**

Capital Accounts

Particulars	A	B	C	Particulars	A	B	C
To B's Capital	90,000		30,000	By Balance b/d	8,00,000	4,20,000	4,00,000
To B's Loan A/c		8,14,000		By General Reserve	1,80,000	1,20,000	60,000
To Balance c/d	11,21,000		5,07,000	By Revaluation	2,31,000	1,54,000	77,000
				By A's Capital		90,000	
				By C's Capital		30,000	
	12,11,000	**8,14,000**	**5,37,000**		**12,11,000**	**8,14,000**	**5,37,000**

Balance Sheet

Liabilities	**Amount**	**Assets**		**Amount**
A's Capital	11,21,000	Cash At Bank		1,50,000
C's Capital	5,07,000	Debtors Less: Provision	3,00,000 (15,000)	2,85,000
Creditors	3,70,000	Stock		2,00,000
B's Loan	8,14,000	Furniture		2,00,000
		Building		15,00,000
		Office Equipment		3,27,000
		JLP		1,50,000
	28,12,000			**28,12,000**

Working Notes:

Calculation of goodwill:

1. Average of last 4 year's profit = (90,000+1,40,000+1,20,000+1,30,000)/4 = 1,20,000
2. Goodwill at three years' purchase 1,20,000 x 3 = 3,60,000

Particulars	**A**	**B**	**C**
Credit in Old Ratio (3:2:1)	1,80,000	1,20,000	60,000
Debit in New Ratio (3:1)	2,70,000	-	90,000
	90,000 Dr.	**1,20,000 Cr.**	**30,000 Dr.**

Question 3: (ICAI Study Material)

F, G and K were partners in LLP sharing profit and losses at the 2:2:1. K wants to retire on 31-12-2023. Given below the Balance Sheet of the partnership as well as other information:

Balance Sheet as on 31-12-2023

Liabilities	₹	Assets	₹
Capital A/cs		Sundry Fixed assets	1,50,000
F	1,20,000	Inventories	50,000
G	80,000	Bank	50,000
K	60,000	Trade Receivables (Including B/R of 20,000)	70,000
Reserve	10,000		
Trade Payables	50,000		
	3,20,000		3,20,000

F and G agree to share profits and losses at the ratio of 3:2 in future. Value of goodwill is taken to be ₹ 50,000. Sundry Fixed Assets are revalued upward by ₹ 30,000 and Inventories by ₹ 10,000. Bills Receivable dishonoured ₹ 5,000 on 31-12-2023 but not recorded in the books. Dishonour of bill was due to insolvency of the customer. F and G agree to bring sufficient cash to discharge claim of K and to make their capital proportionate. Also they wanted to maintain ₹ 75,000 bank balance for working capital.

Pass necessary journal entries, prepare capital accounts and draft the Balance Sheet of M/s F and G.

OR = 2:2:1
NR = 3:2

1) Debtor
To B/R

2) Bad debts / Revaluation
To Debtor

Question 4: (ICAI Study Material)

A,B,C were in partnership sharing profits and losses in the ratio of 3:2:1. The balance sheet of the firm as on 31.3.2023 was as under:

Liabilities		₹	Assets	₹
Capital Accounts:			Fixtures	30,000
A	1,50,000		Stock	1,70,000
B	1,00,000		Sundry debtors	90,000
C	50,000	3,00,000	Cash	50,000
Sundry creditors		40,000		
		3,40,000		3,40,000

A, on account of ill-health, gave notice that he wished to retire from the firm. A retirement agreement was, therefore, entered as on 31.3.2023, the terms of which were as follows:

(a) The profit and loss account for the year ended 31.3.2023, which showed a net profit of ₹ 42,000 was to be re-opened. B was to be credited with ₹ 6,000 as bonus, in consideration of the extra work, which had devolved upon him during the year. The profit sharing basis was to be revised and the revised ratio is to be 2:3:1 as and from 1st April 2022.

(b) Goodwill was to be valued at two years' purchase of the simple average profits of five years. Profits for these five years ending on 31st March were as under:

31.3.2019	15,000
31.3.2020	23,000
31.3.2021	25,000
31.3.2022	35,000
31.3.2023	42,000

	A	B	C
	(21000)	(14000)	(7000)
		6000	
36000	12000	18000	6000
	9000 Dr	10000 Cr	1000 Dr.

(c) Fixtures are to be valued at ₹ 39,800 and a provision of 2% was to be made for doubtful debts and the remaining assets were to be taken at their book value.

(d) That the amount payable to A shall be paid by B.

B and C agreed, as between themselves, to continue the business, sharing profits and losses in the ratio of 3:1 and decided to retain fixtures in the books at the revised value and increase the provision for doubtful debts to 6 %. Total capital of the firm will be ₹3 lakhs as before to be maintained in the new ratio as between B and C.

You are required to give the necessary entries to give effect to the above arrangements. Prepare capital accounts of partners, cash account and balance sheet of B and C.

Solution

Journal Entries

	L.F.	Dr.	Cr.
A's Capital A/c Dr.		21,000	
B's Capital A/c Dr.		14,000	
C's Capital A/c Dr.		7,000	
To P&L Adjustment A/c			42,000
(Being Profit written back for making adjustments)			
P&L Adjustment A/c Dr.		6,000	
To B's Capital A/c			6,000
(Being Bonus credited to B's capital account)			
P&L Adjustment A/c Dr.		36,000	
To A's Capital A/c			12,000
To B's Capital A/c			18,000
To C's Capital A/c			6,000
(Being Distribution of profits in the new ratio)			

Fixtures A/c Dr.		9,800	
To Provision for Bad Debts A/c			1,800
To A's Capital A/c			2,667
To B's Capital A/c OR= 2:3:1			4,000
To C's Capital A/c			1,333
(Being Revaluation of assets on A's retirement)			
B's Capital A/c Dr.		14,000	
C's Capital A/c Dr.		4,667	
To A's Capital A/c			18,667
(Being adjustment entry for goodwill passed)			
B's Capital A/c Dr. 3:1		2,700	
C's Capital A/c Dr.		900	
To Provision for Bad Debts A/c (90000 X 4%)			3,600
(Being provision increased to 6%)			
A's Capital A/c Dr.		1,62,334	
To B's Capital A/c			1,62,334
(Being Amount payable to A paid by B)			
Cash A/c Dr.		30,234	
To C's Capital A/c			30,234
(Being Cash brought by C)			
B's Capital A/c Dr.		34,634	
To Cash A/c			34,634
(Being Cash withdrawn by B)			

Capital Accounts

Particulars	A	B	C	Particulars	A	B	C
To P&L Adj A/c	21,000	14,000	7,000	By Balance b/d	1,50,000	1,00,000	50,000
To A's Capital	-	14,000	4,667	By P&L Adj A/c	-	6,000	-
To PDD	-	2,700	900	By P&L Adj A/c	12,000	18,000	6,000
To B's Capital	1,62,334			By Fixtures & PDD	2,667	4,000	1,333
To Cash		34,634		By B's Capital	14,000		
To Balance c/d	-	2,25,000	75,000	By C's Capital	4,667		
				By A's Capital		1,62,334	
				By Cash	-	-	30,234
	1,83,334	**2,90,334**	**87,567**		**1,83,334**	**2,90,334**	**87,567**

Cash Account

Particulars	Amount	Particulars	Amount
To Balance b/d	50,000	By B's Capital	34,634
To C's Capital	30,234	By Balance c/d	45,600
	80,234		**80,234**

Balance Sheet of B and C as on 31st March, 2023
(after retirement of A)

Liabilities	Amount	Amount	Assets	Amount	Amount
Creditors		40,000	Fixtures		39,800
Capital Accounts			Debtors	90,000	
B	2,25,000		Less: Provision for bad debts	(5,400)	84,600
C	75,000	3,00,000	Stock		1,70,000
			Cash		45,600
		3,40,000			**3,40,000**

Working Notes:

Calculation of goodwill:

1. Average of last five year's profit

31.3.2019	15,000
31.3.2020	23,000
31.3.2021	25,000
31.3.2022	35,000
31.3.2023	42,000
	1,40,000

Average Profit = 1,40,000 / 5 =28,000

2. Goodwill at two years' purchase 28,000 x 2= 56,000

Adjustment of Goodwill

Particulars	A	B	C
Credit in Old Ratio (2:3:1)	18,667	28,000	9,333
Debit in New Ratio (3:1)	-	(42,000)	(14,000)
	18,667 Cr.	**14,000 Dr.**	**4,667 Dr.**

CONCEPT OF DEATH OF PARTNER

- The problems arising on the death of a partner are similar to those arising on retirement. Assets and liabilities have to be revalued and the resultant profit or loss has to be transferred to the Capital Accounts of all partners including the deceased partner. Goodwill is dealt with exactly in the way already discussed in the case of retirement.
- The only additional point is that as death may occur on any day, the representatives of the deceased partner will be entitled to the partner's share of profit from the beginning of the year to the date of death. After ascertaining the amount due to the deceased partner, it should be credited to his Executor's Account.
- If the death takes place during the accounting period, the Executor of the deceased partner is entitled to have a share of profit upto the date of death based on the profit earned in the immediately preceding year or some other agreed basis.

The balance from Capital A/c of deceased partner is transferred to the Deceased Partner's Executor A/c.

Deceased Partner's Capital A/c

Particulars	Amount	Particulars	Amount
To Drawings A/c		By Balance b/d	
To Interest on Drawing A/c		By Interest on capital	
To Goodwill A/c (Existing G/w written off)		By P&L Suspense A/c (Share of profit)	
To Undistributed losses		By Reserve A/c	
To Revaluation (Loss)		By Revaluation A/c (profit)	
To Deceased Partner's Executor A/c (Bal. Fig.)		By Gaining partner's capital A/c (Share of G/w)	

HOW TO CALCULATE OUTGOING PARTNER'S SHARE IN PROFITS EARNED FROM THE DATE OF LAST BALANCE SHEET TO THE DATE OF DEATH / RETIREMENT

Step (1):
Calculate Profits of firm from the date of last Balance sheet to the date of death/retirement.

i. Time Basis

$$\frac{\text{Previous year's profits Or Avg. profits} \times \text{No. of days/months from the date of last b/sheet}}{\text{365 days/12 months}}$$

ii. Sales basis

$$\frac{\text{Previous year's profits Or Avg. profits} \times \text{Sales from the date of last b/sheet}}{\text{Previous years' Sales/Average Sales of past years}}$$

Step (2)
Calculate outgoing partners share in profits.
= Step (1) X Proportion of share of outgoing partner

Accounting Treatment

I) Through P & L suspense A/c

Profit : P & L Suspense A/c Dr.
To Outgoing partner's capital A/c

Loss : Outgoing partner's capital A/c Dr.
To P & L Suspense A/c

Balance of P&L suspense A/c is transferred to the P&L Appropriation A/c at the end of accounting period.

II) Through the Capital A/c of the gaining partner
Gaining partner's capital A/c Dr.
To Outgoing partner's capital A/c

Example
A, B & C are 3 partners having PSR 5:3:2. C died on 30/06/2023. His share of profit is to be calculated on the basis of the previous year profit which was 2,25,000 for FY 2022-23. Find his share of profits till death.

C's share of profit $= \underbrace{\left(225000 \times \frac{3}{12}\right)}_{56250} \times \frac{2}{10} = 11250$

Example
G, M & D. PSR 3:2:1 D died on 31/5/23. Sales of previous year i.e 2022-23 were ₹ 4,00,000 & profit was ₹ 60,000. Sales from 1st April, 2023 till 31st May, 2023 is 1,00,000. Find his share of profit.

Sales = 4L Profit = 60000
Sales = 1L Profit = $\boxed{}$

D's share of profit $= \left(60000 \times \frac{100000}{400000}\right) \times \frac{1}{6}$
$= 2500$

Question 5: (CA Foundation Nov 2019) (10 Marks)

Arup $= \frac{1}{2} = \frac{3}{6}$
Swarup $= \frac{1}{3} = \frac{2}{6}$
Reserve $= \frac{1}{6}$

Arup and Swarup were partners. The partnership deed provides inter alia:
a) That the annual accounts be balanced on 31st December each year;
b) That the profits be allocated as follows:
Arup: One-half; Swarup: One-third and Carried to reserve account: One Sixth;
c) That in the event of death of a partner, his executor will be entitled to the following:

A S
3 : 2

1) The capital to his credit at the date of death;
2) His proportionate share of profit to date of death based on the average profits of the last three completed years; and
3) His Share of goodwill based on three years' purchase of the average profits for the three preceding completed years

Trial Balance as on 31st December 2020

Particulars	Debit (₹)	Credit (₹)
Arup's Capital		90,000
Swarup's Capital		60,000
Reserve		45,000
Bills receivable	50,000	
Investment	55,000	
Cash	1,10,000	
Trade payables		20,000
Total	2,15,000	2,15,000

The profits for the three year were 2018: ₹ 51,000; 2019: ₹ 39,000 and 2020. ₹ 45,000. Swarup died on 1st May 2021.
Show the calculation of Swarup (A) Share of profits; (B) Share of Goodwill; (C) Draw up Swarup's Executors Account as would appear in the firms' ledger transferring the amount to the Loan account.

Solution

(a) Arup : Swarup : Reserve

$$\frac{1}{2} : \frac{1}{3} : \frac{1}{6} = \frac{3:2:1}{6}$$

(A) Calculation of Swarup Share of Profits From 1st Jan, 2021 to 1st May, 2021:

Average profits = (45000+39000+51,000)/3
= 1,35,000/3 = 45,000

Profit From 1st Jan, 2021 to 1st May, 2021 = 45000×4/12 =15000

Swarup's Share in Profit = 15000×2/5 = 6,000

(B) Calculation of Swarup's Share in Firm's Goodwill :

Average profits = (45000+39000+51,000)/3
= 1,35,000/3 = 45000

Goodwill = Average Profits × No. of year's purchase
= 45000×3 = 1,35,000

Swarup's Share in Goodwill = 1,35,000 ×2/5 = 54000

Ledger of Firm

Dr. **Swarup's Executors Account** **Cr.**

Particulars	Amount	Particulars	Amount
To Swarup's Executors Loan A/c (Bal. Fig.)	1,38,000	By Swarup's capital A/c	60,000
		By Profit & Loss Suspense A/c	6,000
		By Arup's Capital A/c (Share in Goodwill)	54,000
		By Reserve (45000×2/5)	18,000
	1,38,000		**1,38,000**

Question 6: (CA Foundation May 2019) (10 Marks)

Monika, Yedhant and Zoya are in partnership, sharing profits and losses equally. Zoya died on 30th June 2021. The Balance Sheet of Firm as at 31st March 2021 stood as

Liabilities	Amount	Assets		Amount
Creditors	20,000	Land and Building		1,50,000
General Reserve	12,000	Investments		65,000
Capital Accounts:		Stock in trade		15,000
Monika	1,00,000	Trade receivables	35,000	
Yedhant	75,000	Less: Prov. for doubtful debt	(2,000)	33,000
Zoya	75,000	Cash in hand		7,000
		Cash at bank		12,000
	2,82,000			2,82,000

In order to arrive at the balance due to Zoya, it was mutually agreed that:

(i) Land and Building be valued at ₹ 1,75,000

(ii) Debtors were all good, no provision is required

(iii) Stock is valued at ₹ 13,500

(iv) Goodwill will be valued at one Year's purchase of the average profit of the past five years. Zoya's share of goodwill be adjusted in the account of Monika and Yedhant.

(v) Zoya's share of profit from 1st April 2021, to the date of death be calculated on the basis of average profit of preceding three years.

(vi) The profit of the preceding five years ended 31st March were:

2021	2020	2019	2018	2017
25,000	20,000	22,500	35,000	28,750

You are required to prepare:

(1) Revaluation account

(2) Capital accounts of the partners and

(3) Balance sheet of the Firm as at 1st July 2021.

Solution

Revaluation Account

Particulars	Amount	Particulars	Amount
To Stock	1,500	By Land and Building	25,000
To Profit transferred		By Prov. for doubtful debt	2,000
Monika	8,500		
Yedhant	8,500		
Zoya	8,500		
	27,000		**27,000**

Partners' Capital Accounts

	Monika	Yedhant	Zoya		Monika	Yedhant	Zoya
To Zoya	4,375	4,375	-	By Balance b/d	1,00,000	75,000	75,000
To Zoya's Executor	-	-	98,125	By Revaluation	8,500	8,500	8,500
To Balance c/d	1,08,125	83,125	-	By Gen. Reserve	4,000	4,000	4,000
				By P&L Suspense A/c*	-	-	1,875
				By Monika & Yedhant	-	-	8,750
	1,12,500	**87,500**	**98,125**		**1,12,500**	**87,500**	**98,125**

*Profit and Loss Suspense = [(25,000 + 20,000 + 22,500)/3] x 3/12 x 1/3 = 1,875

Balance Sheet as at 1.07.2021

Liabilities	₹	Assets	₹
Partners' capital accounts		Land & Building	1,75,000
Monika's capital	1,08,125	Investment	65,000
Yedhant's capital	83,125	Stock	13,500
Zoya's Executor	98,125	Trade receivable	35,000
Sundry creditors	20,000	Profit & Loss Suspense	1,875
		Cash in hand	7,000
		Cash at bank	12,000
	3,09,375		**3,09,375**

<u>Calculation of goodwill and Zoya's share</u>

Average of last five year's profits and losses for the year ended on 31st March.
Average Profit = 1,31,250/5 = 26,250
Goodwill at 1 year purchase = ₹ 26,250 x 1 = ₹ 26,250
Zoya's Share of Goodwill = ₹ 26,250 X 1/3 = ₹ 8,750
which is contributed by Monika and Yedhant in their gaining Ratio
Monika = ₹ 8750X1/2 = ₹ 4375   Yedhant = ₹ 8750X1/2 = ₹ 4375

RETIREMENT / DEATH & ADMISSION

Simultaneous retirement/death and admission do not introduce any new principles of accounting.
The principles studied under admission and retirement/death are combined-the combination of the two sets of transactions.
In case there is retirement/death & simultaneous admission we need to check whether the admission is on the same date or after a subsequent period of time.

<u>Retirement/Death & Admission on the different dates:</u>

1) Treatment of Accumulated Profits, Revaluation of Assets & Liabilities: Adjustment of these will be between old partners in old ratio.
2) Effect of Goodwill: Separate entries will be passed since both the events are on different dates.

<u>Retirement/Death & Admission on the same date:</u>

1) Treatment of Accumulated Profits, Revaluation of Assets & Liabilities: Adjustment of these will be between old partners in old ratio.
2) Effect of Goodwill: Single entry will be passed since both the events are on same date.

Question 7: (CA Foundation Nov 2020) (10 Marks)

M/s. TB is a partnership firm with the partners A, B and C sharing profits and losses in the ratio of 3:2:5. The balance sheet of the firm as on 30th June, 2020 was as under:

Balance Sheet of M/s. TB as on 30-6-2020

Liabilities		₹	Assets	₹
Capital Accounts:			Land	1,20,000
A	1,24,000		Building	2,20,000
B	96,000		Plant and Machinery	4,00,000
C	1,60,000	3,80,000	Investments	42,000
Long Term Loan		4,20,000	Inventories	1,36,000
Bank Overdraft		64,000	Trade receivables	1,59,000
Trade payables		2,13,000		
		10,77,000		10,77,000

It was mutually agreed that B will retire from partnership and in his place D will be admitted as a partner with effect from 1st July, 2020. For this purpose, following adjustments are to be made:

(a) Goodwill of the firm is to be valued at ₹ 3 lakhs due to the firm's location advantage but the same will not appear as an asset in the books of the reconstituted firm.

(b) Building and Plant & Machinery are to be valued at 95% and 80% of the respective balance sheet values. Investments are to be taken over by the retiring partner at ₹ 46,000. Trade receivables are considered good only upto 85% of the balance sheet figure. Balance to be considered bad.

(c) In the reconstituted firm, the total capital will be ₹ 4 lakhs, which will be contributed by A, C and D in their new profit sharing ratio, which is 3:4:3.

(d) The amount due to retiring partner shall be transferred to his loan account.

You are required to prepare Revaluation Account and Partners' Capital Accounts after reconstitution, along with working notes.

Solution

Revaluation Account

Particulars	₹	Particulars		₹
To Buildings	11,000	By Investments		4,000
To Plant & Machinery	80,000	By Loss transferred		
To Bad Debts	23,850	A's Capital	33,255	
		B's Capital	22,170	
		C's Capital	55,425	1,10,850
	1,14,850			**1,14,850**

Partner's Capital Accounts

Particulars	A	B	C	D	Particulars	A	B	C	D
To Revaluation	33,255	22,170	55,425	--	By Bal. b/d	1,24,000	96,000	1,60,000	--
To Investments	--	46,000	--	--	By D's Capital	-	60,000	30,000	--
To B's Loan	-	87,830	-	--					
To B & C's Capital	-	-	-	90,000	By Bank (Bal. Fig.)	29,255	--	25,425	2,10,000
To Bal. c/d	1,20,000	--	1,60,000	1,20,000					
	1,53,255	**1,56,000**	**2,15,425**	**2,10,000**		**1,53,255**	**1,56,000**	**2,15,425**	**2,10,000**

Working Note:

1. Calculation for adjustment of Amount of Goodwill

Particulars	A	B	C	D
Credit in Old Ratio (3:2:5)	90,000	60,000	1,50,000	
Debit in New Ratio (3:4:3)	90,000	-	1,20,000	90,000
	-	**60,000 Cr.**	**30,000 Cr.**	**90,000 Dr.**

2. Capital of partners in the reconstituted firm :

Total capital of the reconstituted firm (given) 4,00,000

A (3/10) 1,20,000   B (4/10) 1,60,000   C (3/10) 1,20,000

RIGHT OF OUTGOING PARTNER TO SHARE SUBSEQUENT PROFITS / CALCULATION OF RELIEF u/s 37

Relief is allowed to outgoing partner. The same can be due to Retirement/Death.
Relief is allowed only if:

a) Outgoing partner's balance has not been fully settled
b) Firm does not allow only interest/share of profits on unsettled balance. i.e., partnership deed is silent.

- Relief is higher of the following

Unsettled balance X 6% p.a. X Period upto relief date

OR

$$\frac{\text{Profits earned upto relief date X Unsettled balance of outgoing partner}}{\text{Total capital of partners \& unsettled balance.}}$$

Note: Capital of partners should be calculated on the date of death/retirement after all adjustments.

Example

A, B, C having PSR 1 : 1 : 1. C retires on 31.10.2022 Capital of partners after all adjustments stood at ₹ 50,000, ₹ 75,000 & ₹ 1,20,000 respectively. A & B continued to carry on business without settling C's account. Final payment to C is made on 1.02.2023. Profits made during 3 months period amounted to ₹ 28,000. Find Relief u/s 37

Relief u/s 37

31/10/22 → 1/2/23

3M

1) $120000 \times 6\% \times \frac{3}{12} = 1800$

OR

2) $28000 \times \frac{120000}{245000} = 13714$

245000 → P: 28000

120000 →

$\boxed{\text{Relief} = 13714}$

JOINT LIFE POLICY

Joint Life Policy (JLP)

It is an insurance policy which is taken out by the partnership firm on the lives of all the partners. The amount of policy is payable by the Insurance Company either on the death or on maturity of policy, whichever is earlier. The firm pays annual premium to the insurer against the policy. The objective of taking such a policy is to minimize the financial hardships to the event of payment of a large sum to the legal representatives of a deceased partner or to the retiring partner.

Instead of life policy taken jointly on the name of all the partners, all the partners may take individual life policies for each of them by paying the premium from the firm

ACCOUNTING TREATMENT OF JOINT LIFE POLICY

METHOD 1: PREMIUM PAID IS TREATED AS EXPENSE (ORDINARY EXPENSE METHOD)

In this case premium is treated as an expense and it is closed every year by transferring to profit and loss account.

1.	Payment of Premium	Insurance Premium A/c Dr. To Bank A/c
2.	Transfer to P&L A/c	Profit & Loss A/c Dr. To Insurance Premium

METHOD 2: PREMIUM PAID IS TREATED AS ASSET (SURRENDER VALUE METHOD)

In this case insurance premium paid is first debited to life policy account and credited to bank account. At the end of the year the amount in excess of surrender value is treated as a loss and is transferred to Profit and Loss Account.

1.	Payment of Premium	JLP A/c Dr. To Bank A/c
2.	Transfer to P&L A/c	Profit & Loss A/c Dr. To JLP (JLP A/c Balance- its Surrender Value)

METHOD 3: PREMIUM PAID IS TREATED AS ASSET & RESERVE IS MAINTAINED (RESERVE METHOD)

Under this method, premium paid is debited to policy account and credited to bank account. At the end of the year, amount equal to premium is transferred from Profit and Loss Appropriation Account to Policy Reserve Account.

After this, policy account is brought down to its surrender value by debiting the life policy reserve account with amount which exceeds the surrender value of the policy.

1.	Payment of Premium	JLP A/c Dr. To Bank A/c
2.	Creation of Reserve	Profit & Loss Appropriation A/c Dr. To JLP Reserve
3.	Amount in excess of Surrender Value	JLP Reserve A/c Dr. To JLP A/c

Note: In the balance sheet JLP will appear on the Asset side & JLP Reserve will appear on the liability side at surrender value.

Example:

A, B and C shared profits and losses in the ratio of 5:3:2. They took out a joint life Policy in 2021 for ₹1,00,000, a premium of ₹5,000 being paid annually on 1st January. The surrender value of the policy on 31st December of various years was as follows: 2021 Nil; 2022 ₹ 3,000; 2023 ₹ 6,500. Prepare ledger accounts

Case 1: Assuming Ordinary Expense Method.

Case 2: Assuming Surrender Value Method.

Case 3: Assuming Reserve Method.

Case 1:

JLP Premium A/c

1/1/21	To Bank A/c	5000	31/12	By P&L A/c	5000
1/1/22	To Bank A/c	5000	31/12	By P&L A/c	5000
1/1/23	To Bank A/c	5000	31/12	By P&L A/c	5000

B/s

	JLP ×

Case 2:

JLP A/c

1/1	To Bank	5000	31/12	By P&L A/c	5000
1/1	To Bank	5000	31/12	By P&L A/c	2000
				By Bal c/d	3000
1/1	To Bal b/d	3000		By P&L A/c (B/F)	1500
	To Bank	5000		By Bal c/d	6500

B/s

Assets	1	2	3
JLP	0	3000	6500

Case 3: Reserve Method

B/s

JLP Res	1	2	3	Assets	1	2	3
	0	3000	6500	JLP	0	3000	6500

JLP A/c

I	To Bank A/c	5000	By JLP Res. A/c	5000
II	To Bank A/c	5000	By JLP Res. A/c	2000
			By Bal c/d	3000
III	To Bal b/d	3000	By JLP Res.	1500
	To Bank	5000	By Bal c/d	6500

JLP Reserve A/c

To JLP A/c	5000	By P&L App. A/c	5000
To JLP	2000	By P&L App. A/c	5000
To Bal c/d	3000		
To JLP	1500	By Bal b/d	3000
To Bal c/d	6500	By P&L App. A/c	5000

DEATH OF PARTNER

Joint Life Policy [Policy Amount]

Ordinary Expense Method	Asset/Surrender Value Method	JLP & JLP Reserve Method
[JLP is not appearing in Books]	[JLP appearing in Books at Surrender Value]	[Reserve Method]
* Premium Charged to P&L A/c every year	* JLP shown as asset at S.V.	* Both maintained at S.V.
* Amount Received (Policy Amount) is credited to Partner's Capital A/c in PSR	* Amount received (net of S.V.) credited to Partner's Capital A/c	* Amount Received is credited to Partner's Capital A/c in PSR

Example:

A, B and C shared profits and losses in the ratio of 3:2:1. C died on 31.03.2023

Policy Amount 1,20,000 & Surrender Value 30,000

Case 1: JLP is not appearing in the books/Ordinary Expense Method

Case 2: JLP is appearing in the books at Surrender Value

Case 3: JLP & JLP Reserve are maintained at Surrender Value

Bank A/c -Dr 120000
To JLP 120000

Case 1:

JLP A/c -Dr 120000
To A 60000
To B 40000
To C 20000

Case 2:

JLP A/c -Dr 90000
To A 45000
To B 30000
To C 15000

Case 3:

JLP Reserve A/c -Dr 30000
To JLP A/c 30000

JLP A/c -Dr 120000
To A 60000
To B 40000
To C 20000

RETIREMENT OF PARTNER

JOINT LIFE POLICY [SURRENDER VALUE]

Ordinary Expense Method	Asset/Surrender Value Method	JLP & JLP Reserve Method
[JLP is not appearing in Books]	[JLP appearing in Books at Surrender Value]	[Reserve Method]
Amount Received (Surrender Value) is credited to Partner's cap. A/c in PSR	No Treatment	Distribute JLP Reserve in Their PSR

Example:
A, B and C shared profits and losses in the ratio of 3:2:1. C retired on 31.03.2021
Policy Amount 1,20,000 & Surrender Value 30,000
Case 1: JLP is not appearing in the books/Ordinary Expense Method
Case 2: JLP is appearing in the books at Surrender Value
Case 3: JLP & JLP Reserve are maintained at Surrender Value

Bank A/c -Dr	30000	
To JLP		30000

Case 1:

JLP A/c -Dr	30000	
To A		15000
To B		10000
To C		5000

Case 2:

No Treatment

Case 3:

JLP Reserve A/c -Dr	30000	
To JLP A/c		30000
JLP A/c -Dr	30000	
To A		15000
To B		10000
To C		5000

DEATH OF PARTNER

Separate/Individual Life Policy

Surrender value not appearing in books	Surrender value appearing in books
Share in Own Policy + Share in Surrender value of Remaining Partner's Policy	Share in Own Policy (Remaining Balance) [i.e. Policy Amount − S.V.]

Example:

A, B and C shared profits and losses in the ratio of 3:2:1. C died on 31.03.2021

	Policy Amount	Surrender Value
A	2,00,000	30,000
B	3,00,000	60,000
C	4,80,000	90,000

Case 1: Surrender Value not appearing in the books

Case 2: Surrender Value appearing in the books

Case 1:

C's share = $480000 \times \frac{1}{6} = 80000$

+

$90000 \times \frac{1}{6} = 15000$

(30000 + 60000)

95000

Case 2:

C's share = $(480000 - 90000) \times \frac{1}{6} = 65000$

RETIREMENT OF PARTNER

Separate / Individual Life Policy

- Surrender value not appearing in books
  - Share in Surrender value of all Partner's Life Policies
- Surrender value appearing in books
  - NO Treatment

Example:

A, B and C shared profits and losses in the ratio of 3:2:1. C retired on 31.03.2021

	Policy Amount	Surrender Value
A	2,00,000	30,000
B	3,00,000	60,000
C	4,80,000	90,000

Case 1: Surrender Value not appearing in the books

Case 2: Surrender Value appearing in the books

Case 1:

C's share = $90000 \times \frac{1}{6} = 15000$

+

$90000 \times \frac{1}{6} = 15000$

(30000 + 60000)

30000

Case 2:

No Treatment

Question 8: (ICAI Study Material)

Diya Riya & Kiya are partners of M/s. DRK Fabrics sharing profits and losses in the ratio of 2:1:2. On 31st March 2023 their Balance Sheet was as under:

Liabilities		₹	Assets	₹
Capital Accounts:			Land & Building	1,65,000
Diya	1,50,000		Furniture	75,000
Riya	1,80,000		Joint Life Policy	60,000
Kiya	70,000	4,00,000	Inventory	88,740
General Reserve		1,40,000	Trade Receivables	96,750
Trade Payables		60,000	Bank	1,14,510
		6,00,000		6,00,000

Kiya died on 30th September, 2023. The partnership deed provides as follows:

(a) That partners be allowed interest at 12% p.a. on their capitals, but no interest be charged on drawings.

(b) That upon the death of a partner, the goodwill of the firm be valued at one years' purchase of the average net profits (after charging interest on capital) for the four years to 31st March preceding the death of a partner.

The profits of the firm before charging interest on capitals were

2019-20	1,62,000	2020-21	1,99,000
2021-22	1,87,000	2022-23	1,96,000

Average capital during preceding four years may be assumed as ₹ 3,00,000

(c) Profits till the date of death to be ascertained on the basis of average profit of previous four years

(d) Upon the death of a partner, she is to be credited with her share of the profits, interest on capitals etc. calculated till the date of death

After the death of Kiya

1. ₹ 2,00,000 was received from insurance company against Joint life Policy.
2. Land & Building was appreciated by 20%, Furniture to be depreciated by 10%, inventory to be revalued at ₹ 80,000. Bad debts amounted ₹ 1760.
3. Amount payable to Kiya was paid in cash.

You are required to prepare

1. Revaluation A/c
2. Partners' Capital A/c
3. Balance Sheet as on 30th September 2023, assuming other Assets and liabilities remaining the same.

Solution

Revaluation Account

Particulars	Amount	Particulars	Amount
To Furniture	7,500	By Land and Building	33,000
To Inventory	8,740		
To Bad Debts	1,760		
To Profit transferred			
Diya	6,000		
Riya	3,000		
Kiya	6,000		
	33,000		**33,000**

Partners' Capital Accounts

	Diya	Riya	Kiya		Diya	Riya	Kiya
To Kiya's Cap.	40,000	20,000	-	By Balance b/d	1,50,000	1,80,000	70,000
To Bank	-	-	2,79,800	By Revaluation	6,000	3,000	6,000
			-	By Gen. Reserve	56,000	28,000	56,000
				By Interest on Capital (70,000 *12%*6/12)			4,200
To Balance c/d	2,28,000	2,19,000		By Joint Life Policy	56,000	28,000	56,000
				By P&L Suspense A/c	-	-	27,600
				By Diya & Riya Cap. Acc			60,000
	2,68,000	**2,39,000**	**2,79,800**		**2,68,000**	**2,39,000**	**2,79,800**

Balance Sheet as at 30.09.2023

Liabilities		₹	Assets	₹
Capital Accounts:			Land & Building	1,98,000
Diya	2,28,000		Furniture	67,500
Riya	2,19,000	4,41,000	Inventory	80,000
Trade Payables		60,000	Trade Receivables	94,990
			Bank (1,14,510+2,00,000-2,79,800)	34,710
			Profit & Loss Suspense A/c (incl. Interest on Capital)	31,800
		5,07,000	(27600 + 4200)	**5,07,000**

Working Notes:

1. **Goodwill Valuation**

Average Profits before Interest on Capital = $\frac{1,62,000+1,99,000+1,87,000+1,96,000}{4}$

= 1,86,000

Less: Interest on Capital (3,00,000*12%) = (36,000)

Adjusted Average Profit = 1,50,000

Goodwill = 1,50,000 * 1 = 1,50,000

Particulars	Diya	Riya	Kiya
Credit in Old Ratio (2:1:2)	60,000	30,000	60,000
Debit in New Ratio (2:1)	(1,00,000)	(50,000)	
	40,000 Dr.	**20,000 Dr.**	**60,000 ~~Dr.~~ Cr.**

2. **Calculation of Kiya's share of Profit**

Average Profit for full year before interest on capital = 1,86,000
6 months Profit = 93,000
Less: Interest on Capital (4,00,000*12%*6/12) = (24,000)
(Considered actual Capital as on 01.04.23)
Adjusted profit till the date of death = 69,000
Kiya's share 2/5th = 27,600

3. **Joint Life Policy**

The JLP in this question is based on surrender value method- where in the amount shown in the balance sheet shall be deducted from the JLP proceeds received from insurance co, on the death of a partner.-

2,00,000 - 60,000 (Balance Sheet Value) = 1,40,000- divided in profit sharing ratio between the partners.

Note: Interest on capital only credited to Kiya (partner which died) & not to other partners on the assumption that remaining partners will be given their Interest on capital at the end of year. We are settling only the account of the partner which has died. However, Interest on capital can be credited to other partners as well.

Question 9: (CA Foundation Jan 2021) (10 Marks)

The partnership deed of a firm consisting of 3 partners - P, Q and R (profit sharing ratio being 2:1:1) & whose fixed capitals are ₹ 30,000, ₹ 12,000 & ₹ 8,000 respectively provides as follows:

(i) The partners be allowed interest @ 8% p.a. on their fixed capitals, but no interest to be allowed on undrawn profits or charged on drawings.

(ii) That upon the death of a partner, the goodwill of the firm be valued at 2 years purchase of the average net profit (after charging interest on capital) for the 3 years to 31st December preceding the death of a partner.

(iii) That an insurance policy of ₹ 25,000 each was taken in individual names of each partner. The premium was charged against the profits of the firm. The surrender value of the policy was 20% of the sum assured.

(iv) Upon the death of a partner, he is to be credited with his share of the profits, interest on capitals, etc. calculated upto 31st December following his death.

(v) That the share of the partnership policy and goodwill be credited to a deceased partner as on 31st December following his death.

(vi) That the partnership books to be closed annually on 31st December.

P died on 30th September, 2020. The amount standing to the credit of his current account as on 31st December, 2019 was ₹ 5,000 and from that date to the date of death he had withdrawn₹ 30,000 from the business.

An unrecorded liability of ₹ 6,000 was discovered on 30th September, 2020 and it was decided to record it and immediately pay it off.

The trading results of the firm (before charging interest on capital) had been as follows:

2017 Profit ₹ 29,340

2018 Profit ₹ 26,470

2019 Loss ₹ 8,320

2020 Profit ₹ 13,470

You are required to prepare an account showing amount due to P's legal heir as on 31st December, 2020.

Note: Impact for unrecorded liability not to be given in earlier years.

Solution

P's Capital Account

2020		₹	2020		₹
Sep. 30	To Current A/c	25,000	Jan. 1	By Balance b/d	30,000
	(30,000 - 5000)		Dec. 31	By Profit and Loss A/c :	
Dec. 31	To Profit and Loss Adjt.	3,000		Interest on Capital	2,400
	(Unrecorded Liability)		Dec. 31	Share of Profit	4,735
Dec. 31	To Balance Transferred to P's Executor's A/c	38,465		Q & R (Goodwill)	11,830
			Dec. 31	Insurance Policies A/c	17,500
		66,465			**66,465**

Working Notes:

(i) Valuation of Goodwill

Year	Profit before Interest on fixed capital ₹	Interest ₹	Profit after interest ₹
2017	29,340	4,000	25,340
2018	26,470	4,000	22,470
2019	(-) 8,320	4,000	(-) 12,320
	47,490	**12,000**	**35,490**

Average	11,830	
Goodwill at two years purchase of average net profits	23,660	
Share of P in the goodwill	11,830	(23660 X 2/4)

(ii) Profit on Separate Life Policy:

P's policy	25,000
Q and R's policy @ 20% of ₹ 50,000	10,000
	35,000
Share of P (1/2)	17,500

(iii) Share in profit for 2020:

Profit for the year		13,470
Less : Interest on capitals	(50000 X 8%)	(4,000)
		9,470
P's share in profit (1/2)		4,735

Question 10: (CA Foundation July 2021) (10 Marks)

It was provided under the Partnership Agreement between Ram, Laxman and Bharat that in the event of death of a partner, the survivors would have to purchase his share in the firm on the following terms:

(a) Goodwill is to be valued at 3 year's purchase of simple average profits of last 4 completed years.

(b) Outstanding amount due to the representative of a deceased partner shall be paid in 4 equal half yearly installments commencing 6 months after the death plus interest @ 5% p.a. on the outstanding dues.

They shared profit and loss in the ratio 9:4:3.

Ram died on 30th September 2020 and Partner's Capital account balances on that date were: Ram - ₹ 21,600, Laxman - ₹ 12,800 and Bharat - ₹ 7,200. Ram's current account on 30th September, 2020 after crediting his share of profit to that date, however showed a debit balance of ₹ 1,920.

Firm profits were for the year ended

- 31st March, 2017 ₹ 70,400
- 31st March, 2018 ₹ 56,320
- 31st March, 2019 ₹ 48,160
- 31st March, 2020 ₹ 17,408

Show Ram's Capital Account and Executor's Account (of Ram) till full payment is made to Ram's Executor.

Solution 3: Journal Entries

			Debit	Credit
1)	Fixed Assets A/c -Dr		30000	
	Inventories A/c -Dr		10000	
	To Revaluation A/c			40000
2)	Revaluation A/c -Dr		5000	
	To B/R A/c			5000
3)	Revaluation A/c -Dr		35000	
	To F's capital A/c			14000
	To G's capital A/c			14000
	To K's capital A/c			7000
4)	Reserve A/c -Dr		10000	
	To F's cap. A/c			4000
	To G's cap. A/c			4000
	To K's cap. A/c			2000

5)	F's capital A/c - Dr		10000	
	To K's capital A/c			10000
6)	Bank A/c - Dr		104000	
	To F's cap. A/c			70000
	To G's cap. A/c			34000
7)	K's capital A/c - Dr		79000	
	To Bank A/c			79000

Capital Accounts

	F	G	K		F	G	K
To K's cap. A/c	10000			By Bal b/d	120000	80000	60000
To Bank (B.f)			79000	By Revaluation	14000	14000	7000
				By Reserve	4000	4000	2000
				By F's cap. A/c			10000
To Bal c/d (NN)	198000	132000		By Bank (B.f)	70000	34000	
	=	=	=		=	=	=

G/W = 50000

	F	G	K
Cr in OR (2:2:1)	20000	20000	10000
Dr in NR (3:2)	(30000)	(20000)	—
	10000 Dr	—	10000 Cr

Balance sheet

Liabilities			Assets	
Capital A/cs			Fixed Assets	180000
F	198000		Inventories	60000
G	132000	330000	Bank	75000
Trade Payables		50000	Trade Rec.	65000
		380000		380000

WN

Computation of Capital

Fixed Assets	180000
Inventories	60000
Bank	75000
Trade Rec.	65000
Trade Payables	(50000)
	330000

Shared in PSR 3:2

F's Cap. 198000

G's Cap: 132000

Solution 10:

Computation of Goodwill

Average Profits = $\frac{70400 + 56320 + 48160 + 17408}{4} = 48072$

G/W = $48072 \times 3 = 144216$

Ram's share = $144216 \times \frac{9}{16} = 81121.50$

r/off to 81122

Ram's Capital A/c

To Ram's Current A/c	1920	30/9	By Bal b/d	21600
To Ram's Executor A/c (B.f.)	100802		By Laxman & Bharat's Cap. A/c (Share of G/W)	81122

4 equal principal Amt. = $\frac{100802}{4} = 25200.50$

Ram's Executor A/c

Date	Particulars	Amount	Date	Particulars	Amount
31/3	To Bank A/c (25200.50 + 2520)	27720.50	30/9/20	By Ram's capital A/c	100802
31/3/21	To Bal c/d (B.f.)	75601.50	31/3	By Interest (100802 x 5% x 6/12)	2520
30/9/21	To Bank A/c (25200.50 + 1890)	27090.50	1/4/21	By Bal b/d	75601.50
31/3/22	To Bank A/c (25200.50 + 1260)	26460.50	30/9	By Interest A/c (75601.50 x 5% x 6/12)	1890
	To Bal c/d	25200.50	31/3	By Interest A/c (50401 x 5% x 6/12)	1260
30/9	To Bank A/c	25830.50	1/4/22	By Bal b/d	25200.50
			30/9	By Interest (25200.50 x 5% x 6/12)	630

Partnership:

Dissolution of Firm & LLP

DISSOLUTION OF FIRM AND LLP

DISSOLUTION

A partnership is dissolved or comes to an end on:

- expiry of the term for which it was formed or completion of the venture for which it was entered into
- death of a partner
- insolvency of a partner.

However, the partners or remaining partners (in case of death or insolvency) may continue to do the business. In such case there will be a new partnership but the firm will continue. When the business comes to an end then only it will be said that the firm has been dissolved

A firm stands dissolved in the following cases:

- The partners agree that the firm should be dissolved
- All partners except one become insolvent
- The business becomes illegal
- In case of partnership at will, a partner gives notice of dissolution and
- The court orders dissolution

The court has the option to order dissolution of a firm in the following circumstances:
(a) Where a partner has become of unsound mind;
(b) Where a partner suffers from permanent incapacity;
(c) Where a partner is guilty of misconduct of the business;
(d) Where a partner persistently disregards the partnership agreement;
(e) Where a partner transfers his interest or share to a third party;
(f) Where the business cannot be carried on except at a loss; and
(g) Where it appears to be just and equitable.

Distinction Between Dissolution of Partnership & Dissolution of Firm

S. No.	Dissolution of Partnership	Dissolution of Partnership Firm
1	Refers to the discontinuance of the relation between the partners of firm.	Implies that entire firm ceases to exist, including the relation among all partners
2	There can be change in PSR or admission/death/retirement of a partner	Dissolution of partnership firm occurs
3	In event of dissolution of the partnership, the business continues as usual, but the partnership is reconstituted.	In event of the dissolution of the firm, the business ceases to end.
4	There is no intervention by the court.	Court has inherent power to intervene. By its order, a firm can be dissolved.
5	Economic relationships among partners may remain same or change.	Economic relationship among partners comes to an end.
6	Assets and liabilities are revalued. New balance sheet is prepared	Assets are sold and realized. Liabilities are paid off.
7	Revaluation account is prepared	Realization account is prepared.
8	Books of accounts are not closed.	Books of accounts are closed.

WINDING UP OF A LIMITED LIABILITY PARTNERSHIP (LLP)

The winding up of a LLP may be either voluntary or by the Tribunal and LLP, so wound up may be dissolved. Winding up of a LLP may be initiated by Tribunal if:

- The LLP wishes to wind up;

- The LLP has less than 2 partners for more than 6 months;
- The LLP is unable to pay its debts;
- The LLP has not acted in the interest of the sovereignty and the integrity of India;
- The LLP has failed to submit with the statements of accounts and solvency or the LLP annual returns for more than five consecutive financial years with the Registrar;
- The Tribunal thinks that it is Just and Equitable that the LLP should be wound up.

ACCOUNTING ENTRIES: BOOKS OF FIRM

1. Transfer of Assets to Realisation Account

Realisation A/c Dr. To Sundry Assets A/c

- By Name of Individual Assets
- To be transferred at *BOOK VALUE*
- Do not transfer the following.
  - Fictitious Assets
  - P & L debit balance
  - Cash & Bank balance
  - Current & Capital Account debit balance
- If any asset is having corresponding provision, then gross value to be transferred.

2. Transfer of Outsider's Liabilities to Realisation Account

Liabilities A/c Dr. To Realisation A/c

- By Name of Individual Liabilities
- To be transferred at *BOOK VALUE*
- Do not transfer the following
  - Partner's capital & current account balances
  - Reserves and surplus
  - Partner's Loan
- Any provision appearing on asset side is to be debited in this entry

3. Realisation of All Assets (whether recorded or unrecorded)

When assets are sold for cash	Cash/Bank A/c Dr. To Realisation Account
When assets are taken away by the partners	Partner's Capital A/c Dr. To Realisation Account
When assets are given away to any of the creditors towards his dues	No Entry

4. Discharge of Outsider's Liabilities (whether recorded or unrecorded)

When the liabilities are discharged in cash	Realisation Account Dr. To Cash/Bank A/c
When any of the partners agree to discharge the liability	Realisation Account Dr. To Partner's Capital A/c

5. Realisation Expenses:

When expenses are paid by the firm on its own behalf	Realisation Account Dr. To Cash/Bank A/c
When expenses are paid by a partner on firm's behalf	Realisation Account Dr. To Partner's Capital A/c

6. Payment of Partner's Loan /Advance

Partner's Loan A/c Dr. To Capital A/c (Only to the extent of Dr. Balance in Capital A/c) To Cash/Bank A/c

7. Ascertainment of Profit/Loss on Realisation A/c & Transfer in Profit Sharing Ratio (PSR)

A: If Profit	B: If Loss
Realisation A/c Dr. To All Partner's Capital A/c	All Partner's Capital A/c Dr. To Realisation A/c

8. Transferring Accumulated Profits/Reserves & Losses to Partner's Capital Account in PSR

For Transfer of Accumulated Profits & Reserves
General Reserves A/c Dr. P&L A/c Dr. To All Partner's Capital A/c *Reverse entry to be passed in case of Accumulated Losses*

Realisation Account

To Sundry Assets (Individually at Book value) × Cash & Bank × Losses × Adv. to partner Current/Capital (Dr. Bal.)		By Sundry Liabilities (outsider) (Individually at Book value) × Capital/Current A/c × Reserves & Profits × Partner's Loan A/c — separately paid off (Exception)	
To Cash & Bank / Partner's Capital A/c (Paid value) (Taken over value) [Including unrecorded Liabilities/ Dissolution Expences]		By Cash & Bank / Partner's Capital A/c (Realised value) (Taken over value) [Including unrecorded Assets]	
To Profit Tfd. to Partner's cap. A/c (B.f.) (PSR)		By Loss tfd. to Partner's cap. A/c (B.f.) (PSR)	

NOTES:

1) Debtors & Provision for Doubtful Debts

Balance Sheet

Liabilities		Assets	
		Debtors 50000 - Provision for Doubtful debt (3000)	47000

Realisation A/c

To Debtors	50000	By Provision for Doubtful Debt	3000

2) Treat Goodwill just like any other normal asset.

Transfer Goodwill to Realisation A/c by passing entry:

Realisation A/c – Dr.

To Goodwill A/c

3) If any asset is assigned for settlement of liability

Only transfer to Realisation A/c with no further effect.

Balance Sheet

Liabilities		Assets	
Creditors	100000	Stock	80000

Realisation A/c

To Stock	80000	By Creditors	100000

4) Question is silent on payment of liabilities & realisation of assets.

For Liabilities: Full payment is made.

For Assets: Depends on nature & value of asset.

Option 1: Assume full value realised.

Option 2: Assume Nil value realised

[Eg. Goodwill, Prepaid Expenses, etc.]

Question 1: (ICAI Study Material)

P, Q and R are partners sharing profits and losses as to 2:2:1. Their Balance Sheet as on 31st March, 2023 is as follows:

Liabilities	₹	Assets	₹
Partners' Capitals:		Plant and Machinery	1,08,000
P	1,20,000	Fixtures	24,000
Q	48,000	Stock in trade	60,000
R	24,000	Sundry debtors	48,000
Reserve Fund	60,000	Cash in hand	60,000
Creditors	48,000		
	3,00,000		**3,00,000**

They decided to dissolve the business. The following are the amounts realized:

	₹
Plant and Machinery	1,02,000
Fixtures	18,000
Stock	84,000
Sundry debtors	44,400

Creditors allowed a discount of 5% and realization expenses amounted to ₹ 1,500. There was an unrecorded asset of ₹ 6,000 which was taken over by Q at ₹ 4,800. A bill for ₹ 4,200 due for GST was received during the course of realization and this was also paid. Prepare:

(i) Realisation account.
(ii) Partners' capital accounts.
(iii) Cash account.

Question 2: (ICAI Study Material) / (RTP Nov 2021)

P and Q were partners sharing profits equally in LLP. Their Balance Sheet as on March 31, 2023 was as follows:

Liabilities		Amount	Assets	Amount
Capitals:			Bank	30,000
P	1,00,000		Debtors	25,000
Q	50,000	1,50,000	Stock	35,000
Creditors		20,000	Furniture	40,000
Q's current account		10,000	Machinery	60,000
Reserves		15,000	P's current account	10,000
Bank overdraft		5,000		
		2,00,000		2,00,000

The firm was dissolved on the above date:

P took over 50% of the stock at 10% less on its book value, and the remaining stock was sold at a gain of 15%. Furniture and Machinery realized for ₹ 30,000 and ₹ 50,000 respectively; There was an unrecorded investment which was sold for ₹ 25,000; Debtors realized 90% only and ₹ 1,245 were recovered for bad debts written off last year; There was an outstanding bill for repairs which had to be paid for ₹ 2,000.

You are required to prepare Realization Account, Partners' capital accounts (including transfer of current account balances) and Bank Account in the books of the firm.

Question 3: (ICAI Study Material) / (RTP Nov 2020) (Similar)

Amit, Sumit & Kumar are partners sharing profit & losses in ratio 2:2:1. The partners decided to dissolve the partnership on 31st March, 2023 when their Balance Sheet was as under:

Liabilities	Amount	Assets	Amount
Capital Accounts:		Land & Building	1,35,000
Amit	55,200	Plant & Machinery	45,000
Sumit	55,200	Furniture-	25,500
General Reserve	61,500	Investments	15,000
Kumar's Loan A/c	15,000	Book Debts 60,000	
Loan from D	1,20,000	Less: Prov. for bad debts (6,000)	54,000
Trade Creditors	30,000	Stock	36,000
Bills Payable	12,000	Bank	13,500
Outstanding Salary	7,500	Capital withdrawn: Kumar	32,400
	3,56,400		3,56,400

The following information is given to you:

(i) Realisation expenses amounted to ₹ 18,000 out of which ₹ 3,000 was borne by Amit.

(ii) A creditor agreed to takeover furniture of book value ₹ 12,000 at ₹ 10,800. The rest of the creditors were paid off at a discount of 6.25%.

(iii) The other assets realized as follows:

Furniture - Remaining taken over by Kumar at 90% of book value

Stock - Realised 120% of book value

Book Debts - ₹ 12,000 of debts proved bad, remaining were fully realized

Land & Building - Realised ₹ 1,65,000

Investments - Taken over by Amit at 15% discount

(iv) For half of his loan, D accepted Plant & Machinery and ₹ 7,500 cash. The remaining amount was paid at a discount of 10%.

(v) Bills payable were due on an average basis of one month after 31st March, 2023, but they were paid immediately on 31st March @ 6% discount "per annum".

Prepare Realisation Account, Bank Account and Partners Capital Accounts in books of firm.

Solution

REALISATION ACCOUNT

To Land and Building		1,35,000	By Provision for bad debts		6,000
To Plant & Machinery		45,000	By Loan from D		1,20,000
To Furniture		25,500	By Creditors		30,000
To Investments		15,000	By Bills payable		12,000
To Book Debts		60,000	By Outstanding salary		7,500
To Stock		36,000	By Kumar's Capital		
To Amit's Capital			Furniture	12,150(13,500*.09)	12,150
Real. Expenses	3,000	3,000	By Amit's Capital		
To Bank			Investments	12,750	12,750
Bill payable	11,940		By Bank A/c		
D's Loan (7,500+54,000)	61,500		Stock	43,200	
Creditors	18,000		Debtors	48,000	
Salary	7,500		Land & Building	1,65,000	2,56,200
Real. Expenses	15,000	1,13,940			
To Profit transferred					
Amit	9,264				
Sumit	9,264				
Kumar	4,632	23,160			
		4,56,600			**4,56,600**

PARTNER'S CAPITAL ACCOUNTS

	Amit	Sumit	Kumar		Amit	Sumit	Kumar
To Balance b/d	-	-	32,400	By Balance b/d	55,200	55,200	-
				By General reserve	24,600	24,600	12,300
To Realisation A/c	12,750	-	12,150	By Kumar's Loan	-	-	15,000
To Bank	79,314	89,064	-	By Realisation A/c	3,000	-	-
				By Realisation A/c (Profit)	9,264	9,264	4,632
				By Bank	-	-	12,618
	92,064	**89,064**	**44,550**		**92,064**	**89,064**	**44,550**

BANK ACCOUNT

	₹		₹
To Balance b/d	13,500	By Realisation A/c	1,13,940
To Realisation A/c	2,56,200	By Amit's Capital	79,314
To Kumar's Capital	12,618	By Sumit's Capital	89,064
	2,82,318		**2,82,318**

Working Notes:

1. <u>Amount paid to creditors</u>

Book Value	30,000
Less: Creditors taking over Furniture	(10,800)
	19,200
Less: Discount @ 6.25%	(1,200)
	18,000

2. <u>Payment to Bills Payable</u>

Book Value	12,000
Less: Discount for early payment {12,000 x 6% x (1/12)}	(60)
	11,940

3. <u>Payment to D's Loan</u>

Book value	1,20,000
50% of Loan adjusted as below:	
Plant & Machinery accepted at Book Value (₹ 45,000) and ₹ 7,500 in cash	7,500
Balance 50% of Loan adjusted as below:	
In cash after allowing discount of 10% i.e. ₹ 60,000 – ₹ 6,000 = ₹ 54,000.	54,000

4. <u>Furniture taken over by Kumar</u>

Book value	25,500
Less: Furniture of Book Value ₹ 12,000 accepted by trade creditors	(12,000)
	13,500
Less: 10% of Book Value	(1,350)
	12,150

TOPIC: INSOLVENCY OF PARTNER

CONSEQUENCES OF INSOLVENCY OF A PARTNER

1. The partner adjudicated as insolvent ceases to be a partner on the date on which the order of adjudication is made.
2. The firm is dissolved on the date of the order of adjudication unless there is a contract to the contrary.
3. The estate of insolvent partner is not liable for any act of firm after the date of order of adjudication
4. The firm cannot be held liable for any acts of insolvent partner after the date of order of adjudication.

Insolvency of Partner
[GARNER vs MURRAY]

1) Deficiency / Shortage on account of insolvency of partner to be borne by remaining (other) solvent partners (having credit balance) in their last agreed capital ratio

2) Realisation loss to be brought in cash by all the solvent partners (including Dr. Balance)

Last Agreed Capital Ratio
(upto the date of dissolution of firm)

Fixed Capital → Ratio of Fixed capital

Fluctuating Capital →

Capital Balances in B/s	xx
± Effect of Reserves, Profits & Losses	xx
	xx

Non Applicability of Garner vs Murray

1. When the solvent partner has a debit balance in the capital account. Only solvent partners will bear the loss of capital deficiency of insolvent partner in their capital ratio. If incidentally a solvent partner has a debit balance in his capital account, he will escape the liability to bear the loss due to insolvency of another partner.
2. When the firm has only two partners.
3. When there is an agreement between the partners to share the deficiency in capital account of insolvent partner.
4. When all the partners of the firm are insolvent.

Insolvency of all Partners

- When the liabilities of the firm cannot be paid in full out of the firm's assets as well as personal assets of the partners, then all the partners of the firm are said to be insolvent. Under such circumstances don't transfer creditors (Outsider Liabilities) to Realisation A/c.
- Creditors (Outsider Liabilities) may be paid the amount available including the amount contributed by the partners in the ratio of their outstanding amount.

Question 4: (ICAI Study Material)

A, B, C and D sharing profits in the ratio of 4:3:2:1 decided to dissolve their partnership on 31st March 2023 when their balance sheet was as under:

Liabilities		₹	Assets	₹
Creditors		15,700	Bank	535
Employees Provident Fund		6,300	Debtors	15,850
Capital Accounts:			Stock	25,200
A	40,000		Prepaid Expenses	800
B	20,000	60,000	Plant & Machinery	20,000
			Patents	8,000
			C's Capital A/c	3,200
			D's Capital A/c	8,415
		82,000		82,000

Following information is given to you :-

1. One of the creditors took some of the patents whose book value was ₹ 5,000 at a valuation of ₹ 3,200. Balance of the creditors were paid at a discount of ₹ 400.
2. There was a joint life policy of ₹ 20,000 (not mentioned in the balance sheet) and this was surrendered for ₹ 4,500.
3. The remaining assets were realised at the following values:- Debtors ₹ 10,800; Stock ₹ 15,600; Plant and Machinery ₹ 12,000; and Patents at 60% of their book-values. Expenses of realisation amounted ₹ 1,500.

D became insolvent and a dividend of 25 paise in a rupee was received in respect of the firms claim against his estate. Prepare necessary ledger accounts.

Question 5: (CA Inter Nov 2019) (15 Marks)

G, S & J were partners sharing profits and losses in the ratio of 4:3:2, no partnership salary or interest on capital being allowed. Their Balance Sheet as on 31.3.2019 is as follows:

Liabilities	Amount	Assets	Amount
Partners' Fixed capital accounts		Fixed assets:	
G	24,000	Goodwill	48,000
S	24,000	Land	9,600
J	12,000	Plant & Machinery	15,360
Partners' current accounts:		Motor Car	840
G	600	Current assets:	
S	10,800	Stock	4,680
J	(480)	Trade debtors 2,400	
Loan from G	9,600	Less: Provision (120)	2,280
Trade creditors	14,880	Cash at bank	240
		Miscellaneous losses:	
		Profit & loss	14,400
	95,400		95,400

On 1st April, 2019, the partnership was dissolved. Motor car was taken over by G at a value of ₹ 600, but no cash was given specifically in respect of this transaction. Sale of other assets realized the following amounts:

Particulars	Amount
Goodwill	Nil
Land	8,400
Plant & Machinery	6,000
Stock	3,600
Trade Debtors	1,920

Trade creditors were paid ₹ 14,040 in full settlement of their debts. The cost of dissolution amounted to ₹ 1,800. The loan from G was repaid; G and S both were fully solvent and able to bring in any cash required but J was forced into bankruptcy and was only able to bring 1/2 of the amount due. You are required to prepare: (Applying Garner Vs. Murray rule.)

(i) Cash & Bank account
(ii) Realization account, and
(iii) Partners' Fixed Capital Accounts (after transferring current accounts balances)

Solution

Cash & Bank Account

Particulars	Amount	Particulars	Amount
To Balance b/d	240	By Realisation A/c-Creditors	14,040
To Realisation A/c-(Assets Realised)	19,920	By Realisation A/c-Expenses	1,800
To Capital Accounts:		By G's Loan A/c	9,600
G 27,200		By G's Capital A/c	16,280
S 20,400		By S's Capital A/c	28,680
J 2,640	50,240		
	70,400		**70,400**

Realisation Account

Particulars	Amount	Particulars	Amount
To Goodwill	48,000	By Trade Creditors	14,880
To Land	9,600	By Provision for Bad Debts	120
To Plant and Machinery	15,360	By Bank:	
To Motor Car	840	Land 8,400	
To Stock	4,680	Plant & Machinery 6,000	
To Sundry Debtors	2,400	Stock 3,600	
To Bank (Creditors)	14,040	Debtors 1,920	19,920
To Bank (Expenses)	1,800	By G (Car)	600
		By Capital Accounts: (Loss)	
		G 27,200	
		S 20,400	
		J 13,600	61,200
	96,720		**96,720**

Partners' Fixed Capital Accounts

Particulars	G	S	J	Particulars	G	S	J
To Current A/c (Transfer)	5,800	-	3,680	By Balance b/d	24,000	24,000	12,000
To Real. A/c (Loss)	27,200	20,400	13,600	By Current A/c (Transfer)	-	6,000	-
To Real. A/c (Car)	600	-	-	By Bank	-	-	2,640
To J's Capital A/c (Def.)	1,320	1,320	-	By Bank (Real. loss)	27,200	20,400	-
To Bank*	16,280	28,680	-	By G&S (Deficiency)	-	-	2,640
	51,200	**50,400**	**17,280**		**51,200**	**50,400**	**17,280**

Note:

1. G, S and J will bring cash to make good their share of the loss on realization.
2. As per Garner Vs. Murray rule, solvent partners- G and S have to bear the loss due to insolvency of a partner J in their fixed capital ratio. 24000 : 24000

*Alternatively, posting may be done for the net amount being received from /paid to G and S respectively. Cap. Ratio

Total due = 5280 Recein 1/2 2640 G 1

Deficiency 2640 S 1

Working Note:

Current account balances of partners have been arrived after adjusting profit and loss account debit balance as follows:

	Current account balance	Profit & Loss 14400 in 4:3:2		
G	600	(6,400)	5,800	Dr.
S	10,800	(4,800)	6,000	Cr.
J	(480)	(3,200)	3,680	Dr.

Question 6: (ICAI Study Material)

M/s X, Y and Z who were in partnership sharing profits and losses in the ratio of 2:2:1 respectively, had the following Balance Sheet as at December 31, 2023:

Liabilities	₹	Assets	₹
Capital: X 29,200		Fixed Assets	40,000
Y 10,800		Stock	25,000
Z 10,000	50,000	Book Debts 25,000	
Z's Loan	5,000	Less: Provision (5,000)	20,000
Loan from Mrs. X	10,000	Cash	1,000
Sundry Trade Creditors	25,000	Advance to Y	4,000
	90,000		90,000

The firm was dissolved on the date mentioned above due to continued losses. After drawing up the balance sheet given above, it was discovered that goods amounting to ₹ 4,000 have been purchased in November, 2023 and had been received but the purchase was not recorded in books.

Fixed assets realised ₹ 20,000; Stock ₹ 21,000 and Book Debt ₹ 20,500. Similarly, the creditors allowed a discount of 2% on the average. The expenses of realisation come to ₹ 1,080. X agreed to take over the loan of Mrs. X. Y is insolvent, and his estate is unable to contribute anything. Give accounts to close the books; work according to the decision in Garner vs. Murray.

Question 7: (ICAI Study Material)

Amal and Bimal are in equal partnership. Their Balance Sheet stood as under on 31st March, 2023 when the firm was dissolved:

Liabilities	₹	Assets	₹
Creditors A/c	4,800	Plant & Machinery	2,500
Amal's Capital A/c	750	Furniture	500
		Debtors	1,000
		Stock	800
		Cash	200
		Bimal's drawings	550
	5,550		5,550

The assets realised as under:

Plant & Machinery	1,250
Furniture	150
Debtors	400
Stock	500

The expenses of realisation amounted to ₹ 175. Amal's private estate is not sufficient even to pay his private debts, whereas Bimal's private estate has a surplus of ₹ 200 only.
Show necessary ledger accounts to close the books of the firm.

* Do not transfer outside Liab. to Realisation A/c.
* They are paid at end to the extent of available cash.

TOPIC: PIECEMEAL DISTRIBUTION

Generally, the assets sold upon dissolution of partnership are realised only in small instalments over a period of time. In such circumstances, the choice is either to distribute whatever is collected or to wait till the whole amount is collected. Usually, the first course is adopted. In order to ensure that the distribution of cash among the partners is in proportion to their interest in the partnership concern either of the two methods described below may be followed for determining the order in which the payment should be made.

PIECEMEAL DISTRIBUTION
(Instalments)

Sequence of Distribution:

1) Provide for Dissolution/Realisation Expenses (Estimated)
   (Actual Amount decided in last instalment)
2) Outsider Liabilities [If >1, distribute in o/s Amount ratio until they are fully paid]
3) Partner's Loan
4) Partner's capital* → Highest Relative capital Method / Maximum loss Method

*

Capital Balances	xx
+ Reserves & surplus	xx
- P&L A/c (Dr.)	(xx)
- Loan to Partner	(xx)
	xx

Question 8: (ICAI Study Material)/ (RTP May 2019) (Similar)

A partnership firm was dissolved on 30th June, 2023. Its Balance Sheet on the date of dissolution was as follows:

Liabilities		₹	Assets	₹
Capital Accounts			Cash	10,800
A	76,000		Sundry Assets	1,89,200
B	48,000			
C	36,000	1,60,000		
Loan A/c – B		10,000		
Sundry Creditors		30,000		
		2,00,000		2,00,000

The assets were realized in instalments and the payments were made on the proportionate capital basis. Creditors were paid ₹ 29,000 in full settlement of their account. Expenses of realization were estimated to be ₹ 5,400 but actual amount spent was ₹ 4,000. This amount was paid on 15th September.

Draw up a statement showing distribution of cash, which was realized as follows:

	₹
On 5th July, 2023	25,200
On 30th August, 2023	60,000
On 15th September, 2023	80,000

The partners shared profits and losses in the ratio of 2 : 2 : 1. Prepare a statement showing distribution of cash amongst the partners by 'Highest Relative Capital' method.

Question 9: (ICAI Study Material)

Following is Balance Sheet of A,B,C on 31st Dec, 2022 when they decided to dissolve partnership

Liabilities	₹	Assets	₹
Creditors	2,000	Sundry Assets	48,500
A's Loan	5,000	Cash	500
Capital Accounts:			
A	15,000		
B	18,000		
C	9,000		
	49,000		49,000

The assets realised the following sums in instalments:

	₹
I	1,000
II	3,000
III	3,900
IV	6,000
V (includes saving in expenses 100)	20,100
	34,000

The expenses of realisation were expected to be ₹ 500 but ultimately amounted to ₹ 400 only. Show how at each stage the cash received should be distributed between partners. They share profits in the ratio of 2:2:1. Show by Maximum Loss Method.

Question 10: (ICAI Study Material)

A, B & C are partners sharing profits & losses in ratio 5:3:2. Their capitals were 9,600, 6,000 and 8,400 respectively. After paying creditors, the liabilities and assets of the firm were:

	₹		₹
Liability for interest on loans from:		Investments	1,000
Spouses of partners	2,000	Furniture	2,000
Partners	1,000	Machinery	1,200
		Stock	4,000

The assets realised in full in the order in which they are listed above. B is insolvent. Prepare statement showing distribution of cash as & when available, applying maximum possible loss procedure.

Balance sheet

Liabilities		Assets	
Capital A/cs		Fixed Assets	Book value
A			
B		Investments	
Partner loan		Current Assets	Dr. Bal
Creditors		Stock	
B/P	✓	Debtors	
		Cash & Bank	×

Solution 1

Realisation A/c

Particulars		Amount	Particulars		Amount
To Plant & Mach.		108000	By Creditors		48000
To Fixtures		24000	By Cash A/c		
To Stock		60000	Plant & Mach.	102000	
To Debtors		48000	Fixtures	18000	
To Cash A/c			Stock	84000	
Creditors (48000 - 5%)	45600		Debtors	44400	248400
Expenses	1500		By Q's Capital A/c		4800
GST Bill	4200	51300			
To Profit trf. to Cap. A/cs (B.F.)		9900			
P	3960				
Q	3960				
R	1980				

Capital Accounts

	P	Q	R		P	Q	R
To Realisation		4800		By Bal b/d	120000	48000	24000
To Cash A/c (B.f.)	147960	71160	37980	By Reserve Fund	24000	24000	12000
				By Realisation	3960	3960	1980

Cash A/c

To Bal b/d	60000	By Realisation A/c	51300
To Realisation A/c	248400	By P's Cap. A/c	147960
		By Q's Cap. A/c	71160
		By R's Cap. A/c	37980
	308400		308400

Sol. 2

Realisation A/c

To Debtors	25000	By Creditors	20000
To Stock	35000	By Bank overdraft	5000
To Furniture	40000	By P's capital A/c	
To Machinery	60000	Stock 15750	15750
		(35000 x 50%) − 10%	
To Bank A/c		By Bank A/c	
Repair bill 2000		Stock 20125	
Creditors 20000		(35000 x 50%) + 15%	
Bank OD 5000	27000	Furniture 30000	
		Machinery 50000	
To Profit (B.f)	2620	Unrec. Inv. 25000	
P 1310		Debtors 22500	
Q 1310		(25000 x 90%)	
		Bad Debts Rec. 1245	148870

Capital A/cs

	P	Q		P	Q
To P's Current A/c	2500		By Bal b/d	100000	50000
To Realisation A/c	15750		By Q's current A/c		17500
To Bank A/c (B.f.)	83060	68810	By Realisation A/c	1310	1310

Current A/cs

	P	Q		P	Q
To Bal b/d	10000		By Bal b/d		10000
To Q's cap. A/c (B.f.)		17500	By Reserves	7500	7500
			By P's cap-A/c (B.f.)	2500	

Bank A/c

To Bal b/d	30,000	By Realisation A/c	27000
To Realisation A/c	148870	By P's cap. A/c	83060
		By Q's cap. A/c	68810
	178870		178870

Solution 4

Realisation A/c

Particulars		Amount	Particulars		Amount
To Debtors		15850	By Creditors		15700
To Stock		25200	By Emp. Provident Fund		6300
To Prepaid Exp.		800	By Bank A/c		
To Plant & Mach.		20000	JLP	4500	
To Patents		8000	Debtors	10800	
To Bank			Stock	15600	
Creditors (15700 - 3200 - 400)	12100		Plant & Mach.	12000	
Expenses	1500		Patents (8000 - 5000) x 60%	1800	44700
Emp. PF	6300	19900	By Loss trf. to cap. A/c (B.F.)		23050
			A 9220, C 4610		
			B 6915, D 2305		

Capital A/cs

	A	B	C	D		A	B	C	D
To Bal b/d	–	–	3200	8415	By Bal b/d	40000	20000	–	–
To Realisation	9220	6915	4610	2305	By Bank				2680
To D's cap.	5360	2680			By A & B's cap.				8040
					By Bank A/c (Real. loss)	9220	6915	4610	–
To Bank A/c (B.f.)	34640	17320			By Bank A/c (B.f.)			3200	

Insolvency of Partner D

Amount due	10720
– Receive 25%	(2680)
Shortfall	8040

Borne by other partners in capital ratio

	A	B	C
Capital	40000	20000	~~(3200)~~
Ratio	2 :	1	

Share in def. 5360 & 2680

A	5360
B	2680
To D	8040

Bank A/c

To Bal b/d	535	By Realisation A/c	19900
To Realisation A/c	44700	By A's cap. A/c	34640
To D's cap. A/c	2680	By B's cap. A/c	17320
To A's cap. A/c	9220		
To B's cap A/c	6915		
To C's cap. A/c	4610		
To C's cap. A/c	3200		
	71860		71860

Solution 6

Realisation A/c

To Fixed Assets	40000	By Prov. for Doubtful debts	5000
To Stock	25000	By Mrs X's Loan	10000
To Book debts	25000	By Creditors (25000 + 4000)	29000
To Cash A/c		By Cash A/c	
Creditors 28420		Fixed Assets 20000	
(29000 − 2%)		Stock 21000	
Expenses 1080	29500	Book debts 20500	61500
To X's Capital A/c (Mrs. X Loan)	10000	By Loss t/d. to Capital A/cs (B.f.) 2:2:1	24000
		X 9600	
		Y 9600	
		Z 4800	

Capital Accounts

	X	Y	Z		X	Y	Z
To Adv. to Y		4000		By Bal b/d	29200	10800	10000
To creditors (4000 in 2:2:1)	1600	1600	800	By Realisation	10000		
To Realisation A/c	9600	9600	4800	By X & Z's cap. A/c		4400	
To Y's cap. A/c	3300		1100	By cash A/c (Real. loss)	9600		4800
To cash A/c (B.f.)	34300		8100				

Cash A/c

To Bal b/d	1000	By Realisation A/c	29500
To Realisation A/c	61500	By Z's Loan A/c	5000
To X's cap. A/c	9600	By X's cap. A/c	34300
To Z's cap. A/c	4800	By Z's cap. A/c	8100
	76900		76900

Insolvency of Partner Y

Deficiency / shortfall = 4400

To be borne by X & Z in capital ratio

	X	Z
Capital A/c	29200	10000
- Reduction (creditors)	(1600)	(800)
	27600	9200
Ratio	3 :	1
Share in Deficiency (4400 in 3:1)	3300 &	1100

Solution 7

Realisation A/c

To Plant & Mach.	2500	By cash A/c		
To Furniture	500	P & M	1250	
To Debtors	1000	Furniture	150	
To Stock	800	Debtors	400	
To cash (Expenses)	175	Stock	500	2300
		By loss trd. to cap. A/c (B.f.)		2675
		Amal	1338	
		Bimal	1337	

Capital A/cs

	Amal	Bimal		Amal	Bimal
To Bal b/d		550	By Bal b/d	750	
To Realisation	1338	1337	By Cash A/c		200
			By Deficiency (B.f.)	588	1687

Cash A/c

To Bal b/d	200	By Realisation A/c	175
To Realisation A/c	2300	By Creditors A/c (B.f.)	2525
To Bimal's cap. A/c	200		

Creditors A/c

To Cash A/c	2525	By Bal b/d	4800
To Deficiency (B.f.)	2275		

Deficiency A/c

To Amal's cap. A/c	588	By Creditors	2275
To Bimal's cap. A/c	1687		

Highest Relative capital Method

Case 1:

	A	B
Capital A/c Balance	300000	220000
Ratio	1	1

Sequence of Distribution

	A		B
First 80000	80000		-
Excess of 80000	1	:	1

Case 2:

	A	B
Capital A/c Balance	300000	220000
Ratio	3	2
Capital / PSR	100000 (3L/3)	110000 (2.20L/2)
Prop. capital taking A as base	300000	200000
Excess	0 (3L − 3L)	20000 (2.20 − 2L)

~~330000 220000~~

~~3 2~~

~~100000 110000~~

~~330000 220000~~

A will only 30000

Sequence

	A	B
First 20000	-	20000
Excess	3 :	2

Solution 8:

Working Note:

Highest Relative capital Method

		A	B	C
1)	Amount	76000	48000	36000
2)	PSR	2	2	1
3)	Capital / PSR (1)/(2)	38000	24000	36000
4)	Proportionate capital taking B as base	48000	48000	24000
5)	Excess capital (1)-(4)	28000	-	12000
6)	PSR	2		1
7)	Capital / PSR	14000		12000
8)	Prop. capital taking C as base	24000		12000
9)	Excess Amt (5)-(8)	4000		-

Summary

	A	B	C
Ist	4000		
IInd (2:1)	24000		12000
IIIrd (2:2:1)	48000	48000	24000
	76000	48000	36000

Statement showing distribution of cash

Particulars		Creditors	B's loan	A	B	C
Amount due / O/s		30000	10000	76000	48000	36000
(1) 1/7 Cash available	10800					
- Expenses	(5400)					
	5400					
- Paid to creditors	(5400)	(5400)				
	x	24600				
(2) 5/7 Amount =	25200					
- Creditors =	(23600)	(23600)				
	1600	1000				
- B's loan	(1600)		(1600)			
	x		8400			

(3) 30/8 Amount =	60000				
- B's loan =	(8400)	(8400) → x			
- Paid to A =	(4000)		(4000)		
- Paid to A/c =	(36000)		(24000)		(12000)
	11600				
- Paid to A, B & C (2:2:1)	(11600)		(4640)	(4640)	(2320)
	x		43360	43360	21680
(4) 15/9 Amount =	80000				
+ Saving in Exp: (5400 - 4000)	1400				
	81400				
- A, B & C (2:2:1)	(81400)		(32560)	(32560)	(16280)
	x				
Balance unpaid (Realisation Loss)			10800	10800	5400

Solution 9.

Statement showing distribution of cash

		Creditors	A's loan	A	B	C
Balance due		2000	5000	15000	18000	9000
I	Opening cash 500					
	+ Amount 1000					
	− Expenses (500)					
	− Creditors (1000)	(1000)				
	x	1000				
II	Amount 3000					
	− Creditors (1000)	(1000)				
	− A's loan (2000)	x	(2000)			
	x		3000			
III	Amount 3900					
	− A's loan (3000)		(3000)			
	− Distribution (900) (WN1)		x		(600)	(300)

				15000	17400	8700
IV Amount =	6000					
− Distribution (WN 2)	(6000)			(960)	(3360)	(1680)
	x			14040	14040	7020
IV Amount	20100					
− Distribution (WN 3)	(20100)			(8040)	(8040)	(4020)
	x					
Amount unpaid				6000	6000	3000

W.N: 1 Distribution of 900

	A	B	C	Total
Amount due	15000	18000	9000	42000
Max. possible loss 41100 (42000-900) shared in PSR 2:2:1	(16440)	(16440)	(8220)	(41100)
	(1440)	1560	780	900
Deficiency / Shortfall of 1440 to be borne by B & C in capital ratio 18000 : 9000 ie 2:1	1440	(960)	(480)	-
	-	600	300	900

WN 2 Distribution of 6000

	A	B	C	Total
Amount due	15000	17400	8700	41100
Max. loss of 35100 shared in PSR 2:2:1	(14040)	(14040)	(7020)	(35100)
	960	3360	1680	6000

WN Distribution of 20100

	A	B	C	Total
Amount due	14040	14040	7020	35100
Max. loss of 15000 shared in PSR 2:2:1	(6000)	(6000)	(3000)	(15000)
	8040	8040	4020	20100

Sol-10

Statement showing distribution of cash

	Int: on Spouse loan	Int. on Partner loan	A	B	C
Amount due	2000	1000	9600	6000	8400
1) Investments					
Amount = 1000					
- Int. on spouse loan (1000)	(1000)				
X	1000				
2) Furniture					
Amount = 2000					
- Int. on spouse loan (1000)	(1000)				
	X				
- Int. on Partner loan (1000)		(1000)			
X		X			

3) Machinery				
Amount =	1200			
- Distribution (WN 1)	(1200)			(1200)
	x			
		9600	6000	7200
4) Stock				
Amount	4000			
- Distribution (WN 2)	(4000)	(200)	(360)	(3440)
	x			
Amount unpaid		9400	5640	3760

WN:1 Distribution of 1200

	A	B	C	Total
Amount	9600	6000	8400	24000
Max. Loss 22800 (24000 - 1200) Shared in 5:3:2	(11400)	(6840)	(4560)	(22800)
	(1800)	(840)	3840	1200
Dy. of A & B borne by C	+1800	+840	(1800) (840)	-
	-	-	1200	1200

WN 2

Distribution of 4000

	A	B	C	Total
Balance	9600	6000	7200	22800
Max. loss 18800 (22800 - 4000) Shared in 5:3:2	(9400)	(5640)	(3760)	(18800)
	200	360	3440	4000

Bank Reconciliation Statement

1. Cheque Issued but not presented for payment

Cash Book (Bank A/c)

To Bal b/d	100000	By Creditors	20000
		By Bal c/d	80000

Pass Book (Customer A/c)

		By Bal b/d	100000
To Bal c/d	100000		

BRS

Starting Point	Cash Book	Pass Book
Balance	80000	100000
	+ 20000	(20000)
	PB 100000	80000 CB

2. Cheque deposited into Bank but not yet cleared

Cash Book
(Bank A/c)

To Bal b/d	100000		
To Customer	30000	By Bal c/d	130000

Pass Book
(Customer A/c)

		By Bal b/d	100000
To Bal c/d	100000		

BRS

Starting Point	Cash Book	Pass Book	
Balance	130000	100000	
	(30000)	+30000	
PB	100000	130000	CB

3. Interest allowed / credited by Bank

4. Interest & Dividend collected by Bank

5. Direct Payment into Bank by customer

6. B/R collected by Bank on customer behalf

Cash Book
(Bank A/c)

To Bal b/d	100000		
		By Bal c/d	100000

Pass Book
(Customer A/c)

		By Bal b/d	100000
To Bal c/d	145000	By Int., D/D, Direct coll.	45000

BRS

	Cash Book	Pass Book	
Starting Point Balance	100000	145000	
	+45000	(45000)	
PB	145000	100000	CB

7. Interest & Expenses charged by Bank
8. Direct Payment by Bank
9. Dishonour of bill discounted with the bank

Cash Book
(Bank A/c)

To Bal b/d 100000	
	By Bal c/d 100000

Pass Book
(Customer A/c)

To Int., Expenses, Direct Payment, B/R Dish. 35000	By Bal b/d 100000
To Bal c/d 65000	

BRS

Starting Point	Cash Book	Pass Book
Balance	100000	65000
	(35000)	+35000
	PB 65000	100000 CB

10 (a) Wrong Dr. in Cash Book / Pass Book

Undercasting of Cr. side of Cash Book

Overcasting of Dr. side of Cash Book

Cash Book

(Bank A/c)

To Bal b/d	100000		5000
(22000+3000)	25000	By Bal c/d	120000

Pass Book

(Customer A/c)

	5000	By Bal b/d	100000
To Bal c/d	117000		22000

BRS

	Cash Book	Pass Book
Starting Point Balance	120000	117000
	(3000)	+3000
	PB 117000	120000 CB

10(b) Wrong Cr. in Cash Book / Pass Book

Undercasting of Dr. side of Cash Book

Overcasting of Cr. side of Cash Book

Cash Book
(Bank A/c)

To Bal b/d	100000	(40000+5000)	45000
	25000	By Bal c/d	80000

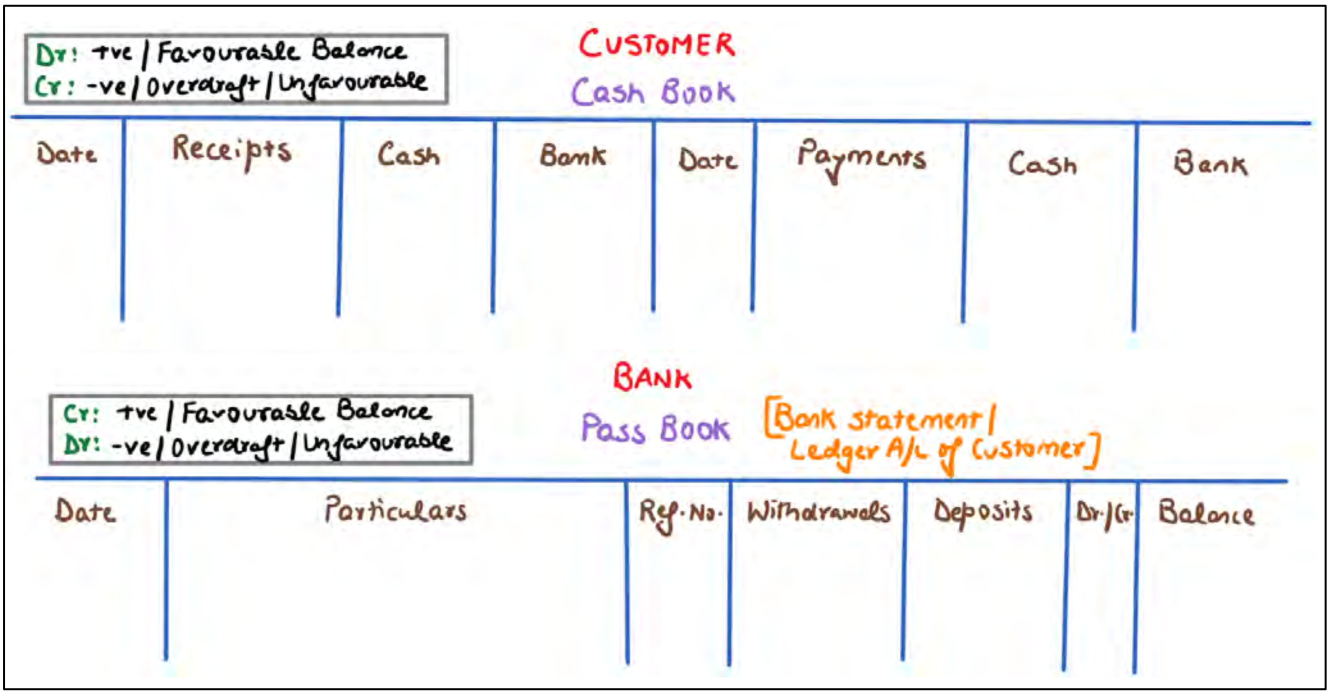
Pass Book
(Customer A/c)

	40000	By Bal b/d	100000
To Bal c/d	85000		25000

BRS

Starting Point	Cash Book	Pass Book
Balance	80000	85000
	+ 5000	(5000)
	PB 85000	80000 CB

BANK RECONCILIATION STATEMENT



BANK PASS BOOK OR STATEMENT

1. Bank Pass Book (also known as Bank Statement) is an extract of the Ledger Account of the customer, as per the Bank's books of Accounts.
2. It is a periodical statement of account in which all transactions, i.e, deposits and withdrawals made by the customer during the particular period is recorded.
3. A comparative analysis of the Cash Book (Bank Column) & Bank Pass Book is given below

Point	In Cash Book of Customer	In Bank Pass Book
Debit Entries in Cash Book	• Deposits of cash into Bank • Receipt of cheques from debtors • Other Incomes/Receipts, e.g. Interest, Dividend, Capital introduced, etc. • B/R Collection, Income on Investment, etc. by the Bank.	These are recorded as "Deposits" in the Pass Book, i.e. on the credit side of the Pass book
Credit Entries in Cash Book	• Withdrawal of cash from Bank • Payment to Creditors/ of Expenses • Bank Interest, Charges by the Bank • Payment as per standing instructions	These are recorded as "Withdrawals" in the Pass book, i.e. on the debit side of the Pass book
Favourable Balance	Such balance will appear on the debit side of cash book (Bank column)	Credit Balance in Pass Book represents favourable balance
Overdraft balance	Such balance will appear on credit side of Cash Book (Bank column)	Debit Balance in Pass Book represents an unfavourable balance

For each entry in the Cash Book, there should be corresponding opposite entry in Pass book.

BANK RECONCILIATION STATEMENT

1. Bank Reconciliation Statement: At periodical intervals, the customer/ business entity (i.e. Account Holder in the Bank), should compare the balance in Bank as shown by the Cash Book with the Pass Book. In case of any differences between the two, they should be analyzed by listing out the various reasons for such difference. Such a statement is called Bank Reconciliation Statement (BRS).
   It is prepared by Customer/Bank Account holder. It is prepared to know the causes for difference between balance as per Bank Column of Cash Book & Pass Book/Bank Statement.

2. Advantages: The advantages of Bank reconciliation statement are-
   (a) To record entries which have been missed out in the Cash Book, e.g. Interest charged/allowed by the bank, bank charges, and direct collection by bank etc.
   (b) To identify any errors that may been committed either in cash book or in bank statement,
   (c) To identify any undue delay in the clearance of cheque and
   (d) To act as a deterrent against embezzlement frauds.

DIFFERENCES BETWEEN BANK STATEMENT AND CASH BOOK

Causes of Difference

Timing
Transaction recorded at 2 different times in cash book & Pass book
* Cheque issued but not presented
* Cheque deposited but not cleared

Transaction
Transactions which bank carries out itself without intimating the customer
* Interest allowed by bank
* Bank charges debited by bank

Error
Mistakes or errors in preparing accounts either in cash book or Pass book

PROCEDURE FOR BANK RECONCILIATION STATEMENT

BRS may be prepared in two ways-
(a) Without adjusting the Cash Book, i.e. Preparation of BRS only.
(b) After adjusting Cash Book for Items 3 to 10 given above, i.e. Preparation of Adjusted Cash Book and BRS.
The Procedures for preparing the BRS is explained below-

METHOD 1: PREPARATION OF BRS ONLY (i.e. WITHOUT ADJUSTING CASH BOOK)

Starting Point	Cash Book Balance		Pass Book Balance	
Balance as per Starting Point	Dr. Balance in Cash Book (Favourable)	Cr. Balance in Cash Book (Overdraft)	Dr. Balance in Pass Book (Overdraft)	Cr. Balance in Pass Book (Favourable)
1. Cheques issued but not yet presented for payment (Item 1)	Add	Subtract	Add	Subtract
2. Cheques deposited into Bank but not yet credited /cleared (Item 2)	Subtract	Add	Subtract	Add
3. Interest allowed by Bank (Item 3)	Add	Subtract	Add	Subtract
4. Interest & Dividends collected by Bank (Item 4)	Add	Subtract	Add	Subtract
5. Direct payments into Bank by a customer (Item 5)	Add	Subtract	Add	Subtract
6. Bill Receivable collected by bank on behalf of the customer (Item 6)	Add	Subtract	Add	Subtract
7. Interest & Expenses charged by Bank (Item 7)	Subtract	Add	Subtract	Add
8. Direct Payments by bank (Item 8)	Subtract	Add	Subtract	Add
9. Dishonour of a bill discounted with the Bank (Item 9)	Subtract	Add	Subtract	Add
10. Wrong Entries (Item 10)				
(a) Wrong Debit in Cash Book or in Pass Book, under-casting of Cr. Side of Cash Book, overcasting of Dr. side of cash book etc.	Subtract	Add	Subtract	Add
(b) Wrong Credit in Cash Book or Pass Book, overcasting of Cr. side of Cash book, undercasting of Dr. side of cash book	Add	Subtract	Add	Subtract
Balances as per End Point	Pass Book Balance		Cash Book Balance	
Positive (+) End Point balance indicates	Favourable i.e Cr. Bal. as per Pass Book	Overdraft i.e. Dr. Bal. as per Pass Book	Overdraft i.e. Cr. Bal. as per Cash Book	Favourable i.e. Dr. Bal. as per Cash Book
Negative (-) End Point balance indicates	Overdraft i.e. Dr. Bal. as per Pass Book	Favourable i.e. Cr. Bal. as per Pass Book	Favourable i.e Dr. Bal. as per Cash Book	Overdraft i.e. Cr. Bal. as per Cash Book

METHOD 2: PREPARATION OF ADJUSTED CASH BOOK AND BRS

When the balance in the cash book is first adjusted for certain adjustments before taking it to the bank reconciliation statement, then it is known as adjusted cash book balance. Adjusting the cash-book before preparing the bank reconciliation statement is completely optional, if reconciliation is done during different months. But if reconciliation is done at the end of the accounting year or financial year, the cash-book must be adjusted so as to reflect the correct bank balance in the balance sheet. Errors occurring in the pass-book are not to be adjusted in the cash book. All the adjustments considered in the adjusted cash-book are not carried again to the Bank Reconciliation Statement.

Step 1: Prepare Adjusted Cash Book with the following Debits and Credits

Receipts	₹	Payments	₹
To balance b/d (in case of Favourable Bal. as per Cash Book)		By balance b/d (in case of Overdraft Bal. as per Cash Book)	
To Interest allowed by Bank	Item 3	By Interest & Expenses charged by bank	Item 7
To Interest & Dividends collected by Bank	Item 4	By Direct payments by bank as per Standing Instructions	Item 8
To Direct Payments into Bank by firm's customers	Item 5	By dishonour of a bill discounted with the bank	Item 9
To Bill Receivable collected by bank on behalf of firm	Item 6		
To Rectification of Error in Cash Book, e.g. double credit posting, credit overcast, debit under cast, debit entry omission etc.	Item 10	By Rectification of Error in cash book, e.g. double debit posting, debit overcast, credit undercast, credit entry omission etc.	Item 10
To balance c/d (in case of Overdraft bal. as per Cash Book)		By balance c/d (in case of Favourable bal. as per Cash Book)	
Total		Total	

Step 2: Prepare Bank Reconciliation Statement as under-

Starting Point	Cash Book Balance		Pass Book Balance	
Balance as per Starting Point	Dr. Balance in Cash Book (Favourable)	Cr. Balance in Cash Book (Overdraft)	Dr. Balance in Pass Book (Overdraft)	Cr. Balance in Pass Book (Favourable)
1. Cheques issued but not yet presented for payment (Item 1)	Add	Subtract	Add	Subtract
2. Cheques deposited into Bank but not yet credited/cleared (Item 2)	Subtract	Add	Subtract	Add
3. Wrong Cr. in Pass Book (Item10)	Add	Subtract	Add	Subtract
4. Wrong Dr. in Pass Book (Item10)	Subtract	Add	Subtract	Add
Balance as per End Point	Pass Book Balance		Cash Book Balance	
Positive (+) End point balance indicates	Favourable i.e. Cr. bal. as per pass book	Overdraft i.e. Dr. Bal, as per Pass Book	Overdraft i.e. Cr. Bal. as per Cash Book	Favourable Dr. Bal. as per Cash Book
Negative (-) End Point balance indicates	Overdraft i.e. Dr. Bal. as per Pass Book	Favourable i.e. Cr. Bal. as per Pass Book	Favourable i.e. Dr. Bal. as per Cash Book	Overdraft i.e. Cr. Bal as per Cash Book

Question 1: (ICAI Study Material)

Prepare a bank reconciliation statement from the following particulars on 30th September, 2023:

Particulars	Amount
Debit balance as per bank column of the cash book	37,20,000
Cheque issued to creditors but not yet presented to the bank for payment	7,20,000
Dividend received by the bank but not yet entered in the cash book	5,00,000
Interest allowed by the bank	12,500
Cheques deposited into bank for collection but not collected by bank up to this date	15,40,000
Bank charges not entered in Cash Book	2,000
A cheque deposited into bank was dishonoured, but no intimation received	3,20,000
Bank paid house tax on our behalf, but no information received from bank in this connection.	3,50,000

Solution

Bank Reconciliation Statement

Particulars	**Amount**
Balance as per Cash book	37,20,000
Add : Cheque issued but not presented	7,20,000
Add : Dividend received by bank not entered in cash book	5,00,000
Add : Interest allowed by bank	12,500
Less : Cheque deposited in bank but not yet credited	(15,40,000)
Less : Bank charges debited by the bank	(2,000)
Less : A cheque deposited into bank was dishonoured	(3,20,000)
Less : House tax paid by bank	(3,50,000)
Balance as per Pass Book	**27,40,500**

Question 2: (CA Foundation July 2021) (5 Marks)

From the following information, ascertain the Cash Book balance of Mr. Bajaj as on 31st March, 2023:

a) Debit balance as per Bank Pass Book ₹ 3,500.
b) A cheque amounting to ₹ 2,500 deposited on 15th March, but the same was returned by the Bank on 24th March for which no entry was passed in the Cash Book.
c) During March, two bills amounting to ₹ 2,500 and ₹ 500 were collected by the Bank but no entry was made in the Cash Book.
d) A bill for ₹ 5,000 due from Mr. Balaji previously discounted for ₹ 4,800 was dishonored. The Bank debited the account, but no entry was passed in the Cash Book
e) A Cheque for ₹ 1,500 was debited twice in the cash book.

Solution

Bank Reconciliation Statement as on 31st March,2023

Particulars	Amount ₹
Balance as per Pass Book (Dr.)	(3,500)
Add: Cheques deposited but returned on 24th March,2023	2,500
Discounted bill from Mr. Balaji dishonoured	5,000
Wrong debit in cashbook	1,500
Less: Bill collected by bank (2,500+500)	(3000)
Balance as per Cash book (Dr. / Favourable)	2,500

Question 3: (RTP May 2019)/(RTP May 2023)(Sim.)

On 30th November, 2023, the Cash Book of Mr. Hari showed an overdrawn position of ₹ 4,480 although his Bank Statement showed only ₹ 3,200 overdrawn. An examination of the two records showed the following errors:

(i) The debit side of the Cash Book was undercast by ₹ 400.

(ii) A cheque for ₹ 1,600 in favour of Y suppliers Ltd. was omitted by the bank from the statement, the cheque was debited to another customer's Account.

(iii) A cheque for ₹ 172 drawn for payment of telephone bill was recorded in the Cash Book as ₹ 127 but was shown correctly in the Bank Statement.

(iv) A cheque for ₹ 425 from Mr. Pal paid into bank was dishonoured and shown as such on the Bank Statement, although no entry relating to the dishonoured cheque was made in the Cash Book.

(v) The Bank had debited a cheque for ₹ 150 to Mr. Hari's Account by mistake, it should have been debited by them to Mr. Kar's Account.

(vi) A dividend of ₹ 100 was collected by the bank but not entered in the Cash Book.

(vii) Cheques totalling ₹ 1,300 drawn on November was not presented for payment.

(viii) Cheque for ₹ 1,200 deposited on 30th November was not credited by the Bank.

(ix) Interest amounting to ₹ 300 was debited by the Bank but yet to be entered in the Cash Book.

You are required to prepare a Bank Reconciliation Statement on 30th November, 2023.

Solution

Bank Reconciliation Statement as on 30th November, 2023

	Particulars	Amount	Amount
	Bank Overdraft as per Bank Statement		(3,200)
Less:	Debit side of the Cash Book was undercast	400	
Less:	Cheque issued but debited by the Bank to another customer's account by mistake	1,600	
Less:	Dividend directly collected by Bank but not entered in the Cash Book	100	
Less:	Cheque issued but yet to be presented for payment	1,300	(3,400)
Add:	Cheque issued for 172 posted in the Cash Book as 127	45	
Add:	Cheque dishonoured but not recorded in the Cash Book	425	
Add:	Wrong debit by the Bank to Hari's A/c	150	
Add:	Cheque deposited but yet to be credited	1,200	
Add:	Interest debited by Bank and yet to be entered in the Cash Book	300	2,120
	Bank overdraft as per the Cash Book (Cr.)		**(4,480)**

Question 4: (CA Foundation May 2019) (10 Marks)

Prepare the Bank Reconciliation Statement of M/s. R.K. Brothers on 30th June 2023 from the particulars given below:

(i) The Bank Pass Book had a debit balance of ₹ 25,000 on 30th June, 2023.

(ii) A cheque worth ₹400 directly deposited into Bank by customer but no entry was made in Cash Book

(iii) Out of cheques issued worth ₹ 34,000, cheques amounting to ₹ 20,000 only were presented for payment till 30th June, 2023.

(iv) A cheque for ₹ 4,000 received and entered in the Cash Book but it was not sent to the Bank.

(v) Cheques worth ₹ 20,000 had been sent to Bank for collection but the collection was reported by the Bank as under.
   (1) Cheques collected before 30th June, 2023, ₹ 14,000
   (2) Cheques collected on 10th July, 2023, ₹ 4,000
   (3) Cheques collected on 12th July, 2023, ₹ 2,000.

(vi) The Bank made a direct payment of ₹ 600 which was not recorded in the Cash Book.

(vii) Interest on Overdraft charged by the bank ₹ 1,600 was not recorded in the Cash Book.

(viii) Bank charges worth ₹ 80 have been entered twice in the cash book whereas Insurance charges for ₹ 70 directly paid by Bank was not at all entered in the Cash Book.

(ix) The credit side of bank column of Cash Book was under cast by ₹ 2,000.

Solution

Bank Reconciliation Statement as on 30th June 2023

	Particulars	Amount	Amount
	Overdraft as per Pass Book (Dr. Balance)		(25,000)
Less:	Cheques issued but not presented ₹ (34,000-20,000)	14,000	
	Cheques deposited into the Bank by Customer but not entered in Cash Book	400	
	Bank charges written twice in Cash Book	80	(14,480)
			(39,480)
	Cheques received, recorded in cash Book but not sent to the Bank	4,000	
	Cheques sent to the Bank but not collected	6,000	
	Direct payment made by the bank not recorded in the Cash book	600	
	Interest on Overdraft charged by Bank	1,600	
Add:	Insurance charges not entered in Cash Book	70	
	Credit side of bank column of Cash Book was undercast	2,000	14,270
	Overdraft as per Cash Book		**(25,210)**

Question 5: (CA Foundation Dec 2022) (10 Marks)

The cash book of Mr. Karan shows ₹ 2,60,400 as the balance of bank as on 31st December, 2023 but you find that it does not agree with the balance as per the bank pass book. On analysis, you found the following discrepancies:

a. On 15th December, 2023 the payment side of the cash book was overcast by ₹ 10,000.
b. A Cheque for ₹ 1,18,000 issued on 6th December, 2023 was not taken in the bank Column.
c. On 20th December, 2023 the debit balance of ₹ 8,460 as on the previous day, was brought forward as credit balance in the cash book.
d. Of the total cheques amounting to ₹ 12,370 drawn in the last week of December 2023, cheques aggregating ₹ 9,360 were encashed in December, 2023.
e. Dividends of ₹ 35,000 collected by the bank and fire insurance premium of ₹ 7,900 paid by the bank were not recorded in the cash book.
f. A Cheque issued to a creditor of ₹ 1,75,000 was recorded twice in the cash book.
g. Bill for collection amounting to ₹ 53,000 credited by the bank on 21st December, 2023 but no advice was received by Mr. Karan till 31st December, 2023.
h. A Customer, who received a cash discount of 3% on his account of ₹ 60,000 paid a cheque on 10th December, 2023. The cashier erroneously entered the gross amount in the bank column of the cash book.

You are required to prepare the bank reconciliation statement as on 31st December, 2023.

Solution

Bank Reconciliation Statement of Mr. Karan as on 31st Dec., 2023

Particulars		Details ₹	Amount ₹
Balance as per the Cash Book			2,60,400
Add: Wrong Casting in Cash book as on 15th December,2023		10,000	
Mistake in bringing forward ₹ 8,460 debit balance as credit balance		16,920	
Cheques issued but not presented:			
Issued	12,370		
Encashed	(9,360)	3,010	
Dividend directly collected by bank but not yet entered in Cash Book		35,000	
Cheque recorded twice in the Cash Book		1,75,000	
Bill for Collection credited in Bank not entered in Cash Book		53,000	2,92,930
Less: Cheques issued but not entered in the Bank column		1,18,000	
Fire Ins. Premium paid by bank directly not recorded in Cash Book		7,900	
Discount allowed wrongly entered in Cash Book		1,800	(1,27,700)
Balance as per the Pass Book			**4,25,630**

Question 6: (MTP October 2021)

Prepare a Bank Reconciliation statement for Satyam Traders as on 31st March,2023 The cash book of Satyam Traders shows a debit balance of ₹ 4,12,200 at bank as on 31st March,2023, but you find that it does not agree with the balance as per Pass Book. After checking you find the following:

1. On 12th March, 2023 the payment side of the Cash Book was under cast by ₹ 12,000/-
2. A cheque of ₹ 85,000 issued on 20th March, 2023 was not taken in the bank column
3. On 22nd March, 2023 the debit balance of ₹ 18,500 as on the previous day, was brought forwards as credit balance.
4. Out of the total cheques amounting to ₹ 42,000 issued in, the last week of March, 2023, cheques aggregating ₹ 28,500 were encashed in March, 2023.
5. Dividends of ₹ 35,000 collected by the Bank and Fire insurance premium of ₹ 20,000 paid by it were not recorded in the cash book.
6. One cheque issued to a Creditor of ₹ 1,29,000 was recorded twice in the Cash book.
7. A debtor Mr. A has deposited the Cheque for ₹ 32,000 into the bank directly in the month of March, 2023 without intimating to Satyam Traders and the same cheque was dishonored by the bank due to insufficient funds in the month of March itself.
8. A cheque from customer for ₹ 5,000 was deposited in bank on 28th March,2023 but was dishonored and advice received from bank on 3rd April, 2023.
9. Bank paid credit card bill of ₹ 2,500 which is not recorded in cash book.
10. Bank wrongly credited cheque of ₹ 25,000 of other customer in our account.
11. Bank credited cheque of ₹ 2,000 in savings account of proprietor of Satyam Traders instead of crediting cheque in current account of Satyam Traders.
12. ₹ 500 discount received wrongly entered in bank column in cash book.
13. Bank debited charges ₹ 200 on 25th March for which no intimation received till 31st March.

Solution

Bank Reconciliation Statement of Satyam Traders as on 31st March, 2023

Particulars	**Amount**	**Amount**
Balance as per Cash Book		4,12,200
Add:		
Mistake in bringing forward 18,500 debit Bal. as credit bal. on 22nd March	37,000	
Cheques issued but not presented Issued = 42,000 less cashed 28,500 = 13,500	13,500	
Dividend directly collected but not entered in cash book	35,000	
Cheques recorded twice in the cash book	1,29,000	
Wrongly credited cheque by bank	25,000	
Discount amount wrongly entered in bank column	500	
TOTAL		**2,40,000**
Less:		
Wrong casting in cash book on12th March, 2023	12,000	
Cheque issued and not entered in the Bank Column	85,000	
Fire Insurance premium paid directly by bank	20,000	
Cheque dishonored not recorded in books	5,000	
Credit card payment not recorded in cash book	2,500	
Cheque wrongly deposited by bank in savings account	2,000	
Bank charges debited not recorded in cash book	200	
TOTAL		**1,26,700**
Balance as per the Passbook		5,25,500
No effects of cheque deposit directly & dishonored in same Month. Alternatively, it can be added as well as deducted from balance as per cash book.		

Question 7: (ICAI Study Material)

On 30th December, 2023 the bank column of A. Philip's cash book showed a debit balance of ₹ 4,610. On examination of the cash book and bank statement you find that:

2) Cheques amounting to ₹ 6,30,000 which were issued to trade payables and entered in the cash book before 30th December, 2023 were not presented for payment until that date.
3) Cheques amounting to ₹ 2,50,000 had been recorded in the cash book as having been paid into the bank on 30th December, 2023, but were entered in the bank statement on 1st January, 2024.
4) A cheque for ₹ 73,000 had been dishonoured prior to 30th December, 2023, but no record of this fact appeared in the cash book.
5) A dividend of ₹ 3,80,000, paid direct to the bank had not been recorded in the cash book.
6) Bank interest and charges amounting to ₹ 4,200 had been charged in the bank statement but not entered in the cash book.
7) No entry had been made in the cash book for a trade subscription of ₹ 10,000 paid vide banker's order in November, 2023.
8) A cheque for ₹ 27,000 drawn by B. Philip had been charged to A. Philip's bank account by mistake in December, 2023.

You are required:

a) to make appropriate adjustments in the cash book bringing down the correct balance, and
b) to prepare a statement reconciling the adjusted balance in the cash book with the balance shown in the bank statement.

Solution

Cash Book (Bank column)

Date	Particulars	Amount	Date	Particulars	Amount
30.12.23	To Balance b/d	4,610	30.12.23	By Trade receivables (Cheque dishonoured)	73,000
	To Dividend Received	3,80,000		By Bank interest & charges	4,200
				By Trade Subscription	10,000
				By Balance c/d	2,97,410
		3,84,610			**3,84,610**

Bank Reconciliation Statement

Particulars	Amount
Balance as per Cash book	2,97,410
Add : Cheque issued but not presented	6,30,000
Less: Cheque paid/deposited into bank but not yet cleared	(2,50,000)
Less: Cheque wrongly charged	(27,000)
Balance as per Pass Book	**6,50,410**

Question 8: (CA Foundation Nov 2019) (10 Marks)

On 30th September, 2023, the bank account of XYZ, according to the bank column of the cash book, was overdrawn to the extent of ₹ 8,062. An examination of the Cash book and Bank Statement reveals the following:

a) A cheque for ₹ 11,14,000 deposited on 29th September, 2023 was credited by the bank only on 3rd October, 2023.
b) A payment by cheque for ₹ 18,000 has been entered twice in the Cash book
c) On 29th September, 2023, the bank credited an amount of 1,15,400 received from a customer of XYZ, but the advice was not received by XYZ until 1st October, 2023.
d) Bank charges amounting to ₹ 280 had not been entered in the cash book.
e) On 6th September 2023, the bank credited ₹ 30,000 to XYZ in error.
f) A bill of exchange for ₹ 1,60,000 was discounted by XYZ with his bank. The bill was dishonoured on 28th September, 2023 but no entry had been made in the books of XYZ.
g) Cheques issued upto 30th September, 2023 but not presented for payment upto that date totalled ₹ 13,46,000.
h) A bill payable of ₹ 2,00,000 had been paid by the bank but was not entered in the cash book and bill receivable for ₹ 60,000 had been discounted with the bank at a cost of ₹ 1,000 which had also not been recorded in cash book.

You are required:

To show the appropriate rectifications required in the cash book of XYZ, to arrive at the correct balance on 30th September, 2023 and to prepare a Bank Reconciliation Statement as on that date.

Solution

Dr. **Cash Book (Revised)** **Cr.**

Particulars	Amount	Particulars	Amount
To Party A/c (Twicely Credited, now rectify)	18,000	By Balance b/d	8,062
To Customers A/c	1,15,400	By Bank charges A/c	280
To Bills receivables A/c	59,000	By Customer (B/R dishonoured)	1,60,000
To Balance c/d (Bal. Fig.)	1,75,942	By Bills payable A/c	2,00,000
	3,68,342		**3,68,342**

Bank Reconciliation Statement As on 30th September, 2023

Particulars	Amount
Credit Balance (Overdraft) as per cash Book	(1,75,942)
Less: A cheque for ₹ 11,14,000 deposited on 29th Sep. 2023 was credited by the bank only on 3rd October, 2023	(11,14,000)
Add: On 6th Sep., 2023 the bank Credited ₹ 30,000 to XYZ in error	30,000
Add: Cheque issued up to 30th Sep., 2023 but not presented for payment up to that date totalled ₹ 13,46,000	13,46,000
Credit Balance (Favourable) as per pass book	**86,058**

Question 9: (ICAI Study Material)

Mr. Manoj is employed by Century Rayon and Carpets Pvt Ltd. as their cashier. The main responsibility of Mr. Manoj is to maintain the company's cash book and prepare a bank reconciliation statement at the end of each month. The cash book (only bank column) is set out below together with a copy of the bank statement for the month of February 2023.

You are required to :

a) Reconcile the cash book with the bank statement.
b) Make necessary entries to update the cash book.
c) Start with the balance as per cash book, list any unpresented cheques and sub-total on the reconciliation statement.

Century Rayon and Carpets Pvt Ltd
Cash Book (Bank Column only)

Date	Particulars	Amount	Date	Particulars	Amount
1/2/23	To Balance b/d	1,42,500	3/2/23	By Bhagwandas	1,980
1/2/23	To Blue & Co.	1,570	5/2/23	By Maruti Ltd. (400460)	1,500
4/2/23	To GM Ltd.	2,430	12/2/23	By Jackson Ltd. (400461)	54,000
8/2/23	To Robinson Ltd.	910	18/2/23	By PC Computers (400462)	1,420
13/2/23	To Donald	750	21/2/23	By Shiv Garage (400463)	49,000
20/2/23	To Avenue Super Mart	4,200	26/2/23	By Petty Cash (400465)	1,500
28/2/23	To Sleep Well Ltd.	940	26/2/23	By Shweta & Co. (400464)	2,100
			26/2/23	By AV Partners (400466)	5,200
			28/2/23	By Balance c/d	36,600
		1,53,300			1,53,300

Customer: Century Rayon and Carpets Pvt Ltd
Account No – xxxxx0439
Account Statement for the month of February 2023

Date	Particulars	Amount (Dr.)	Amount (Cr.)	Dr. or Cr.	Balance
1/2/23	Balance b/d			Cr.	1,42,500
3/3/23	Cheques		1,570	Cr.	1,44,070
6/2/23	Maruti Ltd.	1,500		Cr.	1,42,570
7/4/23	Bhagwandas	1,980		Cr.	1,40,590
12/2/23	GM Ltd.		2,430	Cr.	1,43,020
15/2/23	Robinson Ltd.		910	Cr.	1,43,930
20/2/23	Premium of New India Insurance Ltd.	3,800		Cr.	1,40,130
22/2/23	Donald		750	Cr.	1,40,880
22/2/23	400463	49,000		Cr.	91,880
23/2/23	Cheques		4,200	Cr.	96,080
26/2/23	Savita	1,030		Cr.	95,050
26/2/23	400465	1,500		Cr.	93,550
27/2/23	Shreya		2,200	Cr.	95,750
28/2/23	Bank Charges	2,538		Cr.	93,212

Question 10: (ICAI Study Material)

The following are the Cash Book (bank column) and Pass Book of Jain for the months of March, 2023 and April, 2023:

Cash Book (Bank Column only)

Date	Particulars	Amount	Date	Particulars	Amount
1/3/23	To Balance b/d	60,000	3/3/23	By Cash A/c	2,00,000
6/3/23	To Sales A/c	3,00,000	7/3/23	By Modi	60,000
10/3/23	To Ram	65,000	12/3/23	By Patil	30,000
18/3/23	To Singhal	2,70,000	18/3/23	By Suresh	40,000
25/3/23	To Goyal	33,000	24/3/23	By Ramesh	1,50,000
31/3/23	To Patel	65,000	31/3/23	By Balance c/d	3,13,000
		7,93,000			7,93,000

Pass Book

Date	Particulars	Amount (Dr.)	Amount (Cr.)	Dr. or Cr.	Balance
1/4/23	By Balance b/d		3,65,000	Cr.	3,65,000
3/4/23	By Goyal		33,000	Cr.	3,98,000
5/4/23	By Patel		65,000	Cr.	4,63,000
7/4/23	To Naresh	2,80,000		Cr.	1,83,000
12/4/23	To Ramesh	1,50,000		Cr.	33,000
15/4/23	To Bank Charges	200		Cr.	32,800
20/4/23	By Usha		17,000	Cr.	49,800
25/4/23	By Kalpana		38,000	Cr.	87,800
30/4/23	To Sunil	6,200		Cr.	81,600

Reconcile the balance of cash book on 31/3/2023.

Summary

	Cash Book	Pass Book
Transaction resulting into	1 ↑	3 ↑
	2 ↓	4 ↓

BRS

Starting Point:

CB	xxx	PB	xxx
1)	(−)	1)	+
2)	+	2)	(−)
3)	+	3)	(−)
4)	(−)	4)	+
PB	xxx	CB	xxx

Undercast / Overcast in Cash Book

	Receipts (Debit)		Payments (Credit)
1	Overcast	3	Overcast
2	Undercast	4	Undercast

Starting Point

Bal. as per Cash Book

1	Increase	(-)
2	Decrease	+
3	Decrease	+
4	Increase	(-)

Cash Book

Dr Receipts	Payments Cr

Amount received of 1000

BRS

Starting Point: Cash Book

	Correct	Wrong	
1) 1000 on receipt side not recorded	Dr. 1000	×	+ 1000
2) 1000 ki jagah 100 likh diya	Dr 1000	Dr 100	+ 900
3) 1000 ki jagah 1100 likh diya	Dr 1000	Dr 1100	(100)
4) 1000 ko payment side likh diya	Dr 1000	Cr. 1000	+ 2000
5) 100 ko payment side likh diya	Dr 1000	Cr. 100	+ 1100
6) 1100 ko payment side likh diya	Dr 1000	Cr. 1100	+ 2100

Starting Point

Period Ended 30/9/23

Bal. as per Cash Book xxx

1) Cheque issued but not presented for payment 20000 + 20000

2) Cheque issued in Sept 2023 amounting 100000 but 80000 presented for payment in Sept 2023 + 20000

3) Cheque issued in sept 2023 amounting 100000 out of which 20000 presented for payment in Oct 2023 + 20000

BRS

Preparation of BRS only

(All Differences / transactions shown in BRS only)

Adjusted cash Book & then Preparation of BRS

Adjusted cash Book: Transactions not recorded in cash book, Error in cash Book

Preparation of BRS:
a) Cheque issued but not presented
b) Cheque deposited but not cleared
c) Error by Bank (wrong credit / wrong debit in Pass Book)

Question specifically mention to prepare Adjusted cash Book

OR

Financial Year ending & Bal. as per cash book given

Cash Book (March)

Receipts		Payments
To Bal b/d	xxxx	
1)		a)
2)		b)
3)		c)
4)		d)
5)		e)
6)		f)

Pass Book (March)

Withdrawal	Deposits	
	By Bal b/d	xxxx
a)	1)	
b)	2)	
c)	3)	
e)	4)	
g) Bank charges	7) Interest credited	

Conclusion:

5) & 6) : Cheque deposited but not cleared

7) : Interest credited not recorded in cash book

d) & f) : Cheque issued but not presented

g) : Payment from bank not recorded in cash book (Bank charges)

Solution 9

Entries to be passed in cash book

1) Bank A/c - Dr 2200

To Shreya A/c 2200

2) Insurance Premium A/c - Dr 3800

Sanita A/c - Dr 1030

Bank charges A/c - Dr 2538

To Bank A/c 7368

Adjusted Cash book

To Bal b/d	36600	By Insurance Premium	3800
To Shreya	2200	By Sanita	1030
		By Bank charges	2538
		By Bal c/d (B.f.)	31432

Bank Reconciliation Statement

	Balance as per cash book		31432
Less:	Cheque deposited but not cleared		
	Sleepwell Ltd.	940	(940)
Add:	Cheque Issued but not presented		
	Jackson Ltd.	54000	
	PC Computers	1420	
	Shweta & Co.	2100	
	AV Parmen	5200	62720
	Balance as per Pass Book (Favorable)		93212

Solution 10

Bank Reconciliation Statement

Balance as per cash book			313000
+ Cheque issued but not presented			
	Ramesh	150000	150000
- Cheque deposited but not cleared			
	Goyal	33000	
	Patel	65000	(98000)
Balance as per Pass Book			365000


THANK YOU