Chapter 4: Reconstitution of Partnership (Retirement of Partnership)

Question: 1

Answer in one sentence only.
Who is a retiring partner?

Solution

A partner retiring from a firm, i.e. ceasing to be a partner of the firm due to agreement between them or at his own will or due to any other reason, is called a retiring partner.

Question: 2

Answer in one sentence only.
What is gaining ratio?

Solution

Gaining ratio is the ratio in which the continuing partners acquire the retiring partner's share. It is calculated on retirement or death of a partner for adjusting the retiring partner's share of goodwill. The formula for calculation of gaining ratio is as follows:

Gaining Ratio = New Ratio − Old Ratio

Question: 3

Answer in one sentence only.
How would you treat General Reserve on retirement of a partner?

Solution

The amount of general reserve is transferred to the capital accounts of all the partners in their profit sharing ratio. This is done to give the retiring partner his amount of share in the accumulated profits of the firm. Hence, All Partners' Capital Accounts are credited with their respective shares.

Question: 4

Answer in one sentence only.
How is amount due to a retiring partner settled?

Solution

The amount due to a retiring partner is assumed to be paid through loan if nothing is mentioned in the question regarding the mode of payment. The capital account of the retiring or the deceased partner is closed by transferring the balancing figure to the credit side of the Retiring/Deceased Partner's Loan A/c. The Retiring/Deceased Partner's Loan A/c will be shown on the Liabilities side of the New Balance Sheet (post retirement/death).

Question: 5

Answer in one sentence only.
How would you adjust retiring partner's share of goodwill without opening goodwill account?

Solution

The retiring partner is paid his share of goodwill by debiting the Remaining Partners' Capital Accounts in their gaining ratio and crediting the Retiring Partner's Capital Account with the amount of premium.

Question: 6

Answer in one sentence only.
When is the gaining ratio to be calculated?

Solution

Gaining ratio needs to be calculated at the time of retirement or death of a partner for adjusting the retiring (or deceased) partner's share of goodwill.

Question: 7

Write the term / word / phrase which can substitute the following statement :
The account which shows revaluation of assets and liabilities.

Solution

Revaluation or Profit and Loss Adjustment Account

Explanation: The account which shows revaluation of assets and liabilities is called Revaluation or Profit and Loss Adjustment Account. This account records the revised values of assets and liabilities, so that the retiring partner can be paid his share of profits that the firm has earned till the date of his retirement.

Question: 8

Write the term / word / phrase which can substitute the following statement :
Debit balance of revaluation account.

Solution

Loss on revaluation

Explanation: Debit balance of Revaluation Account represents "Loss on revaluation." Such loss is transferred to All Partners' Capital Accounts in their old profit-sharing ratio (including the retiring partner).

Question: 9

Write the term / word / phrase which can substitute the following statement :
The proportion in which the continuing partners benefit due to retirement of partner.

Solution

Gaining Ratio

Explanation: The proportion in which the continuing partners benefit due to retirement of a partner is called gaining ratio. It is calculated on the retirement or death of a partner for adjusting the retiring/deceased partner's share of goodwill.

Question: 10

Write the term / word / phrase which can substitute the following statement :
Excess of actual capital over proportionate capital.

Solution

Surplus Capital

Explanation: Excess of actual capital over proportionate capital is regarded as surplus capital. This implies that the actual capital of the partners is more than what the capital should be on a proportionate basis. It is to be transferred to the current account or it may be withdrawn by the partners as per the terms of the agreement.

Question: 11

Write the term / word / phrase which can substitute the following statement :
The method under which amount payable to the retiring partner is paid off at a time.

Solution

Lump-sum method

Explanation: The method under which the amount payable to a retiring partner is paid off at a time is termed as Lump-sum method. Under this method, nothing is to be transferred to his loan account, as the payment is made in one single instalment and accordingly, no interest is to be paid to him.

Question: 12

Write the term / word / phrase which can substitute the following statement :
Capital account of a retiring partner always shows balance.

Solution

Credit balance

Explanation: The capital account of a retiring partner always shows credit balance. This is because the amount due to him in the form of share in profits of revaluation account, share of goodwill, accumulated profits and reserves, etc. is always more than the amount which decreases his claim such as drawings, share in accumulated losses, etc.

Question: 12

Select the most appropriate answer from the alternatives given below :

The profit or loss from revaluation on retirement of partner is shared by ___________.

Options

- all the partners
- the remaining partners
- only retiring partner

- none of these

Solution

The profit or loss from revaluation on retirement of a partner is shared by **<u>all the partners.</u>**

Explanation: Revaluation profit arising on retirement of a partner is shared by all the partners in their old profit sharing ratio (including the retiring partner).

Question: 13

Select the most appropriate answer from the alternatives given below :

X, Y, and Z are partners sharing profits in the ratio of 5:3:2. If Y retires then new ratio will be ___________.

Options

- 5:2
- 5:3
- 3:2
- 1:1

Solution

X, Y, and Z are partners sharing profits in the ratio of 5:3:2. If Y retires, then the new ratio will be **<u>5:2</u>**.

Explanation: The new profit sharing ratio between X and Z can be calculated by simply striking out the share of the retiring partner, i.e. Y. In the given question, Y retires. So, his share will be taken out and the remaining partners will share future profits or losses in the ratio of **5:2**.

Question: 14

Himanshu, Gagan and Naman are partners sharing profits and losses in the ratio of 3:2:1. On March 31, 2017, Naman retires.
The various assets and liabilities of the firm on the date were as follows:
Cash Rs 10,000, Building Rs 1,00,000, Plant and Machinery Rs 40,000, Stock Rs 20,000, Debtors Rs 20,000 and Investments Rs 30,000.

The following was agreed upon between the partners on Naman's retirement:
(i) Building to be appreciated by 20%.
(ii) Plant and Machinery to be depreciated by 10%.
(iii) A provision of 5% on debtors to be created for bad and doubtful debts.
(iv) Stock was to be valued at Rs 18,000 and Investment at Rs 35,000.

Record the necessary journal entries to the above effect and prepare the Revaluation Account.

Solution

Books of Himanshu and Gagan
Journal Entries

Date	Particulars	L.F.	Amt (Rs.)	Amt (Rs.)
	Building A/c Dr. Investment A/c Dr. To Revaluation A/c (Value of Building and Investment increased at the time of Naman's retirement)		20,000 5,000	25,000
	Revaluation A/c Dr. To Plant and Machinery A/c To Provision for Bad and Doubt Debts A/c To Stock A/c (Assets revalued and Provision for Bad and Doubtful Debts made at the time of Naman's retirement)		7,000	4,000 1,000 2,000
	Revaluation A/c Dr To Himanshu's Capital A/c To Gagan's Capital A/c To Naman's Capital A/c (Profit on revaluation transferred to all Partners' Capital Accounts in their old profit sharing ratio)		18,000	9,000 6,000 3,000

Revaluation Account

Dr. **Cr.**

Particular	Amt (Rs.)	Amt (Rs.)	Particular	Amt (Rs.)
Plant and Machinery		4,000	Building	20,000
Stock		2,000	Investment	5,000
Provision for Bad and Doubtful debts		1,000		
Profit transferred to Capital Account:				
Himanshu	9,000	18,000		
Gagan	6,000			
Naman	3,000			
		25,000		**25,000**

Question: 15

Select the most appropriate answer from the alternatives given below :

When goodwill is raised at its full value and it is written off ___________ account is to be credited.

Options

- Cash
- goodwill
- all Partners capital account
- loan

Solution

When goodwill is raised at its full value and it is written off, **goodwill** account is to be credited.

Explanation: When goodwill is raised in the books of the firm at its full value and it is written off, then Goodwill Account is to be credited and all partners' Capital Accounts are to be debited in their old profit sharing ratio.

Question: 16

Select the most appropriate answer from the alternatives given below :

Increase in the value of assets should be ____________ to profit and loss adjustment account.

Options

- debited
- credited
- added
- none of there

Solution

Increase in the value of assets should be **credited** to profit and loss adjustment account.

Explanation: Increase in the value of assets represents appreciation and is a gain for the firm. Therefore, the increased value (of asset) is shown on credit side of the Revaluation Account.

Question: 17

Select the most appropriate answer from the alternatives given below :

If the goodwill is raised to the extent of retiring partners share ____________ account is to be debited.

Options

- cash
- goodwill
- all partner's capital
- retiring partners capital

Solution

If the goodwill is raised to the extent of retiring partner's share, **goodwill** account is to be debited.

Explanation: If the goodwill is raised to the extent of the retiring partner's share, Goodwill Account is to be debited. It means that the continuing partners have not compensated their share in favour of the retiring partner; so, there is no need to calculate gaining ratio. Still, the retiring partner's share of goodwill is to be paid, due to which the goodwill account is to be debited.

Question: 18

State whether the following statements is true or false :

Gaining ratio means old ratio minus new ratio.

Options

- True
- False

Solution

False

Explanation: Gaining ratio is the ratio in which continuing partners acquire the retiring partner's share. In other words,

Gaining Ratio = New Ratio − Old Ratio

Hence, the given statement is incorrect.

Question: 19

State whether the following statements is true or false :

Retiring partner's share in profit up to the date of his retirement will be debited to profit and loss suspense account.

Options

- True
- False

Solution

True

Explanation: The retiring partner is entitled to his share of profits or losses that have arisen till the date of his retirement. Such shares are dispensed to the retiring partner by debiting the Profit & Loss Suspense Account and crediting the Retiring Partner's Capital Account. Profit and Loss Suspense Account is opened if any partner retires during the middle of the year as against the usual case of retirement at the year end.

Question: 20

State whether the following statements is true or false :

Amount due to a retiring partner if not paid, appears as his loan in the books of the firm.

Options

- True
- False

Solution

True

Explanation: Amount due to a retiring partner, if not paid, appears as his loan in the books of the firm, as it represents a liability that needs to be paid. Also, interest @ 6% p.a. is allowed till the date such amount remains outstanding.

Question: 21

State whether the following statements is true or false :

Revaluation account is also called Realisation account.

Options

- True
- False

Solution

False

Explanation: Revaluation Account is different from Realisation Account. Revaluation Account is prepared at the time of admission, retirement or death of a partner, which records the effect of changes in the value of assets and liabilities, whereas, Realisation Account is prepared at the time of dissolution of a firm to record the realisation of assets and settlement of liabilities.

Question: 22

State whether the following statements is true or false :

Retirement of a partner leads to dissolution of the firm unless otherwise agreed upon.

Options

- True
- False

Solution

True

Explanation: The above statement is true, especially where there are only two partners in a firm and one of them retires. In order to continue the partnership, the firm needs to admit a new partner. Otherwise, the firm will be dissolved.

Question: 23

State whether the following statements is true or false :

Profit on revaluation account is transferred to continuing partners' capital account only.

Options

- True
- False

Solution

False

Explanation: Revaluation Profit is credited to All Partners' Capital Accounts (including the retiring partners) in their old profit sharing ratio.

Question: 24

Sanil, Nitish, Sapna were partners in a firm sharing profits and losses in the proportion of 1/2, 1/3 and 1/6 respectively. Their Balance Sheet as on 31st March, 2012 was as follows:

Balance Sheet as on 31-03-2012

Liabilities	Amount (Rs)	Assets	Amount (Rs)
Bills Payable	30000	Machinery	40000
Capitals:		Furniture	5000
Sanil	80000	Sundry Assets	60000
Nitish	50000	Stock	30000
Sapna	30000	Debtors	32000
		Bank	23000
	190000		**190000**

Sapna decided to retire on 1st April 2012 on following terms:-

1) Goodwill of the firm will be valued at Rs 30,000/-

2) Furniture was taken over by Sanil for Rs 4,700/-

3) Make a provision for unpaid expenses Rs 1,700/-

4) Out of the amount due to Sapna Rs 7,500/- to be paid by cheque and the remaining amount to be transferred to her loan account.

Solution

Profit and Loss Adjustment Account
Dr. Cr.

Particulars	Amount (Rs)	Particulars		Amount (Rs)
Furniture	300	Loss transferred to :		
Provision for Unpaid Expenses	1700	Sanil's Capital	1000	
		Nitish's Capital	667	2000
		Sapna's Capital	333	

	2000			**2000**

Partners' Capital Accounts

Dr. Cr.

Particulars	**Sanil**	**Nitish**	**Sapna**	**Particulars**	**Sanil**	**Nitish**	**Sapna**
Profit and Loss Adjustment A/c (Loss)	1000	667	333	Balance b/d	80000	50000	30000
Furniture A/c	4700			Goodwill	15000	10000	5000
Bank A/c			7500				
Loan A/c			27167				
Balance c/d	89,300	59,333					
	95000	**60000**	**35000**		**95000**	**60000**	**35000**

Balance Sheet
as on April 01, 2012 after Sapna's retirement

Liabilities		**Amount (Rs)**	**Assets**	**Amount (Rs)**
Bills Payable		30,000	Machinery	40,000
Capital A/cs :			Sundry Assets	60,000
Sanil	89,300	1,48,633	Stock	30,000
Nitish	59,333		Debtors	32,000
Provision for Unpaid Expenses		1,700	Bank (23,000 - 7,500)	15500
Loan A/c of Sapna		27,167	Goodwill	30,000
		2,07,500		**2,07,500**

Note : As per the book the Total of Balance Sheet is Rs 2,12,200 but as per our solution it should be Rs 2,07,500.

Question: 25

Pai, Amba and Manoj are partners in a firm sharing profit and losses in the proportion to their capitals. Their Balance Sheet as on 31.3.2012 is as follow:

Balance Sheet as on 31st March, 2012

Liabilities	**Amount (Rs)**	**Assets**	**Amount (Rs)**
Capitals		Cash	3,000
Pai	30,000	Stock	12,000
Amba	30,000	Debtors	20,000
Manoj	15,000	Plant	13,000
Creditors	7,000	Building	20,000
Outstanding expenses	15,000	Motor Van	31,000
Profit and Loss A/c	20,000	Goodwill	18,000
	1,17,000		**1,17,000**

On the above date Pai retired and the following adjustments have been agreed upon

1) Goodwill was revalued at Rs 15,000

2) Assets and Liabilities were revalued as under debtors Rs 17,000 stock at 90% of book value Building Rs 35,000 Plant Rs 11,500 Motor Van Rs 29, 500, Outstanding expenses Rs 18,000

3) Amba and Manoj contributed additional capital of Rs 20,000 and Rs 10,000 respectively

4) Balance due to Mr. Pai is transferred to his loan account after paying him Rs 1,000/-

Prepare:- Profit and Loss adjustment A/c,. Partner's Capital A/c's and Balance Sheet of new firm

Solution

Profit and Loss Adjustment Account

Dr. Cr.

Particulars		Amount (Rs)	Particulars	Amount (Rs)
Reserve for Discount on Debtors		3,000	Building	15,000
Stock		1,200		
Plant		1,500		
Motor Van		1,500		
Outstanding Expenses		3,000		
Goodwill		3,000		
Profit transferred to:				
Pai's Capital	720			
Amba's Capital	720	1,800		
Manoj's Capital	360			
		15,000		**15,000**

Partners' Capital Accounts

Dr. Cr.

Particulars	Pai	Amba	Manoj	Particulars	Pai	Amba	Manoj
Cash A/c	1,000			Balance b/d	30,000	30,000	15,000
Loan A/c	37,720			Profit and Loss Adjustment A/c (Profit)	720	720	360
Balance c/d		58,720	29,360	Profit and Loss A/c	8,000	8,000	8,000
				Cash A/c		20,000	10,000
	38,720	**58,720**	**29,360**		**38,720**	**58,720**	**29,360**

Balance Sheet
as on April 01, 2012 after Pai's retirement

Liabilities	Amount (Rs)	Assets	Amount (Rs)

Creditors		7,000	Stock	12,000	10,800
Outstanding Expenses		18,000	Less : Depreciation	1,200	
Capital A/cs:			Building		35,000
Amba	58,720	88,080	Debtors	20,000	17,000
Manoj	29,360		Less : Reserve for Doubtful Debts	3,000	
Loan A/c of Pai		37,720	Motor Van	31,000	29,500
			Less : Depreciation	1,500	
			Goodwill		15,000
			Plant	13,000	11,500
			Less : Depreciation	1,500	
			Cash		32,000
		1,50,800			**1,50,800**

Working Notes:

WN 1: Distribution of Profit and Loss A/c

Pai will get = 20,000×2/5=Rs 8,000

Amba will get = 20,000×2/5=Rs 8,000

Manoj will get = 20,000×1/5=Rs 4,000

Cash Account

Dr. Cr.

Particulars	**Amount (Rs)**	**Particulars**	**Amount (Rs)**
Balance b/d	3,000	Pai's Capital A/c	1,000
Capital A/cs:		Balance c/d	32,000
Amba	20,000		
Manoj	10,000		
	33,000		**33,000**

Question: 26

Shailesh, Anil and Das were partners sharing profits and losses in the ratio at 3:3:2. Their Balance Sheet as on 31.3.2012 is as below:

Balance Sheet as on 31st March, 2012

Liabilities	**Amount (Rs)**	**Assets**	**Amount (Rs)**
Capitals		Building	10,000
Shailesh	11,000	Machinery	10,700
Anil	15,000	Furniture	10,000
Das	8,000	Debtors	5,000
Bills Payable	1,900	Stock	6,600

Creditors	9,000	Cash	6,600
Reserve fund	4,000		
	48,900		**48,900**

In 1st April, 2012 Mr. Das retired from the firm on following terms:

1) Shailesh and Anil's share in reserve fund should be continued in new firm.

2) Goodwill of the firm is to be valued at Rs 4,000 however only Das's share in it is to be raised in the books and written off immediately

3) Assets to be revalued as under stock Rs 6,300 machinery Rs 10,000 furniture Rs 10,200

4) R.D.D. to be maintained at 10% on debtors

5) Rs 100 to be written off from creditors

6) The amount payable to Mr. Das is to be transferred to his loan account

Prepare:- Profit and Loss adjustment A/c, Partners capital A/c and Balance Sheet of New firm on 1/04/2012

Solution

Profit and Loss Adjustment Account

Dr. **Cr.**

Particulars	**Amount (Rs)**	**Particulars**		**Amount (Rs)**
Stock	300	Furniture		200
Machinery	700	Creditors		100
Reserve for Doubtful Debts	500	Loss transferred to:		
		Shailesh's Capital	450	
		Anil's Capital	450	1,200
		Das's Capital	300	
	1,500			**1,500**

Partners' Capital Accounts

Particulars	**Shailesh**	**Anil**	**Das**	**Particulars**	**Shailesh**	**Anil**	**Das**
Profit and Loss Adjustment A/c (Loss)	450	450	300	Balance b/d	11,000	15,000	8,000
Loan A/c			9,700	Reserve Fund			1.000
Goodwill (Written off)	500	500		Goodwill			1,000
Balance c/d	10,050	14,050					
	11,000	**15,000**	**10,000**		**11,000**	**15,000**	**10,000**

Balance Sheet

as on April 01, 2012 after Mr. Das’s retirement

Liabilities		**Amount (Rs)**	**Assets**		**Amount (Rs)**
Creditors		8,900	Cash		6,600
Reserve Fund		3,000	Machinery	10,700	10,000
Capital			Less : Depreciation	700	
Shailesh	10,050	24,100	Stock	6,600	6,300
Anil	14,050		Less : Depreciation	300	
Bills Payable		1,900	Debtors	5,000	4,500
Loan A/c of Mr. Das		9,700	Less : Reserve for Doubtful Debts	500	
			Furniture		10,200
			Building		10,000
		47,600			**47,600**

Working Notes:
WN 1: Calculation of Gaining Ratio

New profit sharing ratio of shailesh and Anil = 3 : 3 = 1 : 1

Gaining Ratio = New Ratio - old Ratio

Shailesh's Gain = $\frac{1}{2} - \frac{3}{8} = \frac{1}{8}$

Anil's Gain = $\frac{1}{2} - \frac{3}{8} = \frac{1}{8}$

Gaining Ratio = 1 : 1

WN 2: Calculation Share of Goodwill

Share of goodwill of Mr. Das = $4000 \times \frac{2}{8} = \text{Rs}1000$

WN 3: Goodwill written off

Shailesh's Gain = $\text{Rs}1000 \times \frac{1}{2} = \text{Rs}500$

Anil's Gain = $\text{Rs}1000 \times \frac{1}{2} = \text{Rs}500$

Question: 27

Shedge, Mayekar and Raut were partners sharing profits and losses in the ratio of 4: 3: 3. Their Balance Sheet on 31st March 2012 was as given below:-

Balance Sheet as on 31st March, 2012

Liabilities	**Amount (Rs)**	**Assets**	**Amount (Rs)**
Capitals		Furniture	4,200
Shedge	15,000	Stock	13,000
Mayekar	10,000	Debtors	10,000
Raut	10,000	Bill Receivable	18,000
		Cash/Bank	2,000
		Profit and Loss A/c (Loss)	5,800
	53,000		**53,000**

Raut retired from the business on above date and it was agreed that the amount due to Raut to be paid immediately by availing overdraft facility

1) His share of goodwill was raised at Rs 3,500

2) Revalue furniture Rs 4,000 and stock Rs 16,000

3) Create R.D.D. at 5% on Debtors.

4) Make provision for outstanding printing bill Rs 6,000. Prepare profit and loss adjustment A/c, Capital A/c and Balance Sheet of continuing partners assuming that goodwill is written off by the continuing partners.

Solution

Profit and Loss Adjustment Account

Dr. Cr.

Particulars	**Amount (Rs)**	**Particulars**		**Amount (Rs)**
Furniture	200	Stock		3,000
Reserve for Doubtful Debts	500	Loss to be transferred to:		
Provision for Outstanding Printing Bill	6,000	Shedge's Capital	1,480	
		Mayekar's Capital	1,110	3,700
		Raut's Capital	1,110	
	6,700			**6,700**

Partners' Capital Accounts

Dr. Cr.

Particulars	Shedge	Mayeker	Raut	Particulars	Shedge	Mayeker	Raut
Profit and Loss Adjustment A/c (Loss)	1,480	1,110	1,110	Balance b/d	15,000	10,000	10,000
Profit and Loss A/c (Loss)	2,320	1,740	1,740	Goodwill			3,500
Goodwill (written off)	2,000	1,500					
Bank A/c			10,650				
Balance c/d	9,200	5,650					
	15,000	**10,000**	**13,500**		**15,000**	**10,000**	**13,500**

Balance Sheet
as on April 01, 2012 after Raut's retirement

Liabilities		Amount (Rs)	Assets		Amount (Rs)
Creditors		8,000	Furniture	4,200	
Bank Overdraft		18,650	Less : Depreciation	200	4,000
Capital A/cs:			Stock		16,000
Shedge	9,200		Debtors	10,000	
Mayeker	5,650	14,850	Less : Provision for doubtful debts	500	9,500
Provision for Outstanding Printing Bill		6,000	Bills Receivable		18,000
		47,500			**47,500**

Working Notes:

Old profit Sharing Ratio of Shedge , Mayeker and Raut = 4 : 3 : 3

New Profit Sharing Ratio of Shedge and Mayeker = 4 : 3

Gaining Ratio = New Ratio - Old Ratio

$$\text{Shedge's Gain} = \frac{4}{7} - \frac{4}{10} = \frac{12}{70}$$

$$\text{Mayeker's Gain} = \frac{3}{7} - \frac{3}{10} = \frac{9}{70}$$

Gaining Ratio = 12 : 9

WN 1: Distribution of Profit and Loss A/c (Loss)

$$\text{Shedge's Capital A/c} = 5800 \times \frac{4}{10} = \text{Rs}2320$$

$$\text{Mayekar's Capital A/c} = 5800 \times \frac{3}{10} = \text{Rs}1,740$$

$$\text{Raut's Capital A/c} = 5800 \times \frac{3}{10} = \text{Rs}1,740$$

WN 2: Goodwill written off

$$\text{Shedge's Gain} = 3500 \times \frac{12}{21} = \text{Rs}2000$$

$$\text{Mayekar's Gain} = 3500 \times \frac{9}{21} = \text{Rs}1500$$

Question: 28

Sathe, Deshpande and Madlani were partners sharing profits and losses in the ratio of 5:2:3. Their Balance Sheet was as follows:

Balance Sheet as on 31st March, 2012

Liabilities	**Amount (Rs)**	**Assets**		**Amount (Rs)**
Capitals		Plant and Machinery		50,000
Sathe	70,000	Building		1,00,000
Deshpande	80,000	Motor Van		20,000
Madlani	50,000	Stock		30,000
Creditors	25,000	Debtors	36,000	
Bills Payable	12,000	Less : R.D.D	2,000	34,000
Reserve Fund	25,000	Cash		28,000
	2,62,000			**2,62,000**

Deshpande retired on that date on the following terms:

1) Plant to be depreciated by 10% and Motor Van by 20%.

2) Stock to be appreciated by 10% and building by 20%.

3) R.D.D. is no longer necessary

4) Provision is to be made for Rs 8,000 being compensation to worker

5) The goodwill of the firm to be valued at Rs 40,000 and Deshpande's share in it should be raised.

6) Both the remaining partners decided to write off the goodwill

7) Amount payable to Shri. Deshpande to be kept as his Loan

Prepare:

1) Profit and Loss Adjustment Account

2) Partner’s Capital Accounts

3) New Balance Sheet

Solution

Profit and Loss Adjustment Account

Dr Cr.

Particulars		**Amount (Rs)**	**Particulars**	**Amount (Rs)**
Plant and Machinery		5,000	Stock	3,000
Motor Van		4,000	Building	20,000
Provision for Compensation to workers		8,000	Reserve for Doubtful Debts	2,000
Profit transferred to:				
Sathe’s Capital	4,000			
Deshpande’s Capital	1,600	8,000		
Madlani’s Capital	2,400			
		25,000		**25,000**

Partners’ Capital Accounts

Dr. Cr.

Particulars	**Sathe**	**Deshpande**	**Madlani**	**Particulars**	**Sathe**	**Deshpande**	**Madlani**
Goodwill (written off)	5,000		3,000	Balance b/d	70,000	80,000	50,000
Loan A/c	81,500	94,600	56,900	Reserve Fund	12,500	5,000	7,500
				Profit and Loss Adjustment A/c (Profit)	4,000	1,600	2,400
				Goodwill		8,000	
	86,500	**94,600**	**59,900**		**86,500**	**94,600**	**59,900**

Balance Sheet

as on April 01, 2012 after Deshpande’s retirement

Liabilities	**Amount (Rs)**	**Assets**		**Amount (Rs)**
Creditors	25,000	Plant	50,000	
Bills Payable	12,000	Less : Depreciation	5,000	45,000

Provision for worker's compensation		8,000	Motor Van	20,000	16,000
Loan A/c of Deshpande		94,600	Less : Depreciation	4,000	
Capital A/c's			Debtors		~~36,000~~
Sathe	81,500	1,38,400	Building		1,20,000
Madlani	56,900		Stock		33,000
			Cash		28,000
		2,78,000			**2,78,000**

Working Notes:

Old Profit Sharing Raio = Sathe : Deshpande : Madlani
= 5 : 2 : 3

New Profit Sharing Ratio of Sathe and Madlani = 5 : 3

Gaining Ratio = New Ratio - Old Ratio

Sathe's Gain = $\frac{5}{8} - \frac{5}{10} = \frac{5}{40}$

Madlani's Gain = $\frac{3}{8} - \frac{3}{10} = \frac{3}{40}$

Gaining Ratio = 5 : 3

WN 1: Distribution of Reserve Fund:

Sathe will get = $25000 \times \frac{5}{10} = \text{Rs}12500$

Deshpande will get $= 25000 \times \frac{2}{10} = \text{Rs}5000$

Madlani will get $= 25000 \times \frac{3}{10} = \text{Rs}7500$

WN 2: Calculation Share of Goodwill

Share of Goodwill of Deshpande =$40000 \times \frac{2}{10} = \text{Rs}8000$

WN 3: Goodwill written off

Sathe's Gain = $8000 \times \frac{5}{8} = \text{Rs}5000$

Madlani's Gain = $8000 \times \frac{3}{8} = \text{Rs}3000$

Note: According to the solution provided in the book, amount paid to Deshpande is Rs 34,600 but according to our solution it is Rs 94,600.