Unit IV

PARTNERSHIP ACCOUNT

BASIC CONCEPTS

1. Admission of a Partner

When a new partner is admitted to an existing partnership firm, the rights, responsibilities, and profit-sharing ratio change.

Key Adjustments:

- New **profit-sharing ratio**
- **Sacrificing ratio** (Old partners sacrifice part of their profit)
- **Revaluation of assets and liabilities**
- **Goodwill treatment**
- Adjustment of **capital accounts**

---

2. Retirement of a Partner

When a partner retires, the firm continues with remaining partners.

Key Adjustments:

- New **profit-sharing ratio**
- **Gaining ratio** (remaining partners gain retiring partner's share)
- **Revaluation of assets and liabilities**
- **Goodwill treatment**
- Settlement of **retiring partner's dues**

---

3. Death of a Partner

Similar to retirement, but with a few specific additions.

Additional Adjustments:

- Share of **profit till death**
- **Life insurance** proceeds (if taken)
- Final settlement to **legal heirs**

---

4. Goodwill Treatment

Goodwill is the firm's reputation/value. It's adjusted when partners are admitted, retire, or die.

Accounting Treatments:

- **Premium method**: New partner brings cash for goodwill.
- **Revaluation method**: Goodwill is revalued and adjusted in partners' capital accounts based on sacrificing/gaining ratio.

PROBLEM 1: Admission of a Partner

Q. A and B are partners sharing profits 3:2. C is admitted for 1/5 share. Goodwill of the firm is valued at ₹50,000. C brings ₹10,000 as his share of goodwill. Find sacrificing ratio and pass the journal entry.

Solution:

1. **Old Ratio** = A:B = 3:2
2. **New Share of C** = 1/5
3. **Remaining share** = 4/5 (shared by A & B)
4. **New Ratios**:
   A = 4/5 × 3/5 = 12/25
   B = 4/5 × 2/5 = 8/25
   C = 1/5 = 5/25
   ✅New Ratio = A:B:C = 12:8:5
5. **Old Ratio** = 3:2 = 15:10
   ✅New Ratio (A & B only) = 12:8 = 3:2
   So, Sacrificing Ratio = Old - New
   A = 15/25 – 12/25 = 3/25
   B = 10/25 – 8/25 = 2/25
   ✅Sacrificing Ratio = 3:2
6. **C's goodwill** = ₹10,000
   ➤To be distributed among A & B in 3:2

Journal Entry:

Cash A/c	Dr.	₹10,000
To A's Capital A/c		₹6,000

To B’s Capital A/c ₹4,000

(Being goodwill brought in by C and distributed in sacrificing ratio)

PROBLEM 2: Retirement of a Partner

Q. X, Y, and Z share profits in 5:3:2. Y retires. Goodwill is valued at ₹60,000. New ratio of X and Z is 3:2. Pass journal entry for goodwill adjustment.

Solution:

1. **Gaining Ratio** = New Ratio – Old Ratio
   - X: New = 3/5, Old = 5/10 = 1/2 → Gain = 3/5 – 1/2 = 1/10
   - Z: New = 2/5, Old = 2/10 = 1/5 → Gain = 2/5 – 1/5 = 1/5
     ✅Gaining Ratio = X:Z = 1:2
2. Y’s share of goodwill = ₹60,000 × 3/10 = ₹18,000
   ➤To be borne by X & Z in gaining ratio 1:2
   - X = ₹6,000
   - Z = ₹12,000

Journal Entry:

X’s Capital A/c Dr. ₹6,000

Z’s Capital A/c Dr. ₹12,000

To Y’s Capital A/c ₹18,000

(Being Y’s share of goodwill adjusted in gaining ratio)

PROBLEM 3: Death of a Partner

Q. A, B, and C are partners sharing profits 4:3:3. C dies on June 30. Profit for the year ended December 31 is ₹120,000. Calculate C’s share of profit till death and pass entry.

Solution:

1. **Profit till June 30** = 6 months
   Annual Profit = ₹120,000
   Half-year profit = ₹120,000 × 6/12 = ₹60,000

2. C’s Share = 3/10 × ₹60,000 = ₹18,000

Journal Entry:

Profit & Loss Suspense A/c Dr. ₹18,000

To C’s Capital A/c ₹18,000

(Being C’s share of profit till death credited)

Concept	Key Ratios	Adjustment Needed	Goodwill Treatment
Admission	Old/New/Sacrificing	Revaluation, Capital Adjustment	Brought in or adjusted
Retirement	Old/New/Gaining	Revaluation, Capital Settlement	Adjusted by gaining partners
Death	Old/New/Gaining	Profit till death, Legal Heir payment	Adjusted or insurance-based

---

TOPIC 1: ADMISSION OF A PARTNER

Problem 1: Capital and Goodwill Adjustment

Q. A and B are partners sharing profits in the ratio 3:2. They admit C as a new partner for 1/4th share. C brings ₹50,000 as capital and ₹20,000 for goodwill. The new ratio is 2:2:1. Pass the journal entries.

Solution:

1. **Old Ratio (A:B)** = 3:2

2. **New Ratio (A:B:C)** = 2:2:1
3. **Old Shares of A & B** = A = 3/5, B = 2/5
4. **New Shares** = A = 2/5, B = 2/5
5. **Sacrificing Ratio** = Old – New
    - A = 3/5 – 2/5 = 1/5
    - B = 2/5 – 2/5 = 0
      ➤Only A is sacrificing
6. **C's Goodwill** = ₹20,000
   ➤Given in cash, to be credited to A only (since B did not sacrifice)

Journal Entries:

Bank A/c Dr. ₹70,000
To C's Capital A/c ₹50,000
To Premium for Goodwill A/c ₹20,000
(Being capital and goodwill brought in by C)

Premium for Goodwill A/c Dr. ₹20,000
To A's Capital A/c ₹20,000
(Being goodwill credited to sacrificing partner)

TOPIC 2: RETIREMENT OF A PARTNER

Problem 2: Revaluation and Goodwill Adjustment

Q. X, Y, Z are partners in ratio 5:3:2. Y retires. Goodwill is valued at ₹40,000. The new ratio of X and Z is 3:2. Assets increased by ₹10,000 and liabilities reduced by ₹5,000. Pass necessary entries.

Solution:

Step 1: Goodwill Adjustment

- Y's Share = ₹40,000 × 3/10 = ₹12,000
- Gaining Ratio = New – Old
    - X = 3/5 – 5/10 = 1/10
    - Z = 2/5 – 2/10 = 2/10
      ➤Gaining Ratio = 1:2

So, goodwill will be adjusted:

- X's Capital A/c Dr. ₹4,000
- Z's Capital A/c Dr. ₹8,000
- To Y's Capital A/c ₹12,000

Step 2: Revaluation Account

Increase in Assets = ₹10,000
Decrease in Liabilities = ₹5,000
➤Profit on Revaluation = ₹15,000

Profit sharing ratio = 5:3:2

- X = ₹7,500
- Y = ₹4,500
- Z = ₹3,000

Journal Entries:

1. **Goodwill Adjustment:**

X’s Capital A/c Dr. ₹4,000
Z’s Capital A/c Dr. ₹8,000
To Y’s Capital A/c ₹12,000
(Being Y’s goodwill adjusted)

2. **Revaluation Profit:**

Revaluation A/c Dr. ₹15,000
To X’s Capital A/c ₹7,500
To Y’s Capital A/c ₹4,500
To Z’s Capital A/c ₹3,000
(Being profit on revaluation distributed)

□ TOPIC 3: DEATH OF A PARTNER

□ Problem 3: Share of Profit till Date of Death

Q. P, Q, and R share profits in 3:2:1. R died on March 31. Annual profit for the year is estimated at ₹1,80,000. Calculate R’s share of profit till death and pass the entry.

Solution:

- Period till death = 3 months = 3/12
- Profit till death = ₹1,80,000 × 3/12 = ₹45,000
- R’s Share = 1/6 × ₹45,000 = ₹7,500

Journal Entry:

Profit and Loss Suspense A/c Dr. ₹7,500
To R’s Capital A/c ₹7,500
(Being R’s share of profit till death transferred)

□ TOPIC 4: CHANGE IN PROFIT SHARING RATIO (BONUS)

□ Problem 4: Adjustment for Goodwill without Admission or Retirement

Q. A, B, and C are partners in ratio 4:3:3. They decide to change the ratio to 5:3:2. Goodwill of the firm is valued at ₹60,000. Pass adjustment entry for goodwill.

Solution:

Step 1: Calculate Old and New Shares:

- Old Ratio = 4:3:3 = 10 parts
- New Ratio = 5:3:2 = 10 parts

Step 2: Find Sacrifice / Gain

- A: 4/10 → 5/10 = Gain of 1/10
- B: 3/10 → 3/10 = No Change
- C: 3/10 → 2/10 = Sacrifice of 1/10

So, A has gained 1/10 and C has sacrificed 1/10. Adjust goodwill accordingly.

Goodwill = ₹60,000
Share = 1/10 × ₹60,000 = ₹6,000

Journal Entry:

A's Capital A/c Dr. ₹6,000
To C's Capital A/c ₹6,000
(Being goodwill adjusted due to change in ratio)

QUICK REVISION

Topic	Entry Required?	Common Ratios Needed	Goodwill Impact
Admission	✓Yes	Old, New, Sacrificing	New partner compensates
Retirement	✓Yes	Old, New, Gaining	Retiring partner compensated
Death	✓Yes	Same as retirement	Legal heir gets share
Change Ratio	✓Sometimes	Old vs. New	Gaining partner pays
