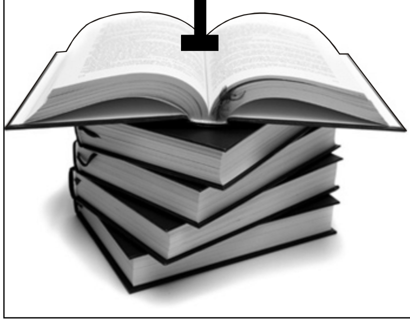
Chapter 1



Partnership Final Accounts

INDIAN PARTNERSHIP ACT, 1932

Sec. 4. Definition of “partnership”, “partner”, “firm” and “firm name”.

“Partnership” is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Persons who have entered into partnership with one another are called individually “partners” and collectively a “firm”, and the name under which their business is carried on is called the “firm name”.

From the above definition of partnership, the essential elements of partnership can be understood as:

“Partnership” is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Persons

There should be at least two persons to form a partnership or partnership firm.

- *Restrictions on the Number of Persons:* The maximum number of members that can exist in partnership is 10 in case of a firm carrying on banking business and 20 in case of any other business.

  This restriction is placed by the Companies Act and not the partnership act.
- *Companies Act, 1956 Hide/Show:* **Sec. 11.** Prohibition of associations and partnerships exceeding certain number:

  (1) No company, association or partnership consisting of more than ten persons shall be formed for the purpose of carrying on the business of banking, unless it is registered as a company under this Act, or is formed in pursuance of some other Indian Law.

(2) No company, association or partnership consisting of more than twenty persons shall be formed for the purpose of carrying on any other business that has for its object the acquisition of gain by the company, association or partnership, or by the individual members thereof, unless it is registered as a company under this Act, or is formed in pursuance of some other Indian law.

(3) This section shall not apply to a joint family as such carrying on a business; and where a business is carried on by two or more joint families, in computing the number of persons for the purposes of Sec. 11(1) and Sec. 11(2), minor members of such families shall be excluded.

(4) Every member of a company, association or partnership carrying on business in contravention of this section shall be personally liable for all liabilities incurred in such business.

(5) Every person who is a member of a company, association or partnership formed in contravention of this section shall be punishable with fine which may extend to ten thousand rupees.

- *Who have Agreed:* There should be an agreement between those persons who are forming the partnership. The agreement is the foundation for the partnership. Partnerships can arise only from a contract and not status.

  Indian Partnership Act, 1932 Hide/Show: **Sec. 5.** Partnership not created by status

  The relation of partnership arises from contract and not from status; and, in particular, the members of a Hindu undivided family carrying on a family business as such, or a Burmese Buddhist husband and wife carrying business as such, are not partners in such business.

- *The Profits of a Business:* There should be a business carried on by the partnership and that too with an intention to make and share profits of that business.

  Therefore, we can say "No Business ⇒ No Partnership" as well as "No intention to share profits ⇒ No Partnership".

  Though no specific mention of sharing of losses is made, we consider that Sharing profits implies sharing losses also.

  Indian Partnership Act, 1932 Hide/Show: **Sec. 2.** Definitions

  (b) "business" includes every trade, occupation and profession;

- *Carried on by all or any of them acting for all:* The business may be carried on by any one or more of the partners.

- *Acting for all:* This implies that a partner conducting the business should be understood as conducting the business on behalf of all the partners. Each partner would be responsible for the acts of the other partners in relation to the firm.

  As far as the outsiders are concerned, the partners and the firm are one and the same.

- *Mutual Agency [Principal Agent Relationship]:* In his/her role as a partner, a person acts both as a principal as well as an agent.

  A partner is an agent for the acts that he/she does on behalf of the firm, whereby he/she can bind the other partners for such acts. The other partners would be the principals for such acts.

  With regard to the acts of the other partners, he/she will act as the principal (since he as a partner is bound by the acts of the other partners on behalf of the firm).

  Where a partner cannot be made responsible for the acts of one or more other partners, we cannot say they together form a partnership. This mutual agency is what really decides whether there is a partnership or not. Thus, it is said the "Mutual Agency" is the real test of partnership.
- *Indian Partnership Act, 1932 Hide/Show:* **Sec 18.** Partner to be agent of the firm.

  Subject to the provisions of this Act, a partner is the agent of the firm for the purpose of the business of the firm.
- *Partners:* Persons who have entered into partnership with one another are called individually "partners".
- *Partnership:* The relationship between the persons is called "partnership".
- *Firm:* The partners are collectively called a "firm".
- *Firm Name:* The name under which the partnership business is carried on is called the "firm name".

Partnership is a form of business organisation. A business and its ownership are independent concepts. The idea that the actual business and the form of organisation that is owning it are different would help you in creating an understanding on the difference in accounting for partnership firms and other forms of business organisations. The same business may be owned by a "sole proprietor", a "partnership firm", a "co-operative society", a "company" or any other form of business organisation.

Ascertaining the profit or loss is an idea related to the business. How the profit made is dealt with is an idea related to the form of business organisation. Thus, the process of profit ascertainment (final accounting) for a business would be the same whatever may be the form of business organisation.

What's the Difference?

The way the profits made by an organisation are shared is what is different from organisation to organisation. Taking a hypothetical case of a business owned by different types of business organisations, the process of ascertaining profits would be more or less the same but the process of dealing with profits made would be different from one form of business organisation to another.

They have an understanding on the difference in accounting where the same business is conducted by two different forms of business organisations, let us consider an example of a business being conducted by a sole proprietor "Mr. Narayanan" and another case of the same business being run by a partnership firm "M/s. Mani and Murthy" who share the profits of the firm between them in the ratio 1 : 2.

Final Accounting » Business Owned by a Sole Proprietor

Final Accounting
Trial Balance of M/s. Wearall Textiles as on 31st March, 2006

Particulars	L/F	Debit Amount (in `)	Credit Amount (in `)
Capital	-		1,00,000
Opening Stock	-	15,000	
Closing Stock	-	25,000	
Purchases	-	1,50,000	
Rent Paid	-	25,000	
Sales	-		3,20,000
Wages	-	50,000	
Commission Received	-		3,000
Assets	-	1,51,000	
Debtors	-	45,000	
Creditors	-		38,000
Total		**4,61,000**	**4,61,000**

Dr. **Trading and Profit and Loss Account** **Cr.**

Particulars	Amount (in `)	Amount (in `)	Particulars	Amount (in `)	Amount (in `)
To Opening Stock		15,000	By Sales		3,20,000
To Purchases		1,50,000	By Closing Stock		25,000
To Wages		50,000			
To Gross Profit		1,30,000			
		3,45,000			**3,45,000**
To Rent		25,000	By Gross Profit		1,30,000
To Net Profit		1,08,000	By Commission Received		3,000
		1,33,000			**1,33,000**

Dr.		Capital Account			Cr.
Particulars	**Amount (in `)**	**Amount (in `)**	**Particulars**	**Amount (in `)**	**Amount (in `)**
To Balance c/d		2,08,000	By Balance b/d		1,00,00
			By Net Profit		1,08,000
		2,08,000			**2,08,000**
			By Balance b/d		2,08,000

RECORDING GROSS PROFIT AND NET PROFIT

Should the posting relating to gross profit and net profit read “To P & L A/c” and “To Capital A/c” respectively. How is it that it shows “Gross Profit” and “Net Profit”.

Final Accounting » Business Owned by the Partnership Firm

Assuming all other data to be the same and the capital of ` 1,00,000 is owned by the two partners Mani and Murthy as ` 30,000 and ` 70,000 respectively.

Trial Balance of M/s. Wearall Textiles as on 31st March, 2006

Particulars	L/F	Debit Amount (in `)	Credit Amount (in `)
Mani’s Capital	-		70,000
Murthy’s Capital	-		30,000
Opening Stock	-	15,000	
Closing Stock	-	25,000	
Purchases	-	1,50,000	
Rent Paid	-	25,000	
Sales	-		3,20,000
Wages	-	50,000	
Commission Received	-		3,000
Assets	-	1,51,000	
Debtors	-	45,000	
Creditors	-		38,000
Total		**4,61,000**	**4,61,000**

The Trading and Profit and Loss Account would be the same ⇒ **Net Profit = ` 1,08,000.**

Dr. **Trading and Profit and Loss Account** **Cr.**

Particulars	Amount (in ₹)	Amount (in ₹)	Particulars	Amount (in ₹)	Amount (in ₹)
To Opening Stock		15,000	By Sales		3,20,000
To Purchases		1,50,000	By Closing Stock		25,000
To Wages		50,000			
To Gross Profit		1,30,000			
		3,45,000			**3,45,000**
To Rent		25,000	By Gross Profit		1,30,000
To Net Profit c/d		1,08,000	By Commission Received		3,000
		1,33,000			**1,33,000**
To Net Profit (Mani)		36,000	By Net Profit b/d		1,08,000
To Net Profit (Murthy)		72,000			
		1,08,000			**1,08,000**

Distribution of Profits among Partners

Partner's profit sharing ratio ⇒ Mani : Murthy = 1 : 2

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

Partner's share of profits = Firm's profit × Profit sharing proportion

Mani's Share $= ₹\ 1{,}08{,}000 \times \frac{1}{3} = ₹\ 36{,}000$

Murthy's Share $= ₹\ 1{,}08{,}000 \times \frac{2}{3} = ₹\ 72{,}000$

₹ 1,08,000

Dr. **Partner's Capital Account** **Cr.**

Particulars	Mani (in ₹)	Murthy (in ₹)	Particulars	Mani (in ₹)	Murthy (in ₹)
To Balance c/d	1,06,000	1,02,000	By Balance b/d	70,000	30,000
			By Net Profit	36,000	72,000
	1,06,000	**1,02,000**		**1,06,000**	**1,02,000**
			By Balance b/d	1,06,000	1,02,000

The difference that you can notice is that the profit of ` 1,08,000 instead of getting into the account representing a single owner (capital account) is distributed among all the owners, i.e., their respective capital accounts.

INCOME DISTRIBUTION

Appropriation

= Setting aside money for a specific purpose

Factors of Production » Returns

In economic terms, the four basic factors of production are Land, Labour, Capital and Organisation. Each of these factors would be compensated by sharing a part of the income earned. What they get is what is called the return for the factor.

- Rent is the return for Land;
- Wages are the returns for Labour/Labour;
- Interest is the return for Capital; and
- Profits are the returns for the Organisation.

Thus, profit earned by the partnership firm can be said to be the returns earned by the organisation.

Organisation » Partnership Firm

Land, Labour and Capital are factors of production which we see or feel. Organisation is an intangible factor that combines these three factors to achieve the intended objective. Organisation can therefore be understood as, the efforts made by those who have contributed capital. These efforts may take many different forms, some tangible and some intangible.

What Constitutes "Organisation" in a Partnership Firm?

In a partnership firm, the efforts made by the partners who are the contributors of capital, represent the "Organisation". All these contributions, apart from the capital they contribute form the factor we call "Organisation".

Partner's contribution to the firm takes many different forms which may be tangible or intangible. Some of them are:

- *Time:* The partners spend their time and energy in working for the firm by looking after the day-to-day affairs of the firm.
- *Business Relations:* The partners through their contacts in the society bring in customers which would result in more sales.

K *Intelligence:* The partners use their intelligence and abilities at various situations like in solving problems faced by the firm, tiding over tough situations, overcoming competitions etc.

Why not Capital?

We do not consider the Capital contributed by the partners since "Capital" itself is dealt with as a separate factor.

Varied Contributions of Partners towards the Organisation

Since no two human beings can be exactly of the same capabilities, the contributions made by the partners for the factor called organisation varies from partner to partner. Each partner contributes according to his/her abilities and possibilities.

Remunerating the Factors of Production in a Partnership Firm

Let us limit our idea to remunerating the two factors of production — Capital and Organisation only.

Judicious Distribution of the Firm's Profits

A, B and C are partners in a firm. The firm has made a profit of ` 3,00,000. What would be the judicious share of profits to be distributed to each partner A, B and C?

Share Equally

A, B and C sharing ` 1,00,000 each.

This sounds prudent if the contributions of A, B and C towards the firm is the same in all respects. Say, A, B and C are of the same intelligence level; they work for the same time for the firm; they have contributed the same amount of Capital for the firm; they are having more or less the same contacts outside through which sales are generated; they have all withdrawn the same amounts of money for their personal uses (drawings) etc. In such a situation, it would be appropriate to give each an equal share.

Equal Share not a Judicious Share Always

If we consider the following aspects, we may have to agree that sharing the profits of the firm equally amongst partners may not be the judicious (best) way.

Unequal Capital Contributions

The capital contributed by A, B and C is ` 2,00,000, ` 75,000 and ` 1,00,000 respectively. Now, since A, B and C have contributed varied amounts of Capital towards the firm, it would not be appropriate to share the profits equally among them.

To Compensate » Pay Interest on Capital

Compensate for the uneven contributions towards capital and then share the profits equally (if contributions of A, B and C towards the firm in all other respects is the same). Greater the Capital contributed, greater the interest earned. This would set right the difference in contributions in the form of capital.

Profit equal to "Interest on Capital" payable to partners is first paid away and then the remaining profit can be shared equally.

Unequal Time Spent

B works full time in the firm and A and C are passive partners. Now, since A, B and C have contributed varied amounts of time and energy towards the firm, it would not be appropriate to share the profits equally among them.

To Compensate » Pay Salary to Partner

Compensate for the uneven contributions of time and energy towards the firm and then share the profits equally (if contributions of A, B and C towards the firm in all other respects is the same). The salary paid to B would be compensation for his greater contribution.

Profit equal to "Salary to Partners" is first paid away and then the remaining profit can be shared equally.

Public Relations/Contacts

C has greater contacts in the outside world, a lot of customers are C's contacts. Now, the contribution of C towards the sales of the firm through his contacts is greater than that of A and B. Therefore, it would not be appropriate to share the profits equally among them.

To Compensate » Pay Commission to Partner

Compensate C for the greater contributions he has made towards the firm and then share the profits equally (if contributions of A, B and C towards the firm in all other respects is the same). The commission paid to C for sales made to customers who are his contacts would be compensation for his greater contribution.

Profit equal to "Commission to Partners" is first paid away and then the remaining profit can be shared equally.

Drawings

The drawings of A, B and C are ` 20,000, ` 2,000 and ` 15,000 respectively. Since drawings is nothing but capital being withdrawn, A and C have withdrawn greater amount of capital whereas B has withdrawn a lesser amount. This would result in A's and C's capital contribution being lesser and B's capital contribution being greater.

Remedy » Charge Interest on Drawings

Greater the drawings greater the interest payable by the partners. This would compensate the unevenness in drawings made by the partners.

Remunerating Organisation = Distributing Profits

As can be seen from the above explanation, Salary to Partners, Commission to Partners, etc., are all paid out of profits made. These are different methods of compensation for the contributions made by partners to the firm.

- All these contributions together are identified as "Organisation"

  and
- Remuneration for organisation is profit.

⇒ The payments for all these are nothing but methods of sharing profits

Profit Distribution » Accounting Treatment

Consider the following information in relation to M/s. ABC and Co., a partnership firm with A, B and C as partners.

Illustration:

1. Net Profit – ` 3,74,000
2. Interest on Capital @ 5% – A: ` 10,000; B: ` 3,750 and C: ` 5,000
3. Salary to Partner – B: ` 24,000
4. Commission to Partner – C: ` 52,000
5. Interest on Drawings @ 5% – A: ` 1,000; B: ` 100 and C: ` 750

Solution:

Since Interest on Capital, Salary to Partners etc., are methods of distribution of profit, they are to be made after ascertaining profits. Thus, the accounting for the distribution of profits is a process that follows the ascertainment of net profits.

Assuming the distribution to have been made through Profit and Loss A/c, the P/L A/c and the Partner's Capital accounts would be as below:

Dr. **Profit and Loss Account** **Cr.**

Particulars	Amount (in `)	Amount (in `)	Particulars	Amount (in `)	Amount (in `)
To Net Profit		3,74 ,000			
		21,33,000			**21,33,000**
To A's Cap (int)	10,000		By Net Profit b/d		3,74,000
To B's Cap (int)	3,750		By A's Cap (int drw)	1,000	
To C's Cap (int)	5,000	18,750	By B's Cap (int drw)	100	
To B's Cap (sal)	24,000	24,000	By C's Cap (int drw)	750	1,850
To C's Cap (comm)	52,000	52,000			
To Bal c/d (Distr Pr)		2,81,100			
		3,75,850			**3,75,850**
To A's Cap (Pr)	93,700		By Bal b/d (Distr Pr)		2,81,100
To B's Cap (Pr)	93,700				
To C's Cap (Pr)	93,700	2,81,100			
		2,81,100			**2,81,100**

Notes:

- Distr. Pr ⇒ Distributable Profit; int. drw ⇒ Interest on Drawings; int ⇒ Interest; Sal ⇒ Salary; Comm ⇒ Commission; Pr ⇒ Profit Share.
- The account is balanced a number of times to enable deriving information easily. Specifically, the Distributable profit is carried down so that we can have the figure which is to be used for calculating the partner's share of profits.

Distribution of Profits among Partners

Partner's profit sharing ratio ⇒ A : B : C = 1 : 1 : 1

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

Partner's Share of Profits = Distributable Profit × Profit Sharing Proportion

Therefore,

A's Share = ` 2,81,100 × $\frac{1}{3}$ = ` 93,700

B's Share = ` 2,81,100 × $\frac{1}{3}$ = ` 93,700

C's Share = ` 2,81,100 × $\frac{1}{3}$ = ` 93,700

` 2,81,100

Dr. **Partner's Capital Accounts** **Cr.**

Particulars	A (in `)	B (in `)	C (in `)	Particulars	A (in `)	B (in `)	C (in `)
To P&L (Int)	1,000	100	750	By Bal b/d	2,00,000	75,000	1,00,000
To Drawings	20,000	2,000	15,000	By P&L (int)	10,000	3,750	5,000
To Bal c/d	2,82,700	1,94,350	2,34,950	By P&L (sal)		24,000	
				By P&L (com)			52,000
				By P&L (pr)	93,700	93,700	93,700
	3,03,700	**1,96,450**	**2,50,700**		**3,03,700**	**1,96,450**	**2,50,700**
				By Bal b/d	2,82,700	1,94,3500	2,34,950

Ledger Postings » Unavailability of Information

If you interpret the ledger postings in the above P/L A/c and the Partner's Capital A/cs, you can find that all the postings in the Partner's Capital A/cs read either "To P/L A/c" or "By P/L A/c" and in the "Profit and Loss A/c" read "To _ Capital A/c" or "By _Capital A/c". These postings can be interpreted as:

K In "Profit and Loss A/c":

There is a transfer of credit balance to "_ Capital A/c" to the extent of ` __.

There is a transfer of debit balance to "_ Capital A/c" to the extent of ` __.

K In "_ Capital A/c":

There is a transfer of a credit balance from "Profit and Loss A/c".

There is a transfer of a debit balance from "Profit and Loss A/c".

Since the natural flow is from the Profit and Loss account to the Capital account, we would interpret it as From P/L A/c to __Capital A/c. Theoretically, it is capable of being interpreted the other way also.

Information not Available

Generally, we would be able to identify the reason for a debit or credit by reading the posting itself. However, here it would be difficult to gather the information relating to all credits and debits that way, since all of them look similar. Thus, we would not be able to derive the information as to the reason for which the debits and credits are made.

Though "To A's Cap (int)" seems to be creating the idea that the posting gives the information relating to the purpose for which the amount is being transferred, it is not so. It would not be practically possible to write down such details as (int), (sal), etc., more so in mechanised systems of accounting (using computers). [To understand this limitation, read the posting as "To _ Capital A/c" only ignoring the wordings within the brackets].

Solution:

To derive the information that we need, we create additional account heads which work as controlling accounts.

The basic purpose of accounting is derivation of information.

The more information we need, the more accounting heads we need to maintain.

Charge against Profits vs. Appropriation of Profits

- Appropriation = Setting aside money for a specific purpose
- Charge = Financial liability

Classification of Debits to Profit and Loss Account

The various items debited to the Profit and Loss A/c can be classified into two as:

- *Charge against Profit:* Debits which represent an expenditure or loss.

  Salaries, Wages, Rent, Depreciation, Loss on Sale of Assets etc., are all charges against profits.
- *Appropriation of Profit:* Debits which result in the profit being kept aside.

  Creation of reserves is an example of profit appropriation. Reserves are created by transferring credit balance (a certain amount of profit) from the profit and loss account to the reserve account.

Journal in the Books of M/s. Razmataz Chemicals for the period from __ to 31st December, 2005

Date	V/R No.	Particulars	L/F	Debit Amount (in `)	Credit Amount (in `)
1st to 30th	–	Profit and Loss A/c Dr. To General Reserve A/c [For the amount transferred to the general reserve.]	- -	xxx	 xxx

The Profit and Loss account is debited both while profits are charged as well as when profits are appropriated. However, creation of a reserve is appropriation as it does not result in the profit being used up. It results in the profit being maintained/shown in two different accounts or profit being transferred to a different account.

Reserves are created by charging profits. Creation of reserves is an appropriation of profits.

Interest on Capital, Salary, Commission etc., to Partners » Appropriations

Distribution of profit to partners is appropriation of profits. It is to be understood as profit being kept aside to be given to the owners as a return for their contributions.

"Interest on Capital", "Salary to Partners", etc., paid to partners are different methods adopted to compensate their varied contributions and thus ensure equitable distribution of profits. Therefore, all these payments made to partners would also be appropriations of profits and not charge against profits.

Using Profit & Loss Appropriation A/c

To differentiate between charges and appropriations of profits being made to the profit and loss account, the P & L A/c is divided into two by creating a new account by name "Profit and Loss Appropriation A/c".

The net profit is transferred to "P & L Appropriation A/c" and all the appropriations are made from this account.

The same postings as above made using the "P & L Appropriation A/c" would be:

Dr. Profit and Loss Account Cr.

Particulars	Amount (in `)	Amount (in `)	Particulars	Amount (in `)	Amount (in `)
To P & L Appr (Net Profit) A/c		3,74 ,000			
		21,33,000			**21,33,000**

Dr. Profit and Loss Appropriation Account Cr.

Particulars	Amount (in `)	Amount (in `)	Particulars	Amount (in `)	Amount (in `)
To A's Cap (int)	10,000		By P/L A/c (Net Profit)		3,74,000
To B's Cap (int)	3,750		By A's Cap (int drw)	1,000	
To C's Cap (int)	5,000	18,750	By B's Cap (int drw)	100	
To B's Cap (sal)		24,000	By C's Cap (int drw)	750	1,850
To C's Cap (comm)		52,000			
To Bal c/d (Distr Pr)		2,81,100			
		3,75,850			**3,75,850**
To A's Cap (Pr)	93,700		By Bal b/d (Distr Pr)		2,81,100
To B's Cap (Pr)	93,700				
To C's Cap (Pr)	93,700	2,81,100			
		2,81,100			**2,81,100**

Dr. **Partner's Capital Accounts** Cr.

Particulars	A (in `)	B (in `)	C (in `)	Particulars	A (in `)	B (in `)	C (in `)
To P&L Appr (Int)	1,000	100	750	By Bal b/d	2,00,000	75,000	1,00,000
To Drawings	20,000	2,000	15,000	By P&L Appr (int)	10,000	3,750	5,000
To Bal c/d	2,82,700	1,94,350	2,34,950	By P&L Appr (sal)		24,000	
				By P&L Appr (com)			52,000
				By P&L Appr (pr)	93,700	93,700	93,700
	3,03,700	**1,96,450**	**2,50,700**		**3,03,700**	**1,96,450**	**2,50,700**
				By Bal b/d	2,82,700	1,94,3500	2,34,950

What Difference does using Appropriation A/c Make?

Using P & L Appropriation account would enable handling all the information relating to appropriation of profits through a separate account. But, when we come to reading the postings in the appropriation account as well as the Capital accounts, the only difference we can see is that "P & L A/c" is replaced by "P & L Appropriation A/c".

Even after replacing the P & L A/c with the P & L Appropriation A/c, we will not get the information as to the reason for which the debits and credits are being made. The postings can be interpreted as:

- In "Profit and Loss Appropriation A/c":

  There is a transfer of credit balance to "_ Capital A/c" to the extent of ` __.

  There is a transfer of debit balance to "_ Capital A/c" to the extent of ` __.

- In "_ Capital A/c":

  There is a transfer of a credit balance from "Profit and Loss Appropriation A/c".

  There is a transfer of a debit balance from "Profit and Loss Appropriation A/c".

Only a Slight Variation

A slightly different idea that the transfers are from profit and loss appropriation account and thus relate to profits distributed can be obtained. But for this, there is virtually no difference in the information available.

Deriving More/Clear Information

The basic purpose of accounting is derivation of information

The more information we need, the more accounting heads we need to maintain.

To derive the information that we need, we create additional accounts.

Interest on Capital

In the absence of an agreement between the partners, a partner is not entitled to receive any interest on capital even if there is a variation in the profit sharing ratio and the capital contribution.

If there is an agreement between the partners, then interest is to be paid at the rates agreed upon.

Interest to be Paid Only Out of Profits

Even where the agreement provides for payment of interest on capital, it will not be paid if there are losses.

Indian Partnership Act, 1932 Hide/Show: **Sec. 13.** Mutual rights and liabilities

Subject to contract between the partners,

(c) where a partner is entitled to interest on the capital subscribed by him, such interest shall be payable only out of profits.

Interest on Drawings

No specific mention is made about drawings in the act. Therefore, it is assumed that the provisions that are applicable for capital would also be applicable for drawings, whereby,

- in the absence of an agreement between the partners, a partner is not entitled to pay any interest on drawings.
- if there is an agreement between the partners, then interest is to be charged at the rates agreed upon.

Interest on Partner's Loans or Advances

In the absence of an agreement between the partners, a partner is entitled to receive interest at the rate of 6% p.a. on any payment or advance made beyond the amount of capital he has to contribute.

If there is an agreement between the partners, then interest is to be paid at the rates agreed upon.

Indian Partnership Act, 1932 Hide/Show: **Sec. 13.** Mutual rights and liabilities

Subject to contract between the partners,

(d) a partner making, for the purposes of the business, any payment or advance beyond the amount of capital he has agreed to subscribe, is entitled to interest thereon at the rate of six per cent per annum.

Some Conventions Followed in Accounting

In addition to the specific provisions available in the "Indian Partnership Act, 1932", a few other conventions are followed in solving problems involving partnerships.

1. **Rate of Interest:** Where the partners have agreed upon to pay interest on capital and/or charge interest on drawings but the agreement is silent as to the rate of interest to be paid or charged, we consider the rate of interest to be 6%. This may be based on the fact that in providing interest for advances, the act specifies 6% rate of interest. Since 6% is considered reasonable in one case, it may be taken in other cases also.

   Partner's Relative's Loans: Practically, partner's relatives are outsiders for the firm and it would not be appropriate to think about them based on the agreement between parties. But where the information is missing and you have to make an assumption to go along with problem solving, you may apply the same rule that is applied to the partner's advances to loans/advances made by the partner's relatives also. This should be a last resort attempt only.

   Where there is no information relating to interest payment to partners relatives as well as the rate of interest, interest should be paid at the rate of 6% p.a.

   By profit sharing ratio in a partnership firm, we mean the ratio in which the profits and losses of the firm are to be distributed amongst the partners. The basis for arriving at the ratio is the agreement between the partners. If there is a partnership deed, the ratio should be ascertained from the provisions in the partnership deed. In the absence of a partnership deed and where there is no indication as to the agreement between the partners in this aspect, it should be considered as equal share for all partners. The ratio may be a specified as absolute values or it may be taken as the ratio fo their Capital account balances or it may be based on anything else as agreed upon by the partners. Deriving this ratio (if it is not given) would be one important requirement in problem solving.

2. **Different Ratios for Profit Sharing and Loss Sharing:** If the partners so agree, the Profit Sharing Ratio and the Loss Sharing Ratio may be different. There may be a partner who has a share in profits only but not in losses.

3. **Share in Losses Only:** There cannot be a partner who has a share in losses only but not in profits. This is for the reason that there would be no partnership if there is no share in profits.

   "Partnership" is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Expressing the Profit Sharing Ratio

The profit sharing ratio may be expressed in a number of different forms. Whatever may be the form in which the ratio is expressed, it can always be converted to a form suitable to you.

1. Simple Ratio [Natural Numbers Represent Shares]:

May, Day and Way are partners sharing profits in the in the ratio 1 : 3 : 4.

Rewriting the ratio as below would aid in your calculations.

May: Day: Way = 1 : 3 : 4

$$= \frac{1}{8} : \frac{3}{8} : \frac{4}{8} \quad [1 + 3 + 4 = 8]$$

This can be simplified further and written as $\frac{1}{8} : \frac{3}{8} : \frac{1}{2}$.

However, expressing the shares as ratios with a common denominator would be helpful.

2. Simple Ratio [Fractions Represent Shares]:

Where the shares are represented by fractional numbers, one should always ensure that the sum of the fractional parts adds up to 1.

3. Like Fractions Represent Shares:

Fractions with the same denominator are like fractions.

Ramu, Damu and Mamu share profits in the ratio $\frac{2}{9} : \frac{3}{9} : \frac{4}{9}$.

Check:

$$\frac{2}{9} : \frac{3}{9} : \frac{4}{9} = \frac{2+3+4}{9}$$

$$= \frac{9}{9}$$

$$= 1$$

$$\text{Sum of Like Fractions} = \frac{\text{Sum of Numerators}}{\text{Common Denominator}}$$

Just check up whether the numerators are adding (2 + 3 + 4) up to the common denominator (9) or not.

Note: To be cautious, make it a habit to write down the ratio in fractional form if the shares are given as natural numbers and *vice versa* so that you can check this aspect as well as have a form useful for calculations.

4. Unlike Fractions Represent Shares:

Fractions without a common denominator are unlike fractions.

Goon, Doon and Moon share profits in the ratio $\frac{1}{2}$, $\frac{1}{3}$ and $\frac{1}{4}$.

$$\text{Sum of Unlike Fractions} = \frac{\text{Sum of (Product of) the Fraction and the LCM of the Denominators}}{\text{LCM of the Denominators}}$$

$$\text{Thus, } \frac{1}{2} + \frac{1}{3} + \frac{1}{4} = \frac{(\frac{1}{2}\times 12)+(\frac{1}{3}\times 12)+(\frac{1}{4}\times 12)}{12}$$

[LCM of denominators i.e., 2, 3, 4 is 12]

$$= \frac{6+4+3}{12}$$

$$= \frac{13}{12}$$

$$\neq 1$$

What to do in such cases: If you find that the fractions representing shares of partners are not adding up to 1, you have to derive the actual ratio using the given fractions.

$$\text{Goon: Doon: Moon} = \frac{1}{2}:\frac{1}{3}:\frac{1}{4}$$

$$= \frac{1}{2}\times 12:\frac{1}{3}\times 12:\frac{1}{4}\times 12$$

[Multiplying all the terms of the ratio with the same number (the LCM of denominators 2, 3, 4, i.e., 12) will not change the ratio.]

= 6: 4: 3

$$= \frac{6}{13}:\frac{4}{13}:\frac{3}{13} \quad [6 + 4 + 3 = 13]$$

This represents the ratio of profit sharing between partners and is in a form suitable for calculations.

Try this: A father left his property to be shared by his three sons as follows: 1/2 to the youngest, 1/3 to the middle and 1/6th to the eldest son. They were struck up with the problem of sharing the 17 horses in their stable. They approached their father's best friend and asked him to help them out. He thought about it and asked them to take one of his horses, include it in the horses to be shared and then share the horses (along with the one he gave). The sons did so and finally were left with 1 horse which they returned to its rightful owner. How did this happen?

This is a small problem that lets you understand the above concept.

Interest on Capital

Interest on Capital is to be paid:

- *Only when agreed upon:* Interest on capital is to be paid to partners only if it is specifically agreed upon. If there is no mention regarding this, in the partnership agreement (deed), then no interest need be paid.
- *Only out of profits:* Interest is to be paid only out of profits. Where there is a loss, no interest should be paid on capital, even if the partnership agreement provides for the same.
- *@ 6% if rate is not mentioned:* Where the partnership deed provides for payment of interest on capital and it does not mention the rate of interest to be paid, it is a convention to pay interest @ 6% p.a.

On What Balance is Interest Paid? Interest is paid on capital for the reason that it has been used for the purpose of the partnership business.

The balance in Capital account unless where it is fixed, keeps fluctuating on account of a number of reasons, thus making it difficult to assess the amount of capital employed in the business. There would be a change on account of appropriations made at the end of the accounting period like salary to partners, commission to partners, etc. Even during the course of the accounting period, the balances may change on account of additional capital introduced, capital withdrawn, etc.

In the absence of appropriate information, it is a convention that interest is paid on the opening balances in Capital Accounts.

In problem solving, we will come across these situations:

- *Opening balance known:* Where the Capital A/c balances at the beginning of the accounting period are known and there is no change in the balance throughout the period, the interest is calculated on the opening balance.
- *Closing balance and appropriations at the end known:* Where the Capital A/c balances at the end are known and the changes at the end of the accounting period that have affected the account are also known, the opening balance in the capital accounts is ascertained and interest is calculated thereon using the information relating to the changes.
- *Closing balance and all transactions known:* Where the Capital A/c balances at the end are known and the changes over the accounting period as well as those at the end of the accounting period are known, the capital account balances at various points of time (when changes take place) and the period for which the capital has been utilised is ascertained and interest is calculated thereon.
- *Closing balance known:* Where the Capital A/c balances at the end are known and no other information is available, or where the information relating to transactions affecting the capital account are known without the information

relating to the date/period of occurrence, we calculate the interest based on the closing balance.

Interest on Drawings

Interest on Drawings is to be charged:

- *Only when agreed upon:* Interest on drawings is to be charged to partners only if it is specifically agreed upon. If there is no mention in the partnership agreement regarding this, no interest need be charged.
- *@ 6% if rate is not mentioned:* Where the partnership deed provides for charging interest on drawings and it does not mention the rate of interest to be charged, it is a convention to charge interest @ 6% p.a.

Calculating Interest on Drawings: Interest is charged on drawings for the reason that the amount has been withdrawn by the partners without allowing it for being used for the purpose of the business. In the absence of appropriate information, it is a convention that the interest on drawings is calculated on the "Drawings A/c" balance at the end. In problem solving, we will come across these variations.

- *Closing balance known:* Where the Drawings A/c balances at the end of the accounting period are known and there is no information relating to the time of drawing, interest is calculated on the closing balance.
- *Amount and dates of drawings are known:* Drawings made during the period and the dates on which the drawings have been made are known. Since the period for which the withdrawn amounts are used is known, interest is calculated based on the amount drawn and the period of use.
- *Drawings made at regular intervals:* Where the Drawings are made at regular intervals, all the drawings are converted to an equivalent of drawings for a specified period and interest is calculated thereon.

Salary to Partners

Salary is to be paid to partners only if it is specifically agreed upon. If there is no mention in the partnership agreement, then no salary need be paid.

Commission to Partners

Commission is to be paid to partners only if it is specifically agreed upon. If there is no mention in the partnership agreement, then no commission need be paid.

Methods of Expressing Commission

Commissions may be calculated on a number of bases, as a % of Sales, as a % of Gross Profit, as a % of Net Profit, as a % of Purchases, etc., depending on the reason for which the commission is being paid and the agreement between the partners. There are two basic methods of expressing commission as a % of something else. Let us consider Commission being calculated as a % of Net Profit as an example.

1. Before Charging Such Commission

This is the normal calculation. Where there is no specific mention of the method, this is what we assume.

E.g.: "8% of Net Profits (` 1,25,000)".

⇒ "8% of Net Profits (` 1,25,000) before charging such commission".

Commission = ` 1,25,000 × 8%

= ` 10,000

2. After Charging Such Commission

Under this method, the commission is expressed as a certain % of something after charging such commission.

E.g.: "8% of Net Profits (` 1,25,000) after charging such commission".

8% after charging such commission

⇒ The commission should work out to 8% of the amount remaining after charging the commission to the net profit, i.e., reducing the commission from the net profit.

Finding Net Profit after Charging Commission (Without Knowing the Commission)

Let the commission be ` x (Using Net Profit = ` 1,25,000)

Net Profit after charging commission = Net Profit – Commission

= ` 1,25,000 – ` x

= ` (1,25,000 – x)

Therefore, Commission = 8% of Net Profits after charging such commission

⇒ Commission = Net Profit after Charging Commission × 8%

⇒ ` x = ` (1,25,000 – x) × $\frac{8}{100}$

⇒ ` x = ` (1,25,000 – x) × $\frac{2}{25}$

⇒ 25x = (1,25,000 – x) × 2

⇒ 25x = (1,25,000 × 2) – (2x)

⇒ 25x + 2x = 2,50,000

$\Rightarrow 27x = 2,50,000$

$$\Rightarrow x = \frac{2,50,000}{27}$$

$\Rightarrow x = 9,259.26$

Verify

Net Profit after charging such commission = ` 1,25,000 – ` 9,259.26

= ` 1,15,740.74

Commission = Net Profit after charging such commission × 8%

= 1,15,740.74 × 8%

= ` 9,259.26

Formula for Calculating Commission after Charging Such Commission

From the above calculations, we can derive a formula that would be easier to remember and use.

Commission = Net Profit after Charging Commission × 8%

$$\Rightarrow \text{\`}\ x = \text{\`}\ (1,25,000 - x) \times \frac{8}{100}$$

$$\Rightarrow 100x = (1,25,000 - x) \times 8$$

$$\Rightarrow 100x = (1,25,000 \times 8) - (8x)$$

$$\Rightarrow 100x + 8x = (1,25,000 \times 8)$$

$$\Rightarrow 108x = (1,25,000 \times 8)$$

$$\Rightarrow x = \frac{1,25,000 \times 8}{108}$$

$$\Rightarrow x = 1,25,000 \times \frac{8}{100+8}$$

$$\Rightarrow \text{Commission} = \text{Net Profit before Charging such Commission} \times \frac{\text{Commission}\%}{100 + \text{Commission}\%}$$

x% of Net Profit

- Before charging such commission = Net Profits before charging commission × x%
- After charging such commission = Net Profit before charging such commission × $\frac{x}{100+x}$

Example

25% of net profits

K Before charging such commission = Net Profits before charging such commission × 25%.

K After charging such commission = Net Profit before charging such commission × $\frac{25}{100+25}$.

Partner's Capital Accounts

The first difference we can notice, between accounting for sole proprietary form of business organisation and partnership form of business organisation is with regard to capital and its related aspects. In place of a single capital account, we see as many capital accounts as there are partners. In manual accounting and during the learning process, we prepare the partner's capital accounts in a columnar form instead of showing each ledger account separately, to enable easier understanding.

Fluctuating Capital Accounts

Interest on Capital, Salaries to Partners, Interest on Drawings, Commission to Partners, Partner's Share of Profits are all amounts that belong to the partners. By convention, we credit/debit all these amounts relating to partners to their capital accounts. This would result in the balance in the partners getting altered.

Since the capital account balances changes (fluctuates) with the regular transactions relating to capital, the Capitals accounts maintained under this method are known as "Fluctuating Capital Accounts".

By convention, this is the normal method adopted for maintaining capital accounts in problem solving, unless there is an instruction to the contrary.

Dr. **Partner's Capital Accounts** **Cr.**

Particulars	A (in `)	B (in `)	C (in `)	Particulars	A (in `)	B (in `)	C (in `)
To Int on Draw	1,000	100	750	By Bal b/d	2,00,000	75,000	1,00,000
To Drawings	20,000	2,000	15,000	By Int on Cap	10,000	3,750	5,000
To Bal c/d	2,82,700	1,94,350	2,34,950	By Salary		24,000	
				By Commission			52,000
				By Profit Share	93,700	93,700	93,700
	3,03,700	**1,96,450**	**2,50,700**		**3,03,700**	**1,96,450**	**2,50,700**
				By Bal b/d	2,82,700	1,94,350	2,34,950

Capital Accounts: Affected by Capital natured and Revenue natured transactions. Since all the transactions which affect the capital accounts are dealt with using the same capital account, we can say that Capital accounts are affected by transactions of both Capital Nature as well as Revenue Nature.

Fixed Capital Accounts

Why Another Type? Profits (revenue) increase capital. Capital also increases when additional capital is brought in by the partner. Under the fluctuating capital account system, the capital account gets affected by transactions of both capital and revenue nature. Thus, both these transactions are recorded using the same capital account.

If the organisation intends to obtain the information relating to the Capital account balance on account of Capital natured transactions and Revenue natured transactions separately, a separate Capital account needs to be maintained to record the revenue natured transactions.

The basic purpose of accounting is derivation of information. The more information we need, the more accounting heads we need to maintain.

Where there is a need for greater information in relation to capital, the total information is divided into two areas and separate ledger accounts are maintained in relation to each area. This gives information relating to long-term and short-term aspects separately.

The transactions relating to the partners are classified as capital and current natured. In recording the transactions which are of current nature, a separate account by name "__ (Partner's) Current A/c" is used instead of the "__ (Partner's) Capital A/c".

Any transaction that relates to the appropriation of profits, drawings, etc., is considered current natured and is recorded through the Current accounts.

Those transactions which relate to bringing in and taking out capital are considered capital natured and are recorded through the Capital accounts. Capital accounts have a fixed balance unless capital is either withdrawn or additional capital is contributed.

Since the capital account balance is more or less fixed, this method is called "Fixed Capital Method".

Drawings » Current/Capital: Regular drawings as agreed upon among partners are also treated to be transactions of current nature and are thus recorded through the current accounts. This is on the premise that, as the firm keeps making profits, the partners would be entitled to withdraw and use some of the profits for their necessities.

Where there is a specific instruction to treat drawings as capital, i.e., to be debited to the Capital accounts, it would have to be done accordingly.

The same information as shown in the capital accounts would appear as below if fixed capital accounts are maintained.

Dr. **Partner's Capital Accounts** **Cr.**

Particulars	A (in `)	B (in `)	C (in `)	Particulars	A (in `)	B (in `)	C (in `)
To Bal c/d	2,00,000	75,000	1,00,000	By Bal b/d	2,00,000	75,000	1,00,000
	2,00,000	**75,000**	**1,00,000**		**2,00,000**	**75,000**	**1,00,000**
				By Bal b/d	2,00,000	75,000	1,00,000

Dr. **Partner's Current Accounts** **Cr.**

Particulars	A (in `)	B (in `)	C (in `)	Particulars	A (in `)	B (in `)	C (in `)
To Bal b/d	–	–	–	By Bal b/d	–	–	–
To Int on Draw	1,000	100	750	By Int on Cap	10,000	3,750	5,000
To Drawings	20,000	2,000	15,000	By Salary		24,000	
To Bal c/d	1,82,700	1,19,350	1,34,950	By Commission			52,000
				By Profit Share	93,700	93,700	93,700
	1,03,700	**1,21,450**	**1,50,700**		**1,03,700**	**1,21,450**	**1,50,700**
				By Bal b/d	82,700	1,19,350	1,34,950

Calculation of Interest on Capital

The capital account balance considered for calculation of interest on capital is dependent on the method adopted for maintaining the capital accounts.

- *Fixed Capital Accounts:* Where the Capital Accounts are being maintained under "Fixed Capital Accounts" method, interest on capital is to be paid on the balances in the capital accounts. Interest on Current account balances is not considered unless there is a specific instruction regarding the same.
- *Fluctuating Capital Accounts:* Where the Capital Accounts are being maintained under "Fluctuating Capital Accounts" method, interest on capital is to be paid on the balances in the capital accounts as that is the only account that is related to capital.

Solved Problems

Illustration1: From the following Trial balance of Ajit and Sujit, you are required to prepare a Trading and Profit and Loss A/c for the year ended 31st December and Balance Sheet as on that date:

Trial Balance as on 31st December, 2003

Particulars	Amt	Amt	Particulars	Amt	Amt
Capitals:			Carriage	2,800	
Ajit		1,20,000	Wages	48,000	
Sujit		80,000	Insurance	3,200	
Drawings:			Discount Received		400
Ajit	4,000		Postage	1,600	
Sujit	2,000		Debtors and Creditors	1,40,800	1,28,400
Stock on 1-1-2003	88,000		Furniture	48,000	
Bills Receivable	3,600		Cash in Hand	19,600	
Purchase and Sales	3,80,000	6,04,000	Machinery	1,60,000	
Return	12,000	4,000	Rent & Taxes	2,400	
Salaries	20,000		Printing & Stationery	800	

Adjustment:

(i) The closing stock on 31st December, 2003 was valued at ` 1,12,000.

(ii) The outstanding expenses wages 4,000, Salaries ` 1,860.

(iii) Goods of ` 4,000 was distributed as free samples.

(iv) Interest on partners capital was to be provided at 7% p.a.

(v) Prepaid insurance was ` 200.

(vi) Depreciation was to be provided on furniture at 10% and on machinery 5%.

(vii) A reserves for doubtful debts was to be created at 5% of sundry debtors.

Solution:

Dr. **Trading Account for the year ended 31-12-2003** **Cr.**

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		88,000	By Sales	6,04,000	
To Purchase	3,80,000		*Less:* Returns	12,000	5,92,000
Less: Returns	4,000	3,76,000	By Goods given as Samples		4,000
To Wages	48,000		By Closing Stock		1,12,000
Add: O/s Wages	4,000	52,000			
To Gross Profit		1,92,000			
		7,08,000			**7,08,000**

Dr. Profit and Loss Account for year ended 31-12-2003 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Salaries	20,000		By Gross Profit		1,92,000
Add: O/s Salaries	1,860	21,860	By Discount Received		400
To Insurance	3,200				
Less: Prepaid Insurance	200	3,000			
To Postage		1,600			
To Rent & Taxes		2,400			
To Printing & Stationery		800			
To Carriage Outwards		2,800			
To Free samples given		4,000			
To Reserves for Doubtful Debts		7,040			
To Depreciation					
Machinery	8,000				
Furniture	4,800	12,800			
To Net Profit		1,36,100			
		1,92,400			**1,92,400**

Dr. Partner's Capital Account Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Interest:			By Net Profit		1,36,100
Ajit	8,400				
Sujit	5,600				
To Net Profit Transferred:					
Ajit	68,050				
Sujit	68,050				
		1,36,100			**1,36,100**

Balance Sheet as on 31-12-2003

Liabilities	Amt	Amt	Assets	Amt	Amt
Capital Account of Ajit			Machinery	1,60,000	
Balance b/d	1,20,000		*Less:* Depreciation	8,000	1,52,000
Add: Interest	8,400		Furniture	48,000	
Add: Net Profit	68,050		*Less:* Depreciation	4,800	43,200
Less: Drawings	4,000	1,92,450	Prepaid Insurance		200
Capital Account of Sujit			Stock		1,12,000
Balance b/d	80,000		Debtors	1,40,800	
Add: Interest	5,600		*Less:* Reserves for D.D	7,040	1,33,760
Add: Net Profit	68,050		Bills Receivable		3,600
Less: Drawings	2,000	1,51,650	Cash in Hand		19,600
Sundry Creditors		1,28,400			
Outstanding Expenses					
Wages	4,000				
Salaries	1,860	5,860			
		4,78,360			**4,64,360**

Illustration 2: A, B and C carried on business in partnership as ready-made cloth dealers. The partnership agreement provided that:

(i) The partners were to be credited at the end of each year with interest at 5% per annum on opening balance of capital.

(ii) No interest was to be charged on drawings.

(iii) Profits and losses were to be shared as to A 5, B 3 and C 2. It was agreed that C's share of profit in any year should not be less than 10,000 and any deficiency in such share was to be borne by the other two partners in their profit sharing ratio.

Particulars	Amt	Amt
Shop fittings (at cost)	30,000	
Freehold Premises	60,000	
Leasehold Premises Purchased During the Year	45,000	
Additions and Alterations to Leasehold Premises	25,000	
Purchases	2,80,000	

Stock on 1-1-2003	42,000	
Salaries and Wages	64,000	
Office and Trade Expenses	45,200	
Rent, Rates and Taxes	10,500	
Professional Charges	3,500	
Debtors	20,600	
Balance at Central Bank Ltd.	43,700	
Partner's Capital Account:		
A		80,000
B		50,000
C		30,000
Partner's Current Account:		
A		16,000
B		8,000
C		12,000
Sales		4,45,000
Trade Creditors		37,000
Depreciation Reseves		14,000
Reserves for Doubtful Debts		500
Drawings other than Monthly Payment:		
A	7,000	
B	6,000	
C	4,000	
	6,92,500	**6,92,500**

You are required to prepare Trading A/c, Profit & Loss A/c, Profit & Loss Appropriation A/c for the year ended 31.12.2003 and balance sheet as on that date.

Solution:

Dr. **Trading Account for year ended 31-12-2003** **Cr.**

Particulars	Amt	Particulars	Amt
To Opening Stock	42,000	By Sales	4,45,000
To Purchase	2,80,000	By Goods Destroyed by Fire	1,000
To Gross Profit c/d	1,60,000	By Goods taken by Partners	1,000
		By Closing Stock	35,000
	4,82,000		**4,82,000**

Dr. **Profit and Loss Account for year ended 31-12-2003** **Cr.**

Particulars	Amt	Amt	Particulars	Amt
To Salaries & Wages		64,000	By Gross Profit b/d	1,60,000
Less: Salaries to Partners	12,600	5,14,000		
To Office & Trade Expenses	45,200			
Add: O/s	2,100	47,300		
To Rent, Rates & Insurance	10,500			
Less: Prepaid Rates	2,500	8,000		
To Professional Charges	3,500			
Less: Exp. on Acquisition of Freehold Premises	2,500	1,000		
To Bad Debts	600			
Add: BDR (new)	1,000			
Less: BDR (old)	500	1,100		
To Depreciation				
Leasehold Premises	2,900			
Shop Fitting	1,800	4,700		
To Goods Destroyed by Fire		300		
To Net profit		46,200		
		1,60,000		**1,60,000**

Dr. **Profit and Loss Appropriation Account** **Cr.**

Particulars	Amt	Particulars	Amt
Interest on Partner's Capital	8,000	By Net Profit	46,200
To Net Profit Transferred to Curr. A/c:			
A	17,625		
B	10,575		
C	10,000		
	46,200		**46,200**

Balance Sheet as on 31-12-2003

Liabilities	Amt	Amt	Assets	Amt	Amt
Capital Account:			Fixed Assest		
A	80,000		Shop Fitting (at cost)	36,000	
B	50,000		*Less:* Dep. upto Curr Year	15,800	20,200
C	30,000	1,60,000	Freehold Premises	45,000	
Current Account:			*Add:* Addition During Year	25,000	
A	24,025		*Add:* Exp on Acquisition	2,500	
B	11,075		*Less:* Dep. Debtors	2,900	
C	16,500	51,600	*Less*: Bad Debts	600	
Trade Creditors		37,000	*Less:* Provision for Bad Debts	1,000	19,000
O/s Office & Trade Expenses		2,100	Bal. at Central Bank Ltd.		43,700
			Insurance Claim Receviable		700
			Prepaid Rates		2,500
			Closing Stock		35,000
		2,50,700			**2,50,700**

Illustration 3: R and K are partners sharing profit equally from the trial balance. Prepare trading and Profit & Loss A/c for the year ended 31st December, 2003 and balance sheet as on that date.

Particulars	Amt	Amt	Particulars	Amt	Amt
R's Capital		1,00,000	Rent and Taxes	2,000	
K's Capital		1,00,000	Motor Car	3,000	
Land and Building	87,000		Carriage Outward	1,400	
Plant and Machinery	17,500		Sales		84,000
Goodwill	20,000		Salaries	3,100	
R's Drawings	10,000		Bank Charges	105	
K's Drawings	12,600		Bad Debts Written Off	2,100	
Deposits	1,000		Provision for Doubtful Debts		1,500
Stock (1-1-2003)	27,000		Printing & Stationery	2,000	

Wages	10,000		Debtors	19,800	
Purchase	69,000		Creditors		7,500
Carriage Inward	600		Bank Current A/c	795	
General Expenses	4,000				

Solution:

Dr. Trading and Profit and Loss Account for year ended 31-12-2003 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		27,000	By Sales	84,000	
To Purchase	69,000		*Add:* Unrecorded Sales	200	
Less: Machinery	1,000	68,000		84,200	
To Wages	10,000		*Less:* Motor Car Sold	2,000	82,200
Less: For Machinery	500	9,500	By Stock Destroyed by Fire		3,000
To Carriage Inward		600	By Closing Stock		46,000
To Gross Profit c/d		26,100			
		1,31,200			**1,31,200**
To General Expenses		4,000	By Gross Profit c/d		26,100
To Rent & Taxes	2,000				
Less: Prepaid	800	1,200			
To Carriage Inward		1,400			
To Salaries		3,100			
To Bank Charges		105			
To Printing & Stationery		2,000			
To Loss on Sale of Motor Car		700			
To Bad Debts	2,100				
Add: New Prov.	2,000				
Less: Old Prov.	1,500	2,600			
To Loss by Fire		3,000			
To Depreciation:					
Plant & Machinery	1,575				
Motor Car	300	1,875			
To Net Profit					
R		3,060			
K		3,060			
		26,100			**26,100**

Balance Sheet as on 31-12-2003

Liabilities	Amt	Amt	Assets	Amt	Amt
Capital Account of R			Goodwill		20,000
Balance b/d	1,00,000		Land & Building		87,000
Add: Profit Transferred	3,060		Plant & Machinery	17,500	
	1,03,060		*Add:* Purchases	1,000	
Less: Drawings	10,000	93,060	Installation Charges	500	
Capital Account of K				19,000	
Balance b/d	1,00,000		*Less:* Depreciation	1,575	17,425
Add: Profit Transferred	3,060		Debtors	19,800	
	1,03,060		*Add:* Unrecorded Sales	200	
Less: Drawings	12,600	90,460		20,000	
Sundry Creditors		7,500	*Less:* Prov. for Bad Debts	2,000	18,000
			Closing Stock		46,000
			Deposits		1,000
			Bank Current A/c		795
			Prepaid Rent & Taxes		800
		1,91,020			**1,91,020**

Illustration 4: Sujata, Sarita and Suman are partners sharing profit and losses in the ratio 3 : 2 : 1 Suman is guaranteed a profit of ` 16,000 p.a. as her minimum share. Any deficiency, will be borne by the other partners in their profit sharing ratio. Interest at the rate of 6% is to be allowed on partner's fixed capital account. On 31st March, 2004, trial balance was as under:

Debit	Amt	Credit	Amt
Building	64,000	Fixed Capital Accounts:	
Machinery	50,000	Sujata	80,000
Vehicles	20,000	Sarita	60,000
Purchases	2,90,000	Suman	40,000
Stock	68,000	Current Account:	
Wages	65,000	Sujata	16,000
Trade Expenses	25,000	Sarita	9,000
Salaries	30,000	Sales	6,72,000
Repairs	28,000	Creditors	48,000
Commission	2,500	Provision for Doubtful Debts	3,000

Office Expenses	33,200	Commission	4,000
Rates & Taxes	22,900	Discount	6,400
Bank Balance	1,42,400		
Debtors	84,000		
Suman's Current A/c	13,400		
	9,38,400		**9,38,400**

Additional Information

(i) Closing stock was valued at ₹ 70,000.

(ii) Sujata has taken goods worth ₹ 3,000 from stock for which no entry is made in the books.

(iii) Sarita is to be paid ₹ 24,000 for travelling expenses for business trips.

(iv) Wages outstanding are ₹ 5,000 and commission received in advance ₹ 1,000.

(v) Depreciation on machinery and building is to be provided @ 10% p.a. and on vehicles @ 15% p.a.

(vi) Provision for doubtful debts is to be increased to ₹ 6,000.

(vii) Goods worth ₹ 10,000 were destroyed by fire, the same were not insured.

Prepare Trading and Profit & Loss A/c, Profit & Loss Appropriation A/c, Partner's Current A/c for the year ended 31.3.2004 and Balance Sheet as on that date.

Solution:

Dr. Trading and Profit and Loss Account for the year ended 31.3.2004 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		68,000	By Sales		6,72,000
To Purchase		2,90,000	By Goods Withdrawn (Sujata)		3,000
To Wages	65,000		By Goods Destroyed		10,000
Add: Outstanding	5,000	70,000	By Closing Stock		70,000
To Gross Profit c/d		3,27,000			
		7,55,000			**7,55,000**
To Trade Expenses		25,000	By Gross Profit		3,27,000
To Salaries		30,000	By Commission	4,000	
To Repairs		28,000	*Less:* Received in Advance	1,000	3,000
To Commission		2,500	By Discount		6,400

To Office Expenses		33,200			
To Rates and Taxes		22,900			
To Travelling Exp. (Sarita)		24,000			
To Provision for D.D	6,000				
Less: Old Provision	3,000	3,000			
To Depreciation:					
Building	6,400				
Machinery	5,000				
Vehicle	3,000	14,400			
To Loss Due to Goods Destroyed		10,000			
To Net profit		1,43,400			
		3,36,400			**3,36,400**

Dr. Profit and Loss Appropriation Account for the year ended 31.3.2004 Cr.

To Interest on Capital:		By Net Profit	1,43,400
Sujata	4,800		
Sarita	3,600		
Suman	2,400		
To Partner's Current A/c:			
Sujata	66,300		
Sarita	44,200		
Suman	22,100		
	1,43,400		**1,43,400**

Dr. Partner's Current Account Cr.

Particulars	Sujata	Sarita	Suman	Particulars	Sujata	Sarita	Suman
To Balance b/d			13,400	By Balance b/d	16,000	9,000	
To Goods w/d	3,000			By Travelling		24,000	
To Balance c/d	84,100	80,800	11,100	By Interest	4,800	3,600	2,400
				By Net Profit	66,300	44,200	22,100
	87,100	**80,800**	**24,500**		**87,100**	**80,800**	**24,500**

Balance Sheet as on 31-3-2004

Particulars	Amt	Amt	Particulars	Amt	Amt
Partner's Capital:			Building	64,000	
Sujata	80,000		*Less:* Dep @ 10%	6,400	57,600
Sarita	60,000		Machinery	50,000	
Suman	40,000	1,80,000	*Less:* Dep @ 10%	5,000	45,000
Partner's Current:			Vehicles	20,000	
Sujata	84,100		*Less:* Dep @ 15%	3,000	17,000
Sarita	80,800		Bank		1,42,400
Suman	11,100	1,76,000	Debtors	84,000	
Creditors		48,000	*Less:* Provision of D.D	6,000	78,000
Outstanding Wages		5,000	Stock		70,000
Commission in Advance		1,000			
		4,10,000			**4,10,000**

Illustration 5: Ram and Shyam are partners. Their Trial Balance as on 31-3-2004 was as follows:

Debit	Amt	Credit	Amt
Building	74,000	Ram's Capital	90,000
Machinry	40,000	Shyam's Capital	90,000
Furniture	20,000	Sales	6,80,000
Purchases	2,98,000	Creditors	52,000
Stock	60,000	R.D.D.	3,000
Wages	65,000	Discount	10,000
Carriage Inward	25,000		
Salaries	40,000		
Repairs	18,000		
Commission	5,700		
General Expenses	30,000		
Rent and Taxes	21,000		
Bank Balance	95,000		
Cash Balance	49,300		
Debtors	84,000		
	9,25,000		**9,25,000**

Additional Information:

(i) Closing stock was ` 50,000.

(ii) Shyam has taken goods worth ` 5,000 for his personal use for which no entry was made in the books.

(iii) Wages outstanding were ` 6,000 and taxes paid in advance ` 2,000.

(iv) Depreciation was to be provided at 10% on machinery, 5% on building and 15% on furniture.

(v) Write off ` 2,000 as bad debts and provision for doubtful debts is to be increased to ` 5,000.

(vi) Goods costing ` 2,500 have been stolen but no entry was passed in the books for the same.

You are required to prepare Trading and Profit and Loss Account for the year ended 31.3.2004 and Balance Sheet as on that date.

Solution:

Dr. Trading and Profit and Loss Account for the year ended 31.3.2004 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		60,000	By Ssales		6,80,000
To Purchase		2,98,000	By Closing Stock		50,000
To Wages	65,000		By Goods taken — Shyam		5,000
Add: O/s	6,000	71,000	By Goods Stolen		2,500
To Carriage Inward		25,000			
To Gross Profit		2,83,500			
		7,37,500			**7,37,500**
To Salaries		40,000	By Gross Profit b/d		2,83,500
To Repairs		18,000	By Discount		10,000
To Commission		5,700			
To General Expenses		30,000			
To Rent & Taxes	21,000				
Less: Prepaid	2,000	19,000			
To Depreciation:					
Building	3,700				
Machinery	4,000				
Furniture	3,000	10,700			

To Bad Debts	2,000				
Add: New R.D.D.	5,000	7,000			
Less: Old R.D.D.	3,000	4,000			
To Loss by theft		2,500			
To Net Profit Tfd					
Ram's Capital A/c	81,800				
Shyam's Capital A/c	81,800	1,63,600			
		2,93,500			**2,93,500**

Balance Sheet as on 31st March, 2004

Liabilities	Amt	Amt	Assets	Amt	Amt
Capital Account			Building	74,000	
Ram's Capital	90,000		*Less*: Depreciation	3,700	70,300
Add: Profit	81,800	1,71,800	Machinery	40,000	
Shyam's Capital	90,000		*Less:* Depreciation	4,000	36,000
Less: Goods taken	5,000		Furniture	20,000	
Add: Profit	81,800	1,66,800	*Less:* Depreciation	3,000	17,000
Creditors		52,000	Debtors	84,000	
Outstanding Wages		6,000	*Less:* Bad Debts	2,000	
				82,000	
			Less: R.D.D.	5,000	77,000
			Closing Stock		50,000
			Prepaid Taxes		2,000
			Bank Balance		95,000
			Cash Balance		49,300
		3,96,600			**3,96,600**

Illustration 6: Ram and Kirti were in partnership in a retail business sharing profits in proportion of 3 : 2 as from 1st January, 2005. They admitted Vikram into partnership giving him one-fifth of the profits. Vikram brought in ` 20,000 in cash of which ` 6,000 were considered as being in payment for his share of goodwill and remainder as his capital.

Particulars	Debit	Credit
Purchases & Sales	1,71,625	2,62,650
Returns	5,250	4,125
Customers & Creditors	40,200	25,525
Bills Receivable & Bills Payable	20,070	11,950
Carriage Inward	15,000	
Carriage Outward	2,175	
Stock (1-1-2005)	39,725	
Reserve for Doubtful Debts		5,200
Outstanding Carriage Inward		1,200
Bad Debts	400	
Salaries	9,795	
Furniture	5,000	
Shop	15,500	
Postage & Insurance	3,240	
Trade Expenses	2,690	
Rent, Rates & Taxes	4,200	
Loan to Vishnu (from 1-8-2005)	6,000	
Prepaid Insurance	240	
Rent Accured but not Paid		900
Cash in Hand	4,440	
Current Account:		
Ram	5,000	
Kirti	4,000	
Vikram	2,000	
Capital Account:		
Ram		15,000
Kirti		10,000
Cash paid by Vikram		20,000
Computer	30,000	
Professional Charges	4,450	
Loan from ICICI Bank		34,450
	3,91,000	**3,91,000**

Adjustment:

- Stock at the end was ` 20,000.
- Depreciation on computer and Furniture is to be charged at 10% p.a.
- One-fifth of the shop are to be written off.
- Goods worth ` 800 have been destroyed by fire and the insurance company has admitted the claim for ` 600 only.
- Bills receivable include a dishonoured bill for ` 1,100 of ` 1,000 due from Customer A/c of sales, who has become insolvent.
- Reserves for Doubtful Debts is to be maintained at 5% on Debtors.

You are required to prepare Trading and Profit and Loss Account for the year ended 31.12.2005 and Balance Sheet as on that date.

Solution:

Dr. Trading and Profit and Loss Account for the year ended 31.12.2005 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock	39,725		By Sales	2,62,650	
To Purchase	1,71,625		*Less:* Returns	5,250	2,57,400
Less: Returns	4,125	1,67,500	By Loss by Fire		800
To Carriage Inward		15,000	By Closing Stock		20,000
To Gross Profit		55,975			
		2,78,200			**2,78,200**
To Carriage Outward		2,175	By Gross Profit b/d		55,975
To Salaries		9,795	By R.D.D.		1,800
To Postage & Insurance		3,240			
To Trade Expenses		2,690			
To Rent, Rate & Taxes		4,200			
To Professional Charges		4,450			
To Shop Written Off (1/5)		3,100			
To Goods Lost by Fire		200			
To Depreciation on					
Furniture	500				
Computer	3,000	3,500			

To Net Profit Transferred					
Ram's Current A/c	11,724				
Kirti's Current A/c	7,816				
Vikram's Current A/c	4,885	24,425			
		57,775			**57,775**

Balance Sheet as on 31-12-2005

Liabilities	**Amt**	**Amt**	**Assets**	**Amt**	**Amt**
Capital A/c:			Furniture	5,000	
Ram	15,000		*Less:* Depreciation	500	4,500
Kirti	10,000		Shop	15,500	
Vikram	14,000	39,000	*Less:* W/o	3,100	12,400
Current A/c:			Computer	30,000	
Ram	10,324		*Less:* Depreciation	3,000	27,000
Kirti	5,916		Closing Stock		20,000
Vikram	2,885	19,125	Debtors	40,200	
Loan from ICICI Bank		34,450	*Add:* B/R Dishonoured	1,100	
Creditors		25,525	*Less:* Kirti (Drawings)	300	
Bills Payable		11,950	*Less:* Bad Debts	1,000	
O/s Carriage Inward		1,200	*Less:* R.D.D.	2,000	38,000
Rent Accured but not Paid		900	Loan to Vishnu		6,000
			Prepaid Insurance		240
			Insurance Claim		600
			Cash in Hand		4,440
			Bills Receivable	20,270	
			Less: Dishonoured	1,100	18,970
		1,32,150			**1,32,150**

Dr. **Current Account** **Cr.**

Particulars	**Ram**	**Kirti**	**Vikram**	**Pariculars**	**Ram**	**kirti**	**Vikram**
To Balance b/d	5,000	4,000	2,000	By P & L A/c	11,724	7,816	4,885
To Debtors		300		By Goodwill	3,600	2,400	
To Balance c/d	10,324	5,916	2,885				
	15,324	**10,216**	**4,885**		**15,324**	**10,216**	**4,885**

Illustration 7: Jaya and Bhaduri were partnership were sharing profit in the ratio of 3 : 2 from 1st January, 2003. They admitted Amit into partnership giving him 1/6th share in profit. He brought ` 10,000 cash, of which ` 3,000 was considered as being in payment for his share of goodwill and the balance as his capital.

Particulars	Amt	Particulars	Amt
Drawings:		Rent Payable	928
Jaya	4,000	Outstanding Wages	2,719
Bhaduri	3,500	Sales	2,63,150
Amit	2,500	Return Outward	3,120
Purchases	1,66,405	Reserve for Doubtful Debts	1,200
Returns Inward	4,250	Creditors	30,106
Debtors	40,200	Bill Payable	8,950
Opening Stock	27,225	Dividend	825
Wages	20,137	Capital:	
Salaries	8,753	Jaya	14,500
Building	6,750	Bhaduri	8,300
Addition to Building	500	Cash Paid by Amit (1-4-2003)	10,000
Patents	7,300		
Postage/Telegram	3,226		
Power/Fuel	1,850		
General Expenses	3,314		
Rent, Rates and Taxes	3,517		
Bad Debts	525		
Loan to 'P' at 6% p.a. (1-9-03)	5,000		
Investment	11,500		
Prepaid Expenses	524		
Cash/Bank	5,752		
Bills Receivable	17,070		
	3,43,798		**3,43,798**

Adjustment:

(i) Closing stock was valued at ` 15,760.

(ii) Goods costing ` 1,000 have been stolen but not entered in the books.

(iii) Write off 1/5th of patents.

(iv) Bills Receivable include dishonoured bill of ` 1,050.

(iv) Maintain reserves for doubtful debts @ 5%.

(v) Depreciate building @ 10% p.a.

(vi) Necessary adjustment in connection with admission is to be made through current accounts of the partners.

(vii) Goodwill should not appear in the books.

Prepare Trading and Profit and Loss Account for the year ended 31.12.2003 and Balance Sheet as on that date.

Solution:

Dr. Trading and Profit and Loss Account for the year ended 31-12-2003 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		27,225	By Sales	2,63,150	
To Purchase	1,66,405		*Less:* Returns	4,250	2,58,900
Less: Returns	3,120	1,63,285	By Goods Stolen		1,000
To Wages		20,137	By Closing Stock		15,760
To Power & Fuel		1,850			
To Gross Profit		63,163			
		2,75,660			**2,75,660**
To Salaries		8,753	By Gross Profit		63,163
To Loss on Goods Stolen		1,000	By Dividend		825
To Bad Debts	525		By Interest Due on Loan P (5,000*6% *4/12)		100
Add: New R.D.D.	2,063				
Less: Old R.D.D.	-1,200	1,388			
To Depreciation on Building		700			
To Depreciation on Patents		1,460			
To Postage/Telegram		3,226			
To General Expenses		3,314			
To Rent, Rates & Taxes		3,517			
To Net Profit:					
Jaya	20,635				
Bhaduri	13,577				
Amit	6,788	40,730			
		64,088			**64,088**

Balance Sheet as on 31-12-2003

Liabilities	Amt	Amt	Assets	Amt	Amt
Partner's Capital:			Building	6,750	
Jaya	14,500		*Add:* Purchased 1-7-03	500	
Bhaduri	8,300		*Less:* Dep (675 + 25)	700	6,550
Amit	7,000	29,800	Patents	7,300	
Partner's Current:			*Less:* Dep (1/5)	1,460	5,840
Jaya	18,165		Loan to P	5,000	
Bhaduri	11,277		*Add:* Interest Due	100	5,100
Amit	4,288	33,730	Investment		11,500
Creditors		30,106	Debtors	40,200	
Bills Payable		8,950	*Add:* Bills Dishonoured	1,050	
Rent Payable		928		41,250	
Outstanding Wages		2,719	*Less:* New R.D.D. @ 5%	2,063	39,187
			Prepaid Insurance		524
			Cash/Bank		5,752
			Stock		15,760
			Bills Receivable	17,070	
			Less: Dishonoured	1,050	16,020
		1,06,233			**1,06,233**

Dr. Partner's Current Account Cr.

Particulars	Jaya	Bhaduri	Amit	Particulars	Jaya	Bhaduri	Amit
To Drawings	4,000	3,500	2,500	By Amit 's Capital A/c	1,800	1,200	
To Balance b/d	18,165	11,277	4,288	By Net profit	20,365	13,577	6,788
	22,165	**14,777**	**6,788**		**22,165**	**14,777**	**6,788**

Illustration 8: The following is the trial balance of firm as on 31st December, 2005:

Particulars	Amt	Particulars	Amt
Cash	29,700	Creditors	40,500
Debtors	93,000	Sales	5,40,000
Rent & Taxes	17,700	Capital:	
Salary	36,000	D	72,000
Sundry Expenses	15,600	E	36,000

Stock	75,000	F (Including Goodwill)	12,000
Purchases	3,30,000		
Sundry Assets	31,500		
Drawing:			
D	45,000		
E	22,500		
F	4,500		
	7,00,500		**7,00,500**

Adjustments:

(i) D and E were partners sharing profits and losses equally.

(ii) Mr. F was admitted to the partnership on 1st July, 2005.

(iii) On 31st December, 2005, stock was valued at ` 70,500.

(iv) Rent and taxes paid in advance ` 700.

(v) Sundry expenses were outstanding ` 400.

(vi) Depreciate Sundry Assets by 20% p.a.

(vii) Goodwill of the firm was valued at ` 6,000 on 1st July, 2005 and not to appear in the balance sheet.

(viii) Interest on capital to be charged at the rate of 10% p.a.

Prepare Trading Account, Profit and Loss Account and Profit & Loss Appropriation A/c for the year ended 31.12.2005 and Balance Sheet as on that date.

Solution:

Dr. Trading, Profit and Loss Account Appropriation for the year ended 31-12-2005 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		75,000	By Sales		5,40,000
To Purchase		3,30,000	By Closing Stock		70,500
To Gross profit		2,05,500			
		6,10,500			**6,10,500**

Particulars	Jan-Jun	Jul-Dec	Particulars	Jan-Jun	Jul-Dec
To Salaries	18,000	18,000	By Gross Profit b/d	1,02,750	1,02,750
To Rent & Rates	17,700	17,700			
Less: Prepaid	700	700			
To Sundry Expenses	15,600	15,600			
Add: Outstanding	400	400			
To Depreciation on Assets	3,150	3,150			
To Net Profit	65,100	65,100			
	1,02,750	**1,02,750**		**1,02,750**	**1,02,750**
To Interest on Capital:			By Net Profit	65,100	65,100
D	3,600	3,600			
E	1,800	1,800			
F		500			
To Net Profit Transferred:					
D	29,850	19,733			
E	29,850	19,733			
F		19,734			
	65,100	**65,100**		**65,100**	**65,100**

Balance Sheet as on 31-12-2005

Liabilities	Amt	Amt	Assets	Amt	Amt
Capitals:			Sundry Assets	31,500	
D	84,783		*Less:* Depreciation	6,300	25,200
E	67,683		Closing Stock		70,500
F	25,734	1,78,200	Sundry Debtors		93,000
Sundry Creditors		40,500	Prepaid Rent & Rates		700
Outstanding Expenses		400	Cash		29,700
		2,19,100			**2,19,100**

Dr. **Partner's Capital Account** Cr.

Particulars	D	E	F	Particulars	D	E	F
To Drawings	45,000	22,500	4,500	By Balance b/d	72,000	36,000	12,000
To Goodwill	2,000	2,000	2,000	By Goodwill	3,000	3,000	
To Balance c/d	84,783	67,683	25,734	By Int on Capital	7,200	3,600	500
				By Net Profit	29,850	29,850	
				By Net Profit	19,733	19,733	19,734
	1,31,783	**92,183**	**32,234**		**1,31,783**	**92,183**	**32,234**

Illustration 9: X and Y were partners sharing profit and loss as 3 : 2. On 1-7-2003, M, manager, joins for 1/4th share. M was getting a salary of ` 500 p.m. After his admission, his salary is borne by Y personally. M's share is guaranteed at ` 9,000 p.a. by X. He paid ` 2,000 Goodwill and ` 5,000 capital and the entire amount was credited to his Suspense Account.

Particulars	Amt	Amt
X's Capital	6,000	31,000
Y's Capital	5,000	21,000
M's Suspense Account		7,000
Closing stock	18,000	
Furniture	2,000	
Machinery: Opening	20,000	
Acquired on 30-9-2003	4,000	
Salaries (Including M's Salary)	13,000	
Rent, Rates & Taxes	3,000	
Postage & Telephone	1,000	
Printing & Stationery	2,000	
Travelling & Conveyance	3,000	
Debtors & Creditors	38,000	11,000
Cash & Bank	5,000	
Gross Profit		50,000
	1,20,000	**1,20,000**

Provide depreciation at 10% p.a on Furniture & Machinery

You are Required to Prepare Final Accounts for the year ended 31.12.2003 and Balance Sheet as on that date.

Solution:

Dr. Profit and Loss Account for the year ended 31-12-2003 Cr.

Particulars	Jan-June	July-Dec	Particulars	Jan-June	July-Dec
To Salaries: Total	3,500	3,500	By Gross Profit	25,000	25,000
To Managers Salary	3,000				
To Rent, Rates & Taxes	1,500	1,500			
To Postage & Telephone	500	500			
To Printing & Stationery	1,000	1,000			
To Travelling & Conveyance	1,500	1,500			
To Depreciation					
Furniture	100	100			
Machinery	1,000	1,000			
New		100			
To Net Profit	12,900	15,800			
	25,000	**25,000**		**25,000**	**25,000**

Dr. Profit and LossAppropriation Account for the year ended 31-12-2003 Cr.

Particulars	Jan-June	July-Dec	Particulars	Jan-June	July-Dec
To Net Profit (upto 30-6)			By Net Profit	12,900	15,800
X	7,740				
Y	5,160				
To Net Profit (upto 1-7)					
X		6,560			
Y		4,740			
M		4,500			
	12,900	**15,800**		**12,900**	**15,800**

Balance Sheet as on 31-12-2003

Liabilities	Amt	Amt	Assets	Amt	Amt
Capital Account:			Furniture	2,000	
X		40,500	*Less:* Depreciation	200	1,800
Y		23,700	Machinery	24,000	
M		9,500	*Less:* Depreciation	2,100	21,900

Creditors		11,000	Closing Stock		18,000
			Debtors		38,000
			Cash and Bank		5,000
		84,700			**84,700**

Dr. **Partner's Capital Account** **Cr.**

Particulars	X	Y	M	Particulars	X	Y	M
To Balance b/d	6,000	5,000		By Balance b/d	31,000	21,000	
To Salary		3,000		By Goodwill	1,200	800	
To Balance c/d	40,500	23,700	9,500	By Capital from Suspense A/c			5,000
				By N.P upto 30-6	7,740	5,160	
				By N.P upto 1-7	6,560	4,740	4,500
	46,500	**31,700**	**9,500**		**46,500**	**31,700**	**9,500**

Illustration 10: Retirement during Accounting Year.

The following is the Trial Balance of a firm as on 31-12-2004:

Particulars	Amt	Particulars	Amt
Purchases	1,56,000	Capital Account:	
Return Inward	2,400	A	30,000
Stock	24,000	B	30,000
Drawings:		C	30,000
A	12,000	Sales	2,94,000
B	12,000	Return Outward	2,000
C	12,000	R.D.D.	8,800
Salary	27,000	Bank Loan	20,000
Office Expenses	16,500	Creditors	76,500
Bad Debts	2,100	Bills Payable	8,700
Carriage Inward	4,500		
Carriage Outward	6,750		
Debtors	1,00,000		
Bills Receivable	3,250		
Bank Balance	8,000		
Cash Balance	2,500		

Investment	25,000		
Premises	50,000		
Machinery	36,000		
	5,00,000		**5,00,000**

On 1st July, 2004, 'A' retired and the following adjustments were agreed upon:

(i) Goodwill of ` 90,000 was bought into the books of account.

(ii) Furniture worth ` 20,000 was purchased on 31-3-2004 but the invoice was not recorded in the books.

(iii) Balance in A's account after making all adjustments was to be transferred to his Loan A/c carrying interest @ 16%.

(iv) Closing stock was valued at ` 42,000.

(v) Provide depreciation on machinery by 10%, premises by 5% and furniture by 5%.

(vi) Provide interest on capital at 10%.

You are required to Prepare Trading and Profit & Loss Account, Partner's Capital Account & Balance Sheet as on that date.

Solution:

Dr. Trading Account for the year ended 31-12-2004 Cr.

Particulars	Amt	Amt	Particulars	Amt	Amt
To Opening Stock		24,000	By Sales	2,94,000	
To Purchase	1,56,000		*Less:* Return Inward	2,400	2,91,600
Less: Returns	2,000	1,54,000	By Closing Stock		42,000
To Carriage Inward		4,500			
To Gross Profit		1,51,100			
		3,33,600			**3,33,600**

Dr. Profit and Loss Account for the year ended 31-12-2004 Cr.

Particulars	Jan-June	July-Dec	Particulars	Jan-June	July-Dec
To Salary	13,500	13,500	By Gross Profit	75,550	75,550
To Office Expenses	8,250	8,250			
To Bad Debts	1,050	1,050			
To Carriage Inward	3,375	3,375			

To Depreciation:					
Machinery	1,800	1,800			
Premises	1,250	1,250			
Furniture	250	500			
To Interest on Loan		5,069			
To Net Profit	46,075	40,756			
	75,550	**75,550**		**75,550**	**75,550**

Balance Sheet as on 31-12-2004

Liabilities	Amt	Amt	Assets	Amt	Amt
Capitals:			Goodwill		90,000
B	83,736		Furniture	20,000	
C	83,737	1,67,473	*Less:* Depreciation	750	19,250
A's Loan	63,358		Machinery	36,000	
Add: O/s Interest	5,069	68,427	*Less:* Depreciation	3,600	32,400
Bank Loan		20,000	Premises	50,000	
Creditors	76,500		*Less:* Depreciation	2,500	47,500
Add: Pur. to Furniture	20,000	96,500	Investments		25,000
Bill Payable		8,700	Closing Stock		42,000
			B/R		3,250
			Debtors	1,00,000	
			Less: R.D.D.	8,800	91,200
			Bank		8,000
			Cash		2,500
		3,61,100			**3,61,100**

Dr. **Partner's Capital Account** **Cr.**

Particulars	A	B	C	Particulars	A	B	C
To Drawings	12,000	12,000	12,000	By Balance c/d	30,000	30,000	30,000
To Loan	63,358			By Goodwill	30,000	30,000	30,000
To Balance c/d		83,736	83,737	By Interest on Capital	1,500	3,000	3,000
				By P&L A/c	13,858	13,858	13,859
				By P&L A/c		18,878	18,878
	75,358	**95,736**	**95,737**		**75,358**	**95,736**	**95,737**

Illustration 11: X and Y shared Profit and Losses equally. Their Trial Balance as on 31^{st} December, 2003 was as under:

Particulars	Amt	Amt
Capital Account:		
X		75,000
Y		75,000
Current Account:		
X	7,500	
Y	7,500	
Fixed Assets	75,000	
Debtors	25,000	
Bank	25,000	
Stock (Opening)	12,500	
Purchases	62,500	
Wages	6,250	
Office & Administration Expenses	12,500	
Selling & Distribution Expenses	10,000	
Creditors		12,500
Sales		1,12,500
Advances	31,250	
	2,75,000	**2,75,000**

Additional Information

(i) Z retired on 30^{th} June, 2003. His capital was paid off but the amounts due to him for profit of the year, share of goodwill ` 10,000, interest on his capital ` 1,250 were to be paid.

(ii) X, Y and Z were sharing profit and losses in the ratio of 2 : 2 : 1.

(iii) Closing stock was ` 6,250 on 30-6-2003 and ` 7,500 31-12-2003.

Item	Upto 30-6-2003	After 31-12-2003
Purchases	37,500	25,000
Wages	3,750	2,500
Sales	75,000	37,500

Other expenses were to be equally distributed between the two periods:

(a) Depreciation on fixed assets by 10% p.a.

(b) Allow interest at 10% p.a. on capital.

Solution:

Dr. Trading Account for the year ended 31-12-2003 Cr.

Particulars	Jan-June	July-Dec	Particulars	Jan-June	July-Dec
To Opening Stock	12,500	6,250	By Sales	75,000	37,500
To Purchase	37,500	25,000	By Closing Stock	6,250	7,500
To Wages	3,750	2,500			
To Gross Profit c/d	27,500	11,250			
	81,250	**45,000**		**81,250**	**45,000**

Dr. Profit and Loss Account for the year ended 31-12-2003 Cr.

Particulars	Jan-June	July-Dec	Particulars	Jan-June	July-Dec
To Office & Admin Exp	6,250	6,250	By Gross Profit	27,500	11,250
To Selling & distri Exp	5,000	5,000	By Net Loss c/d		3,750
To Dep. on Fixed Asset	3,750	3,750			
To Net Profit	12,500				
	27,500	**15,000**		**27,500**	**15,000**

Dr. Profit and Loss Appropriation for the year ended 31-12-2003 Cr.

Particulars	Jan-June	July-Dec	Particulars	Jan-June	July-Dec
To Net Loss b/d		3,750	By Net Profit b/d	12,500	
To Interest on Capital:			By Net Loss (after 1-7):		
X	3,750	3,750	X		5,625
Y	3,750	3,750	Y		5,625
Z	1,250				
To Net Profit (30-6):					
X	1,500				
Y	1,500				
Z	750				
	12,500	**11,250**		**12,500**	**11,250**

Balance Sheet as on 31-12-2003

Liabilities	Amt	Amt	Assets	Amt	Amt
Capital Account:			Fixed Assets	75,000	
X	75,000		*Less:* Depreciation	7,500	67,500
Y	75,000	1,50,000	Closing Stock		7,500
Due to Z		12,000	Debtors		25,000
Creditors		12,500	Bank		25,000
			Advances		31,250
			Current Account:		
			X		9,125
			Y		9,125
		1,74,500			**1,74,500**

Dr. **Partner's Current Account** **Cr.**

Particulars	X	Y	Z	Particulars	X	Y	Z
To Balance b/d	7,500	7,500		By Interest	7,500	7,500	1,250
To Goodwill w/o	5,000	5,000		By Profit (upto 30-6)	1,500	1,500	750
To Net Loss (after 1-7)	5,625	5,625		By Goodwill			10,000
To Tfd Due to Z A/c			12,000	by Balance c/d	9,125	9,125	
	18,125	**18,125**	**12,000**		**18,125**	**18,125**	**12,000**

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