Revaluation of Assets & Re-assessment of liabilities

1 Mark Question

1. Why are assets and liabilities revalued at the time of admission of a partner? (Compartment 2014)

Ans. Assets and liabilities are revalued at the time of admission of a partner, so that profit or loss arising on account of revaluation, may be adjusted among old partners in their old profit sharing ratio, since it belongs to them.

2 Mark Question

2. State any two reasons for the preparation of revaluation account on the admission of a partner. (All India 2008)

Ans. At the time of admitting a new partner, revaluation account is prepared for the below stated reasons:
(i) An incoming partner will not likely to suffer any loss relating to the period prior to his admission.
(ii) Old partners will not like to share the gain relating to the period prior to his admission.

3. What is a revaluation account? (All India 2008)

Ans. The account which is prepared to record changes in the value of assets and liabilities at the time of admission, retirement, death and change in profit sharing ratio is called revaluation account.

8 Marks Questions

4. W and R were partners in a firm sharing profits in the ratio of 3 : 2 respectively. On 31st March, 2013, their balance sheet was as follows

Balance Sheet
as at 31st March, 2013

Liabilities		Amt (₹)	Assets		Amt (₹)
Creditors		17,500	Cash		2,500
Investment Fluctuation Fund		4,000	Debtors	10,000	
Capital A/cs			(–) Provision for Doubtful Debts	350	9,650
W	20,000		Stock		12,500
R	15,000	35,000	Plant		17,500
Bank Loan		10,000	Patents		10,350
			Investments		10,000
			Goodwill		4,000
		66,500			66,500

B was admitted as a new partner on the following conditions:
(i) B will get 4/15th share of profits.
(ii) B had to bring Rs. 15,000 as his capital.
(iii) B would pay cash for his share of goodwill based on 2.5 years purchase of average profit of last 4 years.
(iv) The profits of the firm for the years ending 31st March, 2010, 2011, 2012 and 2013 were Rs. 10,000, Rs. 7,000 , Rs. 8,500, and Rs. 7,500 respectively.
(v) Stock was valued at Rs. 10,000 and provision for doubtful debts was raised up to X
(vi) Plant was revalued at Rs. 20,000.
Prepare revaluation account, partners' capital account and the balance sheet of the new firm. (Compartment 2014)

Dr **Revaluation Account** Cr

Particulars	Amt (₹)	Particulars		Amt (₹)
To Stock A/c (12,500 – 10,000)	2,500	By Plant (20,000 – 17,500)		2,500
To Provision for Doubtful Debts A/c (500 – 350)	150	By Loss in Revaluation Transferred to		
		W's Capital A/c	90	
		R's Capital A/c	60	150
	2,650			2,650

Dr **Partner's Capital Account** Cr

Particulars	W	R	B	Particulars	W	R	B
To Revaluation A/c	90	60	—	By Balance b/d	20,000	15,000	—
To Goodwill A/c	2,400	1,600	—	By Cash A/c	—	—	15,000
To Balance c/d	23,210	17,140	15,000	By Investment Fluctuation Fund A/c	2,400	1,600	—
				By Premium for Goodwill A/c	3,300	2,200	—
	25,700	18,800	15,000		25,700	18,800	15,000

Balance Sheet
as at............

Liabilities		Amt (₹)	Assets		Amt (₹)
Creditors		17,500	Cash		23,000
Capitals			Debtors	10,000	
W	23,210		(−) Provision for Doubtful Debts	500	9,500
R	17,140		Stock		10,000
B	15,000	55,350	Patents		10,350
Bank Loan		10,000	Plant		20,000
			Investments		10,000
		82,850			82,850

Working Note

$$\text{Average Profit} = \frac{10,000 + 7,000 + 8,500 + 7,500}{4} = 8,250$$

$$\text{Goodwill} = \text{Average Profit} \times \text{Number of Years Purchase}$$
$$= 8,250 \times 2.5 = 20,625$$

B's Share $= 20,625 \times \frac{4}{15} = 5,500$ which will be distributed among W and R in their sacrificing ratio, i.e. 3 : 2

5. Alfa and Beta were partners in a firm. They were trading in artificial limbs. On 1st April, 2013 they admitted Gama, a good friend of Beta into the partnership, Gama lost his one hand in accident and Alfa and Beta decided to give one artificial hand free of cost to Gama. The balance sheet of Alfa and Beta as at 31st March, 2013 was as follows.

Balance Sheet
as at 31st March, 2013

Liabilities		Amt (₹)	Assets	Amt (₹)
Provision for Doubtful Debts		40,000	Cash	1,00,000
Workmen's Compensation Fund		56,000	Sundry Debtors	8,00,000
Outstanding Expenses		30,000	Stock	2,00,000
Creditors		3,00,000	Machinery	3,86,000
Capitals A/cs			Profit and Loss A/c	40,000
Alfa	5,00,000			
Beta	6,00,000	11,00,000		
		15,26,000		15,26,000

Gama was admitted in the firm on the following terms:
(i) Gama will bring Rs. 4,00,000 as his share of capital, but he was unable to bring any amount for goodwill.
(ii) The new profit sharing ratio between Alfa, Beta and Gamma will be 3 : 2 : 1.
(iii) Claim on account of workmen compensation was Rs. 30,000.
(iv) To write off bad debts amounted to Rs. 40,000.

(v) Creditors were paid Rs. 20,000 more.
(vi) Outstanding expenses be brought down to Rs. 12,000.
(vii) Rs. 20,000 be provided for an unforeseen liability.
(viii) Goodwill of the firm was valued at Rs. 1,80,000.

Prepare revaluation account, capital accounts of partners and the opening balance sheet of the new firm. Also, identify any one value which the partners wanted to communicate to the Society. (Compartment 2014; VBQ)

Dr **Revaluation Account** Cr

Particulars	Amt (₹)	Particulars		Amt (₹)
To Creditors	20,000	By Outstanding Expenses		18,000
To Unforeseen Liability	20,000	By Loss on Revaluation Transferred to		
		Alfa's Capital A/c	11,000	
		Beta's Capital A/c	11,000	22,000
	40,000			40,000

Dr **Partner's Capital Account** Cr

Particulars	Alpha	Beta	Gamma	Particulars	Alpha	Beta	Gamma
To Profit and Loss A/c	20,000	20,000	—	By Balance b/d	5,00,000	6,00,000	—
To Beta's Capital A/c	—	—	30,000	By Workmen's Compensation Fund A/c (56,000 – 30,000)	13,000	13,000	—
To Revaluation A/c	11,000	11,000	—	By Cash A/c	—	—	4,00,000
To Balance c/d	4,82,000	6,12,000	3,70,000	By Gamma's Capital A/c (Treatment of goodwill)	—	30,000	—
	5,13,000	6,43,000	4,00,000		5,13,000	6,43,000	4,00,000

Balance Sheet
as at ....

Liabilities		Amt (₹)	Assets	Amt (₹)
Outstanding Expenses		12,000	Cash WN # 1	1,80,000
Workmen Compensation Fund		30,000	Sundry Debtors	7,60,000
Capital A/c's			Stock	2,00,000
Alfa	4,82,000		Machinery	3,86,000
Beta	6,12,000			
Gamma	3,70,000	14,64,000		
Unforeseen Liability		20,000		
		15,26,000		15,26,000

Value conveyed by the partners
Care and concern towards differently abled persons.

Working Note

Dr **Cash Account** Cr

Particulars	Amt (₹)	Particulars	Amt (₹)
To Balance b/d	1,00,000	By Creditors (3,00,000 + 20,000)	3,20,000
To Gamma's Capital A/c	4,00,000	By Balance c/d	1,80,000
	5,00,000		5,00,000

Calculation of Sacrificing Ratio

Sacrificing Ratio = Old Ratio – New Ratio

$$\text{Alfa} = \frac{1}{2} - \frac{3}{6} = \frac{3-3}{6} = \text{Nill}$$

$$\text{Beta} = \frac{1}{2} - \frac{2}{6} = \frac{3-2}{6} = \frac{1}{6}$$

NOTE (i) In the absence of any information, old ratio is assumed to be equal.
(ii) Bad debts are written-off from provision for doubtful debt.
(iii) Only Beta sacrifices on Gamma's admission.

6. Murari and Vohra were partners in a firm with capitals of Rs. 1,20,000 and Rs. 1,60,000 respectively. On 1st April, 2010 they admitted Yadav as a partner for l/4th share in profits on his payment of Rs. 2,00,000 as his capital and Rs. 90,000 for his l/4th share of goodwill. On that date, the creditors of Murari and Vohra wereRs. 60,000 and bank overdraft was Rs. 15,000. Their assets apart from cash included stock Rs. 10,000; debtors Rs. 40,000; plant and machinery Rs. 80,000; land and building Rs. 2,00,000. It was agreed that stock should be depreciated by Rs. 2,000; plant and machinery by 20%, Rs. 5,000 should be written-off as bad debts and land and building should be appreciated by 25%.
Prepare revaluation account, capital accounts of Murari, Vohra and Yadav and the balance sheet of the new firm. (All India 2011)

Dr **Revaluation Account** Cr

Particulars		Amt (₹)	Particulars	Amt (₹)
To Stock A/c		2,000	By Land and Building A/c	50,000
To Plant and Machinery A/c		16,000		
To Provision for Doubtful Debts A/c		5,000		
To Profit Transferred to				
Murari's Capital A/c	13,500			
Vohra's Capital A/c	13,500	27,000		
		50,000		50,000

Dr **Partners' Capital Account** Cr

Particulars	Murari	Vohra	Yadav		Murari	Vohra	Yadav
To Balance c/d	1,78,500	2,18,500	2,00,000	By Balance b/d	1,20,000	1,60,000	—
				By Cash A/c	—	—	2,00,000
				By Premium for Goodwill A/c	45,000	45,000	—
				By Revaluation A/c (Profit)	13,500	13,500	—
	1,78,500	2,18,500	2,00,000		1,78,500	2,18,500	2,00,000

Balance Sheet
as at 1st April, 2010

Liabilities		Amt (₹)	Assets		Amt (₹)
Capital A/cs			Stock (10,000 – 2,000)		8,000
Murari	1,78,50		Plant and Machinery (80,000 – 16,000)		64,000
Vohra	2,18,50		Debtors	40,000	
Yadav	2,00,000	5,97,000	(–) Provision for Doubtful Debts	5,000	35,000
Creditors		60,000	Land and Building (2,00,000 + 50,000)		2,50,000
Bank Overdraft		15,000	Cash		3,15,000
		6,72,000			6,72,000

Working Note

Memorandum Balance Sheet

Liabilities		Amt (₹)	Assets	Amt (₹)
Capital A/c's			Stock	10,000
Murari	1,20,000		Debtors	40,000
Vohra	1,60,000	2,80,000	Plant and Machinery	80,000
Creditors		60,000	Land and Building	2,00,000
Bank Overdraft		15,000	Cash (Balancing Figure)	25,000
		3,55,000		3,55,000

Dr **Cash Account** Cr

Particulars	Amt (₹)	Particulars	Amt (₹)
To Balance b/d	25,000	By Balance c/d	3,15,000
To Yadav's Capital A/c	2,00,000		
To Premium for Goodwill A/c	90,000		
	3,15,000		3,15,000