Ch-05 : Retirement and Death of a partner.

Accounting for Partnership firms – Retirement and death of a partner-

- Effect of retirement / death of a partner on change in profit sharing ratio, treatment of goodwill, treatment for revaluation of assets and reassessment of liabilities, adjustment of accumulated profits and reserves and preparation of balance sheet.
- Calculation of deceased partner's share of profit till the date of death.
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RETIREMENT AND DEATH OF A PARTNER

A partner has right to retire from the firm after giving due notice inadvance. After retirement anew partnership comes into existence between the remaining partners. Partner can retire from the firm in the following circumstances.

(a) With the consent of all the partners
(b) As per the terms of the partnership agreement
(c) By giving a notice in writing to all other partners, if the partnership is at will.

The retirement of a partner is called reconstitution of the partnership firm because the old agreement is terminated but thefirm continues and the new agreement comes into force.

Following accounting treatment required while retiring a partner.
(a) Calculation of a new ratio and gaining/sacrificing ratio (in some cases)ratio.
(b) Treatment of goodwill.
(c) Adjustment of revaluation of assets and reassessment of liabilities.
(d) Adjustment of undistributed reserves and profits and losses A/c.
(e) Capital adjustments and preparation of new balance sheet.

CALCULATION OF NEW RATIO AND GAINING RATIO:

*****New ratio = Old share + Acquired share
*Gaining ratio=New ratio – Old ratio
Gaining ratio is calculated to ascertain the amount of goodwill payableto retiring or deceased partner by the remaining partners

TREATMENT OF GOODWILL:-

The retiring partner share of goodwill is credited to capital account of respective partner and debited to remaining partners' capital in gaining ratio.

JOURNAL ENTRY:-

Gaining Partner Capital or Current A/c Dr (in Gaining Ratio)
To Retiring or Deceased Partner's Capital A/c (With the Share of Goodwill)

The existing goodwill (if any) will be written off by Debiting All Partners' Capital account in their Old Ratio and Crediting the Goodwill A/c.
Old Partners' Capital A/c or **C**urrent A/c Dr (in Old Ratio)
To Goodwill A/c (Goodwill existing goodwill)
Special Note: **-** Goodwill cannot be shown in books unless and untilit is purchased by paying some

consideration.(AS-26).

Journal entry for the transfer of profit and loss on revaluation at the time of retirement/death of a partner.

For Profits:

Revaluation A/c Dr.
To All Partner's Capital A/c (in Old Ratio)
(Being Profit on Revaluation transferred to All Partners' Capital A/c in Old Profit Sharing Ratio)

For losses:

All the Partners' Capital A/c Dr. (in Old Ratio)
To Revaluation A/c
(Being loss on Revaluation transferred to All Partners' Capital A/c in Old Profit Sharing Ratio**)**

Treatment of undistributed profit at the time of retirement/death of the partner.

The undistributed **profits** are transferred to all partners' capital account in the old profit sharing ratio.

General Reserve A/c Dr.
Profit& Loss A/c Dr.
To All Partners' Capital A/c (in Old Ratio)
(Being undistributed profits transferred to All Partners' Capital A/c in Old Profit Sharing Ratio)

Treatment of undistributed losses at the time of retirement/death of a partner

The **undistributed losses** are transferred to all partners' capitalaccounts in their old profit sharing ratio.

All partners' Capital A/c Dr. (in Old Ratio)
To Profit & Loss A/c
To Advertisement Suspense A/c
To Deferred Revenue A/c
(Being undistributed losses are transferred to All Partners' Capital A/c in Old Profit Sharing Ratio)

Practice Questions:-

Q1. A, B, & C are partners with ratio 4:5:6. Find out new ratio if i) A retires, B retires, C retires.
Sol. Old Ratio between partners A, B & C is 4:5:6. So, New Ratio i) 5:6 ii) 4:6 iii) 4:5

Q2. A, B, & C are partners with ratio 3:2:1.Find out new ratioif A retires and his share is purchased by B alone.
Sol. Old Ratio between partners A, B, & C is 3:2:1. A retires leaving the share of 3/6 and this share is purchased by B. So, B's New Share 2/6 +3/6 =5/6 and C's share is 1/6. So New Ratio is 5:1.

Q3. Roman, Preet and Sanjay are partners with equal profit sharing ratio.Roman decided to retire from the firm and new ratio is fixed as 5:3, determine the gaining ratio.

Sol. Gaining Ratio = New Ratio – Old Ratio
Preet's Gaining Share = 5/8-1/3=15/24-8/24=7/24
Sanjay's Gaining Share =3/8-1/3=9/24-8/24=1/24

Gaining Ratio=7:1

Q4. A, B and C were partners sharing profits in the ratio of 5:3:2. B retires on 1^{st} January, 2016 with A and C agreed to share the profits in futurein the ratio of 6:4. Find the Gaining ratio.

Sol. Gaining Ratio = New Ratio – Old Ratio
A's Gaining Ratio = 6/10-5/10 = 1/10
C's Gaining Ratio=4/10-2/10=2/10
Gaining ratio= 1:2

Q5. A, B and C are partners in a firm sharing profits in the ratioof 5:3:2. A retires and his share is taken up by B and C equally.Goodwill of the firm is ₹ 60,000. Pass necessary journal entry.

Sol:- B's Capital A/c Dr 15,000
C's Capital A/c Dr 15,000
To A's Capital A/c 30,000
(Being adjustment of goodwill done on retirement of A)
Working Note:- Old Ratio is 5:3:2, New Ratio11:9 and Gaining Ratio is1:1.
A's share of goodwill =₹ 60,000 x 5/10=₹ 30,000

Q6. L, M and N were partners sharing profits and losses in the ratio of 5:3:2. On 31st March, 2016 their Balance Sheet was as under:
Prepare Revaluation Account, Partners' Capital A/c and Balance sheet.
N retired on 31stMarch2016 and it was agreed that:
Goodwill of the firm is to be valued at ₹ 2, 00,000.
Machinery be valued at ₹1, 40,000; Patents at ₹40, 000and Property at ₹1, 50,000 on this date.

Liabilities	**Amt. (₹)**	**Assets**	**Amt. (₹)**
Capitals:		Property	1,20,000
L-1,50,000		Patents	30,000
M-1,25,000		Machinery	1,50,000
N-75,000	3,50,00	Stock	1,90,000
General Reserve	30,000	Bank	40,000
Creditors	1,50,000		
	5,30,000		5,30,000

Sol.

Revaluation A/c

Particulars	**Amt. (₹)**	**Particulars**	**Amt. (₹)**
To Machinery	10,000	By Patents	10,000
To Profit transferred to Capital A/c:- L- 15,000 M- 10,000 N- 5,000	30,000	By Property	30,000
	40,000		40,000

Partner's Capital A/c

Particulars	L (₹)	M (₹)	N (₹)	Particulars	L (₹)	M (₹)	N (₹)
To N's Loan A/c	……..	…….	85,000	By balance b/d	1,50,000	1,25,000	75,000
To balance c/d	1,80,000	1,45,000	……	By General Reserve A/c	15,000	10,000	5,000
				By Profit on Revaluation A/c	15,000	10,000	5,000
	1,80,000	1,45,000	85,000		1,80,000	1,45,000	85,000

Opening Balance Sheet of New Firm

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capitals:		Property	1,50,000
L - 1,80,000		Patents	40,000
M - 1,45,000	3,25,000	Machinery	1,40,000
N 's Loan a/c	85,000	Stock	1,90,000
Creditors	1,50,000	Bank	40,000
	5,60,000		**5,60,000**

Q. X, Y and Z are partners in a firm with 3:2:1

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Provision for Doubtful Debts	1,300		
Sundry creditors	15,000	Cash at bank	10,000
Capitals:		Debtors	16,000
X 78,750		Stock	20,300
Y 70,000		Machinery	60,000
Z 61,250	2,10,000	Land and Building	1,20,000
	2,26,300		**2,26,300**

Z retires on the above date and the new profit sharing ratiobetween X and Y will be 5:4.following terms were agreed:

(a) Land and buildings be reduced by10%.
(b) Out of the Insurance premium paid during the year ₹5, 000 be carried forward as unexpired.
(c) There is no need of any provision for doubtful debts.
(d) Goodwill of the firm be valued at ₹ 36, 000 and adjustment in this respect be made without raising a goodwill A/c.

Pass necessary Journal Entries & Prepare the Capital Accounts and the New Balance sheet.

Q.2. A, B, C and D were partners sharing profits in the ratioof 3:3:2:2 respectively. On 1st April, 2014 D retired owing to ill health. It was decided by A, B and C that in future their profit sharing ratio would be

3:2:1.Complete the following Journal in this regard:

Date	Particulars	L. F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c Dr. B's Capital A/c Dr. C's Capital A/c Dr. D's Capital A/c Dr. To………………… (Being the existing goodwill written off)		………. ………. ………. 10,000	 ……….
	A's Capital A/c Dr. B's Capital A/c Dr. To C's capital A/c To D's capital A/c (Being the adjustment for the Goodwill made on account of Change in Profit Sharing Ratio)		1,20,000 ……….	 ………. ……….