CHAPTER 5

ADMISSION OF A NEW PARTNER

Why a new partner is admitted?	A new partner may be admitted when the firm needs a. Additional Capital b. Managerial Help c. Both
How can a new partner be admitted?	Unless it is otherwise provided in the partnership deed a new partner can be admitted only when the existing partners unanimously agree for it.
Two main Rights acquired by a newly admitted partner	1. Right to share the assets of the partnership firm. 2. Right to share the profits of the partnership firm and Right to participate in the business activity
What does a new partner bring to acquire the rights?	To acquire share in the assets and profits of the firm, the partner brings 1. An agreed amount of Capital either in Cash or kind and / or some technical skill 2. Additional amount known as premium of Goodwill
Why is new partner required to bring premium?	This is due to compensate the existing partners for loss of their Share in the Super Profits of the firm. When a person pays for Goodwill, he pays for sacrifice of the profits by old partners.
New profit sharing ratio and sacrificing ratio	The ratio in which all partners, including new partner will share future profits losses of the firm is known as new profit sharing ratio. Sacrificing ratio is the ratio in which old or existing partners forego their share of profit in favour of the new partner.

	New Profit Sharing Ratio and Sacrificing Ratio
When share of new partner is given but sacrifice made by old partners is not given	(i) Deduct the new partner's share from 1 (ii) Divide the remaining share among old partner in old profit sharing ratio. **Sacrificing Ratio** is same as that of **Old Profit Sharing Ratio.**
When share of new partner is given and new share of old partner is given	(i) Deduct the new partners' share from 1 (ii) Divide the remaining share among old partner in new profit sharing ratio. Sacrificing share = Old share – New share
When new partner acquires his share from old partners' equally or in particular ratio.	(i) Deduct the sacrifice made in favour of new partner from the old share of old partners. (ii) Share surrendered by old partners is added to calculate new partner share.
When existing partner retains his original share on admission of a partner	(i) Deduct the new partners' share and share of existing partner (who retains his old share) from 1 (ii) Divide the remaining share among old partner in profit sharing ratio.

Treatment of Goodwill in case of Admission of a Partner	**When Goodwill is Paid Privately**	**No Entry**
	When goodwill is brought in cash or cheque by new partner and retained in the firm	Cash / Bank A/c Dr. To new partner' capital A/c To premium for goodwill A/c (Being capital and premium for goodwill brought in) **Premium for Goodwill A/c** Dr. **To Sacrificing Partners' Capital/ Current A/cs** (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) Current A/c incase of Fixed capitals
	When Goodwill is brought in cash or cheque by new	**Cash/Bank A/c Dr.** **To New partners' CapitalA/c** **To premium for Goodwill A/c**
	Partner and Withdrawn by sacrificing partners	(Being capital and premium for goodwill brought in) **Premium for Goodwill A/c** **Dr.** To sacrificing Partners Capital / Current A/cs (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) **Sacrificing Partners' Capital / Current A/Cs** **Dr.** **To Cash / Bank A/c** (Being withdrawal of premium by the partners)
		Current A/C in case of Fixed capitals

	When Goodwill is Brought in Kindt	Asset A/c To New Partners' Capital A/c To Premium for Goodwill A/c To Liabilities A/c (Being asset contributed as capital and premium for goodwill) **Premium for Goodwill A/c** **Dr.** To sacrificing Partners' Capital / Current A/cs (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) Current A/c in case of Fixed capitals
	When Goodwill is not Brought in Full or Part by the New Partner (In case Goodwill is not Raised)	**Cash / Bank A/c Dr.** **To new Partners' Capital A/c** **To Premium for Goodwill A/c** (with share of goodwill brought in) (Being capital and premium for goodwill brought in) Premium for Goodwill A/c (with paid share of goodwill) Dr. Incoming partners' Current A/c (with unpaid share of goodwill) Dr. **To sacrificing partners' Capital / Current A/cs** (Being premium for goodwill is distributed among sacrificing partners's in sacrificing ratio) Sacrificing partners current A/c in case of Fixed capital
	When Goodwill is Raised and Written Off (In case Goodwill is Brought in Part By the New Partner	Cash / Bank A/c To New Partners' Capital A/c To Premium for Goodwill A/c (Being capitals premium for goodwill brought in)

		Premium for Goodwill A/c (with share of goodwill brought in) **Dr.** To Sacrificing Partners' Capital / Current A/cs (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) **Goodwill A/c Dr.** To Sacrificing Partners' Capital / Current A/cs (Being goodwill is raised in old ratio) **Sacrificing Partners' Capital / Current A/cs Dr.** **Incoming Partners' Current A/c Dr.** **To Goodwill A/c** (Being goodwill written off in new ratio) Sacrificing partners Current A/c in case of Fixed capital.
	When Goodwill is Raised Written Off (In Case Goodwill is not Brought in Full)	**Cash / Bank A/c Dr.** **To New Partner's Capital A/c** (Being capital brought in by new partner Goodwill A/c) **Dr.** To Sacrificing Partner's capital Current A/cs (Being goodwill is raised in old ratio) Sacrificing Partner's Capital / Current A/cs **Dr.** Incoming Partner's current A/c **Dr.** To Goodwill A/c (Being goodwill written off in new ratio)

<table>
<tr><td></td><td><table><tr><td>When Existing Good will is Written Off</td><td>Old Partner's Capital / Current A/cs
To Goodwill A/c
(Being goodwill written off among old partner's in old ratio)
Current A/c incase of Fixed capitals</td></tr></table></td></tr>
<tr><td>Treatment of Reserves, Accumulated Profits and Losses</td><td>Accumulated profits include credit balance of P and L A/c, General Reserves, Reserve Fund, Workmen Compensation Reserves, Investment Fluctuation Reserve etc.
Accumulated Losses include debit balance of P and L A/c, Deferred Revenue Expenditure i.e., Advertisement Suspense A/c.
(A) When question is silent of when accumulated profits of losses are to be distributed or when accumulated profits or losses are not to be shown in new balance sheet
Contingency Reserve A/c **Dr.**
Reserve A/c **Dr.**
P and L A/c (Cr. Balance) **Dr.**
Workmen Compensation Reserve A/c **Dr.**
Investment Fluctuation Reserve A/c **Dr.**
To Old Partners' Capital / Current A/cs
(Being reserves and accumulated profits transferred to old partners in old ratio)
Old Partners' Capital / Current A/Cs **Dr.**
To P and L A/c (Dr. balance)
To Deferred Revenue Expenditure A/c
(Being accumulated losses transferred to old partners in old ratio)
Current A/c in case of Fixed capitals</td></tr>
<tr><td></td><td>**Treatment of Workmen Compensation Reserve**<table><tr><td>**Case 1.**
When there is no Claim</td><td>Workmen Compensation Reserve A/c Dr.
To Old Partners' Capital / Current A/cs</td></tr><tr><td>**Case 2.** WCC = WCR (equal)</td><td>Workmen Compensation Reserve A/c Dr.
To Provision for Workmen Compensation Claim A/c</td></tr></table></td></tr>
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Case 3. WCC < WCR (less)	Workmen Compensation Reserve A/c Dr. To Provision for Workmen Compensation Claim A/c To Old Partners' Capital / Current A/cs
Case 4. WCC > WCR (more)	Workmen Compensation Reserve A/c Dr. Revaluation A/c Dr. To Provision for Workmen Compensation Claim A/c To Old Partners' Capital / Current A/cs To Revaluation A/c

WCC stands for Workmen Compensation Claim

WCR stands for Workmen Compensation Reserve

Treatment of Investment Fluctuation Reserve

Case 1. BV = MV	Investment Fluctuation Reserve A/c Dr. To Old Partners' Capital / Current A/cs
Case 2. BV < MV	Investment Fluctuation Reserve A/c Dr. To Old Partners' Capital / Current A/cs (Entire reserve distributed in partners' old ratio) Investment A/c Dr. To Revaluation A/c (For increase in value of Investments) Revaluation A/c To Old Partners' Capital / Current A/cs
Case 3. BV > MV	(i) When fall in value is less than investment Fluctuation Reserve Investment Fluctuation Reserve A/c Dr. To Investment A/c (BV-MV) To Old Partners' Capital / Current A/cs (In Old ratio) (ii) When fall in value is equal to investment Fluctuation Reserve Investment Fluctuation Reserve A/c Dr. To Investment A/c

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<tr><td></td><td>(iii) When fall in value is more than investment Fluctuation Reserve
Investment Fluctuation Reserve A/c Dr.
Revaluation A/c Dr.
To Investment A/c
Old Partners' Capital / Current A/cs Dr.
To Revaluation A/c</td></tr>
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BV stands for Book value of Investment
MV stands for Market value of investment
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<td>Revaluation of Assets and Reas- sess- ment of Liabilities</td>
<td>
It is a nominal account and prepared to revalue assets and reassess liabilities.
(A) When Revised Values of Assets and Liabilities are to be Recorded
Revaluation A/c is prepared and Profit/Loss of revaluation is distributed among old partners' in old ratio.
Dr. RevaluationA/c Cr
<table>
<tr><th>Particulars</th><th>Amount (Rs)</th><th>Particulars</th><th>Amount (Rs.)</th></tr>
<tr><td>To asset (decrease in value)</td><td>xxx</td><td>By asset (increase in value)</td><td>xxx</td></tr>
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<tr><td>Total</td><td>xxx</td><td>Total</td><td>xxx</td></tr>
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<td>Adjustment of capital</td>
<td>
(i) Adjustment of Old Partners' Capital on the basis of new Partners' Capital
Step 1. Calculate total Capital of the firm on the basis of New Partners' Capital :
Total capital of the firm on the basis of New Partners' Capital $= \dfrac{\text{Capital of the New Partner}}{\text{Share of profitof New Partner}}$
Step 2. Determine New Capital of each Partner by dividing the Total Capital in new profit sharing ratio.
Step 3. Ascertain Present Capital of the Old Partners' after all adjustments
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Step 4. Find Surplus / Deficit—

Surplus = Present Capital > New Capital

Deficit = Present Capital < New Capital

Step 5. In case of **Surplus** (Present Capital > New Capital)

Concerned partners' Capital A/c Dr.

To Bank / Cash A/c

To Concerned Partners' Current A/c

In case of **Deficit** (Present Capital < New Capital)

Bank / Cash A/c Dr.

Concerned Partners' Current A/c Dr.

To Concerned Partners' Capital A/c

(ii) **Adjustment of New Partners' Capital on the basis of Old Partners' Capital**

Step 1. Determine Total Adjusted Capital of the Old Partners' after all adjustments

Step 2. Calculate Total Capital of the new firm on the basis of Old Partner's after all adjustment:

Total Capital of the new firm

$$= \frac{\text{Total adjusted Capital of Old Partners}}{\text{Total Share of Old Partners}}$$

Step 3. Determine Capital of New Partner by multiplying the total Capital by Share of New Partner.

NEW PROFIT SHARING RATIO

Illustration 1.

A and B are partners in a firm sharing profit and losses in the ratio of 3 : 2. C is admitted for 1/5th share in profits of the firm.

Calculate new profit sharing ratio; if—

(a) C gets his share equally from A and B.

(b) C gets it from A and B in 2 : 1.

(c) C gets it 3/20 from A and 1/20 from B.

(d) C gets it wholly from A

Solution.

(a) C gets 1/5 equally from A and B

Share acquired by C from A = $\frac{1}{2} \times \frac{1}{5} = \frac{1}{10}$

Share acquired by C from B = $\frac{1}{2} \times \frac{1}{5} = \frac{1}{10}$

A's New Share = $\frac{3}{5} - \frac{1}{10} = \frac{6-1}{10} = \frac{5}{10}$

B's New Share = $\frac{2}{5} - \frac{1}{10} = \frac{4-1}{10} = \frac{3}{10}$

C's New Share = $\frac{1}{5}$ or $\frac{2}{10}$

New Profit sharing Ratio = A : B : C = 5 : 3 : 2

(b) C gets 1/5 from A and B in 2 : 1

Share acquired by C from A = $\frac{2}{3} \times \frac{1}{5} = \frac{2}{15}$

Share acquired by C from B = $\frac{1}{3} \times \frac{1}{5} = \frac{1}{15}$

A's new share = $\frac{3}{5} - \frac{2}{15} = \frac{9-2}{15} = \frac{7}{15}$

B's new share = $\frac{2}{5} - \frac{1}{15} = \frac{6-1}{15} = \frac{5}{15}$

C's new share = $\frac{1}{5}$ or $\frac{3}{15}$

New profit sharing ratio = A : B : C = 7 : 5 : 3

(c) C gets 1/5 from A and B as 3/20 and 1/20 respectively

A's new share = $\frac{3}{5} - \frac{3}{20} = \frac{12-3}{20} = \frac{9}{20}$

B's new share = $\frac{2}{5} - \frac{1}{20} = \frac{8-1}{20} = \frac{7}{20}$

C's new share = $\frac{3}{20} + \frac{1}{20} = \frac{4}{20}$

New profit sharing Ratio = A : B : C = 9 : 7 : 4

(d) C gets 1/5 wholly from A

A's new share = $\frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

B's new share = $\frac{2}{5}$

C's new share = $\frac{1}{5}$

New profit sharing Ratio = 2 : 2 : 1 in A : B : C

In case (d), B retains his old share (2/5)

SACRIFICING RATIO

Illustration 2.

X and Y are partners sharing profit in the ratio 3 : 2. They admit P and Q as new partners. X surrendered 1/3rd of his share in favour of P and Y surrendered 1/4th of his share in favour of Q.

Calculate (a) Sacrificing ratio

(b) New profit sharing ratio X, Y, P and Q.

Solution:

(a) Calculation of Sacrificing Ratio

X surrenders 1/3 of his share in factor of P = $\frac{1}{3} \times \frac{3}{5} = \frac{3}{15}$

Y surrenders 1/4 of his share in favour of Q = $\frac{1}{4} \times \frac{2}{5} = \frac{2}{20}$

$$X : Y = \frac{3}{15} : \frac{2}{20}$$

$$\frac{3}{15} \times \frac{4}{4} : \frac{2}{20} \times \frac{3}{3}$$

$$\frac{12}{60} : \frac{6}{60}$$

$\Rightarrow$ 12 : 6 or 2 : 1

(b) Calculation of New Profit sharing ratio

X's New share = $\frac{3}{5} - \frac{3}{15} = \frac{9-3}{15} = \frac{6}{15}$ or $\frac{24}{60}$

Y's New share = $\frac{2}{5} - \frac{2}{20} = \frac{8-3}{20} = \frac{6}{20}$ or $\frac{18}{60}$

P's = $\frac{3}{15}$ or $\frac{12}{60}$

Q's = $\frac{2}{20}$ or $\frac{6}{60}$

X : Y : P : Q = 24 : 18 : 12 : 6

= 4 : 3 : 2 : 1

Illustration 3.

X and Y are partners sharing profit and losses in the ratio 3 : 2. They admit Z into the partnership, who acquires 1/4th of his share from X and 3/16th share from Y.

Calculate New Profit Sharing Ratio and Sacrificing Ratio.

Solution:

Since Z acquires $\frac{1}{4}^{th}$ of his share from X

It means he acquires $\frac{3}{4}^{th}\left(1-\frac{1}{4}\right)$ of his share from Y.

If 3/4th share of Z = $\frac{3}{16}$ (Received from Y)

Z's share = $\frac{3}{16}\times\frac{4}{3}=\frac{1}{4}$

Share acquired by Z from X = $\frac{1}{4}\times\frac{1}{4}=\frac{1}{16}$

Share acquired by Z from Y = $\frac{3}{16}$

Hence, X's new share = $\frac{3}{5}-\frac{1}{16}=\frac{48-5}{80}=\frac{43}{80}$

Y's new share = $\frac{2}{5}-\frac{1}{16}=\frac{32-5}{80}=\frac{17}{80}$

Z's share = $\frac{1}{4}$ or $\frac{20}{80}$

New profit sharing ratio = X : Y : Z = 43 : 17 : 20

Sacrificing Ratio X : Y = $\frac{1}{16}:\frac{3}{16}=1:3$

Illustration 4.

(a) A, B and C are partners sharing profits and losses in the ratio of 5 : 3 : 2. C retired and his capital balance after adjustments regarding reserves, accumulated profits/losses and gain/loss on revaluation was ₹ 2,50,000. C was paid ₹ 3,00,000 in full settlement. Afterwards D was admitted for $1/4^{th}$ share. Calculate the amount of goodwill premium brought by D.

Solution:

Goodwill share of C = ₹ 3,00,000 – ₹ 2,50,000 = ₹ 50,000

Firm's Goodwill = $50{,}000 \times \frac{10}{2}$ = ₹ 2,50,000

D's share in Goodwill = ₹ 2,50,000 × $\frac{1}{4}$ = ₹ 62,500

(b) A and B were partners in a firm. They admitted C as a new partner for 20% share in the profits. After all adjustments regarding general reserve, goodwill, gain or loss on revaluation, the balances in capital accounts of A and B were ₹ 3,85,000 and ₹ 4,15,000 respectively. C bought proportionate capital so as to give him 20% share in the profits.

Calculate the amount of capital to be brought by C.

Solution:

Combined capital of A and B

= ₹ 3,85,000 + ₹ 4,15,000 = ₹ 8,00,000

C's share = $\frac{1}{5}^{th}$ of total capital

Remaining share = $1-\frac{1}{5}=\frac{4}{5}$

$\frac{4}{5}$ = ₹ 8,00,000

C's capital = ₹ 8,00,000 × $\frac{5}{4}\times\frac{1}{5}$

= ₹ 2,00,000

(C) Rekha, Sunita and Teena are partners in a firm sharing profits in the ratio of 3 : 2 : 1. Samiksha joins the firm. Rekha surrenders 1/4th of her share; Sunita surrenders 1/3rd of her share and Teena surrenders 1/5th of her share in favour of Samiksha. Find the new Profit sharing ratio.

Solution:

Rekha surrenders for Samiksha = $\frac{1}{4}\times\frac{3}{6}=\frac{3}{24}$

Sunita surrenders for Samiksha = $\frac{1}{3}\times\frac{2}{6}=\frac{2}{18}$

Teena surrenders for Samiksha = $\frac{1}{5}\times\frac{1}{6}=\frac{1}{30}$

New share of Rekha = $\frac{3}{6}-\frac{3}{24}=\frac{9}{24}$

New share of Sunita = $\frac{2}{6}-\frac{2}{18}=\frac{4}{18}$

New share of Teena = $\frac{1}{6}-\frac{1}{30}=\frac{4}{30}$

Share of Samiksha = $\frac{3}{24}+\frac{2}{18}+\frac{1}{30}=\frac{97}{360}$

New ratio : $\frac{9}{24}:\frac{4}{18}:\frac{4}{30}:\frac{97}{360}$ = 135 : 80 : 48 : 97

Illustration 5. When Premium for Goodwill is Brought in Cash

(a) A and B are partners in a firm sharing profits and losses in the ratio of 3 : 2. C is admitted as a new partner. A surrenders 1/5th of his share and B 2/5th of his share in favour of C. Goodwill of the firm is valued at ₹ 75,000. C brings his share of goodwill in cash.

Journalise the above transaction when–

(i) Goodwill is retained in the firm

(ii) Goodwill is withdrawn by old partners

Solution:

(i) **Goodwill is Retained in the Firm**

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		21,000	
	To Premium for Goodwill A/c			21,000
	(Being the amount of Goodwill brought in)			
	Premium for Goodwill A/c Dr.		21,000	
	To A's Capital A/c			9,000
	To B's Capital A/c			12,000
	(Being goodwill distributed between A and B in sacrificing ratio, i.e., 3 : 4)			

(ii) **Goodwill is Withdrawn by Old Partners**

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		21,000	
	To Premium for Goodwill A/c			21,000
	(Being the amount of Goodwill brought in)			
	Premium for Goodwill A/c Dr.		21,000	
	To A's Capital A/c			9,000
	To B's Capital A/c			12,000
	(Being amount of goodwill distributed between A and B in sacrificing ratio, i.e., 3 : 4)			
	A's Capital A/c Dr.		9,000	
	B's Capital A/c Dr.		12,000	
	To Bank A/c			21,000
	(Being amount of goodwill is withdrawn by old partners)			

Working Notes:

1. Calculation of Sacrificing ratio–

A's Sacrifice $\frac{1}{5}$ of his share = $\frac{1}{5} \times \frac{3}{5} = \frac{3}{25}$

B's Sacrifice $\frac{2}{5}$ of his share = $\frac{2}{5} \times \frac{2}{5} = \frac{4}{25}$

Thus, Sacrificing ratio of A : B = 3 : 4

2. Calculation of C's share of Goodwill–

C's share of profit = $\frac{3}{25} + \frac{4}{25} = \frac{7}{25}$

Hence, C's share of Goodwill = $\frac{7}{25} \times 75,000$ = ₹ 21,000

(b) When Premium for Goodwill is Brought in Kind

A and B are partners in a firm sharing profits and losses in the ratio of 3 : 2. C is admitted as a new partner for 3/13th share in the profits. C contributed following assets towards his capital and for his share of goodwill. Land ₹ 90,000; Machinery ₹ 90,000; Stock ₹ 60,000; Debtors ₹ 60,000. On the date of admission, Goodwill of the firm is valued at ₹ 5,20,000. Journalize the above transaction.

Solution:

Goodwill is Brought in Kind

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Land A/c Dr.		90,000	
	Machinery A/c Dr.		90,000	
	Stock A/c Dr.		60,000	
	Debtors A/c Dr.		60,000	
	To premium for Goodwill A/c (5,20,000 × 3/13)			1,20,000
	To C's Capital A/c (b/f)			1,80,000
	(Being the amount of capital and Goodwill brought in kind)			
	Premium for Goodwill A/c Dr.		1,20,000	
	To A's Capital A/c			72,000
	To B's Capital A/c			48,000
	(Being goodwill distributed between A and B in sacrificing ratio, i.e., 3 : 2)			

(c) When Premium for Goodwill is not Brought in Kind

Neeta and Sunita are partners in a firm sharing profits and losses in the ratio of 2 : 1. Geeta is admitted as anew partner for 1/4th share in the profits. Geeta pays ₹ 50,000 as capital but does not bring any amount for goodwill. Goodwill of the firm is valued at ₹ 36,000.

(i) Journalize the above transaction.

(ii) Also, give journal entries if Goodwill is raised and written off.

Solution:

(i) Goodwill is not Brought in Cash and Adjusted Through Partner's Current A/c

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Cash A/c Dr.		50,000	
	To Geeta's Capital A/c			50,000
	(Being the amount of capital brought in)			
	Geeta's Current A/c Dr.		9,000	
	To Neeta's Capital A/c			6,000
	To Sunita's Capital A/c			3,000
	(Being goodwill distributed between Neeta and Sunita in sacrificing ratio, i.e., 2 : 1)			

(ii) When Goodwill is Raised and Written Off

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Cash A/c Dr.		50,000	
	To Geeta's Capital A/c			50,000
	(Being the amount of capital brought in)			
	Goodwill A/c Dr.		36,000	
	To Neeta's Capital A/c			24,000
	To Sunita's Capital A/c			12,000
	(Being goodwill raised in old ratio, i.e., 2 : 1)			
	Neeta's Capital A/c Dr.		18,000	
	Sunita's Capital A/c Dr.		9,000	
	Geeta's Capital A/c Dr.		9,000	
	To Goodwill A/c			36,000
	(Being Goodwill written off in new ratio i.e., 2 : 1 : 1)			

Working Note: Calculation of New Profit sharing ratio–

Let total share of the firm = 1

Geeta's share = $\frac{1}{4}$

Remaining share = $1-\frac{1}{4}=\frac{3}{4}$

Neeta's new share = $\frac{3}{4}\times\frac{2}{3}=\frac{2}{4}$

Sunita's new share = $\frac{3}{4}\times\frac{1}{3}=\frac{1}{4}$

Hence, New profit sharing ratio N : S : G = 2 : 1 : 1

(d) When Premium for Goodwill is Partly Brought in Cash

Neeta and Sunita are partners in a firm sharing profits and losses equally. Geeta is admitted as a new partner. Geeta pays ₹ 1,000 for premium out of her share of goodwill of ₹ 1,600 for 1/4th share of profit. Goodwill A/c appears in the books at ₹ 6,000.

(i) Journalize the above transaction.

(ii) Also, give journal entries if Goodwill is raised and written off.

Solution: (i) When Premium for Goodwill is Partly Brought in Cash

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		1,000	
	To Premium for Goodwill A/c			1,000
	(Being the amount of Goodwill brought in cash)			
	Premium for Goodwill A/c Dr.		1,000	
	Geeta's Current A/c Dr.		600	
	To Neeta's Capital A/c			800
	To Sunita's Capital A/c			800
	(Being goodwill distributed between Neeta and Sunita in sacrificing ratio, i.e., 1 : 1)			
	Neeta's Capital A/c Dr.		3,000	
	Sunita's Capital A/c Dr.		3,000	
	To Goodwill A/c			6,000
	(Being existing goodwill written of between old partners in old ratio i.e., equal)			

(ii) When Goodwill is Raised and Written Off

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		1,000	
	To Premium for Goodwill A/c			1,000
	(Being the amount of Goodwill brought in cash)			
	Premium for Goodwill A/c Dr.		1,000	
	To Neeta's Capital A/c			500
	To Sunita's Capital A/c			500
	(Being goodwill distributed between Neeta and Sunita in sacrificing ratio, i.e., 1 : 1)			
	Goodwill A/c (600 × 4/1) Dr.		2,400	
	To Neeta's Capital A/c			1,200
	To Sunita's Capital A/c			2,200
	(Being goodwill raised in old ratio, i.e., 1 : 1)			

	Neeta's Capital A/c Dr.		900	
	Sunita's Capital A/c Dr.		900	
	Geeta's Current A/c Dr.		600	
	To Goodwill A/c			2,400
	(Being goodwill written off in new ratio i.e., 3 : 2 : 2)			
	Neeta's Capital A/c Dr.		3,000	
	Sunita's Capital A/c Dr.		3,000	
	To Goodwill A/c			6,000
	(Being existing goodwill written off between old partners in old ratio i.e., equal)			

Working Note: 1. Calculation of New profit sharing ratio–

Geeta's share = $\frac{1}{4}$

Remaining share = $1-\frac{1}{4}=\frac{3}{4}$

Neeta's new share = $\frac{3}{4}\times\frac{1}{2}=\frac{3}{8}$

Sunita's new share = $\frac{3}{4}\times\frac{1}{2}=\frac{3}{8}$

Hence, New profit sharing ratio N : S : G = 3 : 3 : 2

2. Calculation of amount of Goodwill to be raised and written off

Amount of Goodwill not brought by Geeta = 400

His share of profit = $\frac{1}{4}$

Amount of Goodwill to be raised and written off = $400\times\frac{4}{1}=2400$

Illustration 6.

Naresh and Suresh are partners in a firm sharing profits and losses in the ratio of 3 : 1. On April 1st 2019, they admitted Rahul as a partner for 1/5th share in the profits of the firm. On the date of admission, the balance sheet showed a General Reserve of ₹ 1,20,000; a debit balance of ₹ 60,000 in Profit and Loss A/c; Workmen compensation Reserve of ₹ 1,50,000 and Investment fluctuation Reserve of ₹ 10,000.

The following terms were agreed upon–

(i) Rahul will bring ₹ 1,50,000 as his capital and his share of goodwill in cash.

(ii) Goodwill of the firm be valued at ₹ 2,40,000.

(iii) There was a claim of Workmen compensation for ₹ 1,70,000

(iv) The market value of investment was ₹ 18,000 less than the Book value.

(v) The partners decided to share future profits in the ratio of 3 : 1 : 1.

Pass the necessary Journal entries on Rahul's admission.

Solution:

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
1st April 2019	General Reserve A/c Dr.		1,20,000	
	To Naresh's Capital A/c			1,20,000
	To Suresh's Capital A/c			
	(Being General Reserve distributed between old partners in oldratio, 3 : 1)			
	Naresh's Capital A/c Dr.		45,000	
	Suresh's Capital A/c Dr.		15,000	
	To Profit and Loss A/c			60,000
	(Being P and L distributed between old partners in old ratio, 3 : 1)			
	Workmen compensation Reserve A/c Dr.		1,50,000	
	Revaluation A/c Dr.		20,000	
	To Provision for Workmen Compensation Claim A/c			1,70,000
	(Being Workmen Compensation Claim adjusted against Workmen compensation Reserve)			
	Investment fluctuation Reserve A/c Dr.		10,000	
	Revaluation A/c Dr.		8,000	
	To Investment A/c			18,000
	(Being fall in value of investment adjusted against Investment fluctuation Reserve and Revaluation A/c)			
	Naresh's Capital A/c Dr.		21,000	
	Suresh's Capital A/c Dr.		7,000	
	To Revaluation A/c			28,000
	(Being loss on revaluation transferred to old partners in old ratio)			

	Bank A/c Dr. To Rahul's Capital A/c To Premium for Goodwill A/c (2,40,000 × 1/5) (Being the amount of capital and Goodwill brought in)		1,98,000	 1,50,000 48,000
	Premium for Goodwill A/c Dr. To Naresh's Capital A/c To Suresh's Capital A/c (Being amount of Goodwill distributed between Naresh and Suresh sacrificing ratio, i.e., 3 : 1)		48,000	 36,000 12,000

Hidden Goodwill

Illustration 7.

A and B are partners with capital of ₹ 26000 and ₹ 22000 respectively. They admit C as partner with 1/4th share in the profits of the firm. C brings ₹ 26,000 as his share of capital.

Give journal entry to record goodwill on C's admission

Solution :

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
1st April 2019	Bank A/c Dr. To C's Capital A/c (Being the amount of Capital brought in by new partner)		26,000	 26,000
	C's Current A/c Dr. To A's Capital A/c To B's Capital A/c (Being the Goodwill credited to sacrificing partners Capital A/cs in their sacrificing ratio, i.e., equal)		7,500	 3,750 3,750

Working Note :

(1) Calculation of C's share of Goodwill–

Total capital of new firm on the basis of C's capital

$$= 26000 \times \frac{4}{1} = ₹\ 1,04,000$$

Total capital of A, B and C

= ₹ 26000 + ₹ 22000 + ₹ 26000

= ₹ 74000

Goodwill of the firm

= Total capital of new firm – Combined capital of A, B and C

= ₹ 104000 – ₹ 74000

= ₹ 30000

C's share of Goodwill

$= 30000 \times \frac{1}{4} = ₹\ 7500$

(2) In the absence of information, profits will be shared Equally.

Illustration 8.

X and Y were partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance sheet as at 31st March, 2019 was as follows:

Liabilities	₹	Assets	₹
Creditors	42,000	Current Assets	2,00,000
Employee's Provident Fund	20,000	Investments	50,000
Contigency Reserve	30,000	Furniture	20,000
Profit and Loss Account	45,000	Machinery	90,000
Workment Compensation Reserve	18,000	Advertisement Expenditure (Deffered Revenue Expenditure)	20,000
Investment Fluctuation Reserve	25,000		
Capitals X 1,20,000			
Capitals Y 80,000	2,00,000		
	3,80,000		3,80,000

They admit Z into partnership on 1st April, 2019 and the new profit sharing ratio is agreed at 2 : 1 : 1. It is estimated that:

(i) Claim on account of Workmen's Compensation is estimated at ₹ 10,000.

(ii) Market value of Investments is ₹ 46,000.

Give necessary journal entries to adjust accumulated profits and losses.

Solution:

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
1st April 2019	Investment Fluctuation Reserve Dr.		4,000	
	To Investment A/c			4,000
	(Value of Investment brought down to market value)			

	Workmen Compensation Reserve A/c Dr. To Provision for Workmen Compensation Claim A/c (Provision made for workmen compensationclaim)		10,000	10,000
1st April 2019	Contigency Reserve Dr. Profit and Loss A/c Dr. Workmen Compensation Reserve (₹ 18,000 – ₹ 10,000) Dr. Investment Fluctuation Reserve (₹ 25,000 – ₹ 4,000) Dr. To X's Capital A/c To Y's Capital A/c (Transfer of accumulated profits to old partners in their old profit sharing ratio i.e., 3 : 2)		30,000 45,000 8,000 21,000	62,400 41,600
1st April 2019	X's Capital A/c Dr. Y's Capital A/c Dr. To Advertisement Expenditure A/c (Transfer of accumulated loss to old partners in their old profit sharing ratio i.e., 3 : 2)		12,000 8,000	20,000

Working Note: Employee's Provident Fund is outside liability payable by the firm.

Illustration 9.

X and Y are in partnership, sharing profits in the ratio of 5 : 3 respectively. Their balance sheet is as follows:

Liabilities	₹	Assets	₹
Creditors	28,000	Cash at Bank	15,800
Workment Compensation Reserve	12,000	Debtors 40,000 Less : Provision 1,800	38,200
Z's Loan A/c	30,000	Stock	56,000
		Investment	10,000
Capitals X 1,20,000	50,000	Goodwill	10,000
Capitals Y 80,000	40,000	Plant	30,000
	1,60,000		1,60,000

Z is admitted into partnership on the following terms:

1. The new profit-sharing ratio will be 4 : 3 : 2 between X, Y and Z respectively.

2. Z's loan should be treated as his capital.
3. Goodwill of the firm is valued at ₹ 27,000.
4. ₹ 8,000 of investments were to be taken over by X and Y in their profit sharing ratio.
5. Stock be reduced by 10%.
6. Provision for doubtful debts should be @ 5% on debtors and a provision for discount on debtors @ 2% should also bemade.
7. The liability of Workmen's Compensation Reserve was determined to be ₹ 15,000.
8. X is to withdraw ₹ 6,000 in cash.

Give journal entries to record the above and prepare balance sheet of the new firm.

Solution:

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Revaluation A/c Dr. To Stock A/c To Provision for Doubtful Debts To Provision for Discount on Debtors (Decrease in the value of stock and creation of provision on debtors)		6,560	 5,600 200 760
	Workmen Compensation Reserve A/c Dr. Revaluation A/c Dr. To Liability for Workmen's Compensation A/c (Recording of liability for Workmen's Compensation)		12,000 3,000	 15,000
	X's Capital A/c Dr. Y's Capital A/c Dr. To Revaluation A/c (Loss on revaluation transferred to old partner's Capital A/cs)		5.975 3,585	 9,560
	X's Capital A/c Dr. Y's Capital A/c Dr. To Investments A/c (Investments taken over by old partners)		5,000 3,000	 8,000

	X's Capital A/c Dr. Y's Capital A/c Dr. To Goodwill A/c (Existing goodwill written off in old ratio i.e., 5 : 3)		6,250 3,750	10,000
	Z's Current A/c Dr. To X's Capital A/c To Y's Capital A/c (Z's share of goodwill credited to old partners in the sacrificing ratio i.e., 13 : 3)		6,000	4,875 1,125
	Z's Loan A/c Dr. To Z's Capital A/c (Z's Loan Account transferred to Z's Capital Account)		30,000	30,000
	X's Capital A/c Dr. To Bank A/c (Cash withdrew by X)		6,000	6,000

Partner's Capital Accounts

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Revaluation	5,975	3,585	–	By Balance b/d	50,000	40,000	–
To Investment	5,000	3,000	–	By Z's Current A/c	4,875	1,125	–
To goodwill A/c	6,250	3,750	–	By Z's Loan A/c	–	–	30,000
To Bank A/c	6,000	–	–		–	–	30,000
To Balance c/d	31,650	30,790	30,000				
	54,875	41,125	30,000		54,875	41,125	30,000

Balance Sheet as at .....

Liabilities	₹	Assets	₹
Creditors	28,000	Cash at Bank	9,800
Liabilities for Workmen's		(₹ 15800 – ₹ 6000)	
Compensation	15000	Debtors 40,000	

Capital A/cs :			Less : Provision for Doubtful Debts		
X	31,650			2,000	
Y	30,790			38,000	
Z	30,000	92,440	Less : Provision for Discount on Debtors		
				760	37,240
			Stock		50,400
			Investment		2,000
			Plant		30,000
			Z's Current A/c		6,000
		1,35,440			1,35,440

Working Note: (1) Calculation of sacrificing ratio–

Sacrificing ratio = Old ratio – New ratio

$$X = \frac{5}{8} - \frac{4}{9} = \frac{45-32}{72} = \frac{13}{72}$$

$$Y = \frac{3}{8} - \frac{3}{9} = \frac{27-24}{72} = \frac{3}{72}$$

Sacrificing ratio = 13 : 3

(2) From Z's share of goodwill, his current A/c has been debited instead of A/c so that his Capital is not reduced and remains intact at ₹ 30,000.

Illustration 10.

Deepika and Rajshree are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 31st March, 2017, their Balance Sheet was as under:

Liabilities		₹	Assets		₹
Sundry Creditors		16,000	Cash in Hand		1,200
Public Deposits		61,000	Cash at Bank		2,800
Bank Overdraft		6,000	Stock		32,000
Outstanding Liabilities		2,000	Prepaid Insurance		1,000
Capital Accounts :			Sundry Debtors		
Deepika	48,000			28,000	
Rajshree	40,000	88,000	Less : Provision for Doubtful Debts		
				800	28,000
			Plant and Machinery		48,000
			Land and Building		50,000
			Furniture		10,000
		1,73,000			1,73,000

On the above date, the partners decide to admit Anshu as a partner on the following terms:

(i) The new profit-sharing ratio of Deepika, Rajshree and Anshu will be 5 : 3 : 2, respectively

(ii) Anshu shall bring ₹ 32,000 as his capital.

(iii) Anshu is unable to bring in any cash for his share of goodwill. Partners, therefore, decide to calculate goodwill on the basis of Anshu's share in the profits and the capital contribution made by him to the firm.

(iv) Plant and Machinery would be increased by ₹ 12,000.

(v) Stock would be increased to ₹ 40,000.

(vi) Provision for Doubtful Debts is to be maintained at ₹ 4,000. Value of Land and Building has appreciated by 20%. Furniture has depreciated by 10%.

(vii) There is an additional liability of ₹ 8,000 being outstanding salary payable to employees of the firm. This liability is not included in the outstanding liabilities, stated in the above Balance sheet. Partners decide to show this liability in the books of accounts of the reconstituted new firm.

Prepare revaluation account, Partner's Capital Accounts and the Balance Sheet Deepika, Rajshree and Anshu.

Solution:

Revaluation Account

Particulars	₹	Particulars	₹
To Provision for Doubtful debts	3,200	By Plant and Machinery	12,000
			8,000
To Furniture	1,000	By Stock	10,000
To Outstanding Salary	8,000	By Land and Building	
To Profit transferred to :			
Deepika Capital A/c (3/5) 10,680			
Rajshree Capital A/c (2/5) 7,120	17,800		
	30,000		30,000

Capital Accounts

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
				By Balance b/d	48,000	40,000	—
				By Revaluation	10,680	7,120	—
				By Anshu's Current A/c	2,220	2,220	—
To Balance c/d	60,900	49,340	32,000	By Bank A/c	—		32,000
	60,900	49,340	32,000		60,900	48,340	32,000

Opening Balance Sheet

(as at 1st April, 2017)

Liabilities		₹	Assets		₹
Sundry Creditors		16,000	Cash in Hand		1,200
Public Deposits		61,000	Cash at Bank		28,800
Outstanding Liabilities		10,000	Stock		40,000
Capital Accounts :		2,000	Prepaid Insurance		1,000
Deepika	48,000		Sundry Debtors		
Rajshree	40,000			28,000	
Anshu	32,000	1,42,240	Less : Provision		
				4,000	24,800
			Plant and Machinery		60,000
			Land and Building		60,000
			Furniture		9,000
			Anshu's Current A/c		4,440
		2,29,240			2,29,240

Working Note: (1) Bank Balance : ₹ 2,800 + ₹ 32,000 – Bank Overdraft ₹ 6,000 = ₹ 28,800.

(2) Calculation of Hidden Goodwill –

Total capital of firm based on Anshu shave should be–

$$₹\ 32,000 \times \frac{10}{2} = ₹\ 1,60,000$$

Less Capital of Deepika (48,000 + 10,680) = ₹ (58,680)

Capital of Rajshree (40,000 + 7,120) = ₹ (47,120)

Capital of Anshu = ₹ (37,000)

Value of Goodwill = ₹ 22,200

Anshu's share of Goodwill = 22,200 × $\frac{2}{10}$ = ₹ 4440

(3) Calculation of sacrificing ratio

Deepika = $\frac{3}{5}-\frac{5}{10}=\frac{6-5}{10}=\frac{1}{10}$ (Sacrifice)

Rajshree = $\frac{2}{5}-\frac{3}{10}=\frac{4-3}{10}=\frac{1}{10}$ (Sacrifice)

(4) Journal Entry–

Anshu's current A/c Dr.	4,440	
To Deepika Capital A/c		2,220
To Rajshree CapitalA/c		2.220
(Being amount of goodwill credited to sacrificing partner in their SR)		

Illustration 11.

Divya, Yasmin and Fatima are partners in a firm, sharing profits and losses in 11 : 7 : 2 respectively. The balance sheet of the firm as on 31st March 2018 was as follows:

Balance Sheet As at 31st April 2018

Liabilities	₹	Assets	₹
Sundry Creditors	70,000	Factory Building	7,35,000
Public Deposits	1,19,000	Plant and Machinery	1,80,000
Reserve fund	90,000	Furniture	2,60,000
Outstanding Expenses	10,000	Stock	1,45,000
Capital Accounts :		Debtors	
Divya 5,10000		Less :	
Yasmin 3,00000		Provision 1,50000	1,20,000
Fatima 5,00000	13,10,000	Cash at bank (30000)	1,59,000
	15,99,000		15,99,000

On 1-4-2018, Aditya is admitted as a partner for one-fifth share in the profits with a capital of ₹ 4,50,000 and necessary amount of his share of goodwill on the following terms:

(i) Furniture of ₹ 2,40,000 were to be taken over Divya, Yasmin and Fatima equally.

(ii) A creditor of ₹ 7,000 not recorded in books to betaken into account.

(iii) Goodwill of the firm is to be valued at 2.5 years purchase of average profits of last two years. The profit of the last three years were:

2015-16 ₹ 6,00,000;

2016-17 ₹ 2,00,000;

2017-18 ₹ 6,00,000

(iv) At time of Aditya's admission Yasmin also brought in 50,000 as fresh capital.

(v) Plant and Machinery is re-valued to ₹ 2,00,000 and expenses outstanding were brought down to ₹ 9,000. Prepare Revaluation Account, Partners Capital Account and the balance sheet of the reconstituted firm.

Solution:

Revaluation Account

Particulars		₹	Particulars	₹
To Creditors		7,000	By Machinery	20,000
To Partner's Capital A/c			By Outstanding	
Divya	7,700		Expenses	1,000
Yasmin	4,900			
Fatima	1,400	14,000		
		20,000		21,000

Partner's Capital Account

Particulars	Divya	Yasmin	Fatima	Aditya	Particulars	Divya	Yasmin	Fatima	Aditya
To furniture A/c	80000	80000	80000		By Balance b/d	510000	300000	500000	
To Balance C/d	597200	376400	450400	450000	By Bank A/c		50000		450000
					By Reserve Fund	49500	31500	9000	
					By Premium for goodwill A/c	110000	70000	20000	
					By Revaluation Ac	7700	4900	1400	
	677200	456400	530400	450000		677200	456400	530400	450000

Balance Sheet As at 1-4-2018

Liabilities		₹	Assets		₹
Sundry Creditors		77,000	Factory Building		7,35000
Public deposits		1,19,000	Plant and Machinery		2,00000
Outstanding Expenses		9,000	Furniture		20,000
Capital accounts			Stock		1,45,000
Divya	5,97,200		Debtors	1,50000	
Yasmin	3,76,400		Less : Proviion	(30000)	1,20000
Fatima	4,50,400		Cash at bank		8,59000
Aditya	4,50,000	18,74,000			
		20,79000			20,79000

Working Note: Goodwill = 2.5 × $\left\{\frac{(60,000+20,00)}{2}\right\}$ = ₹ 10,00,000

Bank Account

Particulars	Amount ₹	Particulars	Amount ₹
To Balance B/d	1,59,000	By balance c/d	8,59,000
To Aditya's Capital A/c	4,50,000		
To Premium for Goodwill A/c	2,00,000		
To Yasmin's Capital A/c	50,000		
	8,59,000		8,59,000

Illustration 12.

P and K were partners in a firm. On March 31, 2019 their Balance Sheet was as follows:

Bank Account

Liabilities		Amount ₹	Assets		Amount ₹
Capitals:			Bank		18,000
P	3,00,000		Stock		19,000
K	2,00,000	5,00,000	Debtors	22,000	
General Reserve		1,00,000	Less : Prov. For D/d		
Creditors		50,000		1,500	20,500
Outstanding Expenses		8,000	Unexpired Insurance		5,000
C's Loan		1,20,000	Shares in X Limited		65,000
Profit and Loss Account (Profit			Plant and Machinery		1,45,500
for 2018-19)		55,000	Land and Building		5,60,000
		8,33,000			8,33,000

On April 1, 2019, they decided to admit C as a new partner for 1/4th share in profits on the following terms:

(i) C's Loan will be converted into his capital.

(ii) C will bring his share of goodwill premium by cheque. Goodwill of the firm will be calculated on the basis of Average Profits of previous three years. Profits for the year ended March 31, 2017 and March 31, 2018 were ₹ 55,000 and ₹ 1,00,000 respectively.

(iii) 10% depreciation will be charged on Plant and Machinery and Land and Building will be appreciated by 5%.

(iv) Capitals of P and K will be adjusted on the basis C's capital. Adjustments be done through bank and in case required overdraft facility be availed.

Pass necessary Journal entries on C's admission.

Solution:

Revaluation Account

Particulars	Amount ₹	Particulars	Amount ₹
To Plant and Machinery To Profit transferred to Partner's Current Accounts A 35,375 B 21,225 C 14,150	20,000 70,750	By Provision for Doubtful Debts By Land and Building	750 90,000
	90,750		90,750

Partner's Capital Account

Date	Particulars	A	B	C	Date	Particulars	A	B	C
31/3 /19	To C's Current A/c	38,250	22,950		31/3 /19	By Revaluation Account	35,375	21,225	14,150
	To Profit and Loss A/c	1,20,500	72,300	48,200		By A's current account			38,250
	To C's Capital Account			42,150		By B's current account			22950
						By General Reserve	37,500	22,500	15,000
						By Balance c/d	85,875	51,525	
		1,58,750	95,250	90,350			1,58,750	95,250	90,350

Partner's Capital Account

Date	Particulars	A	B	C	Date	Particulars	A	B	C
31/3/19	To Bank Account			35500	31/3/19	By Balance b/d	500000	300000	200000
	To C's Loan Account			206650		By C's Current Account			
	To Balance c/d	500000	300000						
		500000	300000	242150			500000	300000	242150

Balance Sheet as at March 31, 2019

Liabilities	Amount ₹	Assets	Amount ₹
Capitals:		Bank	21,000
A 5,00,000		Stock	9,000
B 3,00,000	8,00,000	Debtors 15,000	
C's Loan	2,06,650	Less : Prov. For D/d	
Creditors	23,000	750	14,250
Outstanding Salary	7,000	Plant and Machinery	1,80,000
B's Loan	15,000	Land and Building	6,90,000
		A's Current Account	85,875
		B's Current Account	51.525
	10,51,650		10,51,650

Illustration 13.

A and B are in partnership sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as on 31/3/2019 is as under–

Liabilities	Amount ₹	Assets	Amount ₹
A's Capitals 88,000		Goodwill	5,000
B's Capitals 1,27,000	2,15,000	Land and Building	30,000
Workmen Compensation Reserve	10000	Investments (Market value ₹ 22,500)	25,000
Investment Fluctuation Reserve	5000	Debtors 47,500	45,000
Employee's Provident Fund	5000	Less Prov. For D/d	
C's Loan	1,50,000	2,500	1,50,000
		Stock	1,25,000
		Bank	1,25,000
		Advertisement Suspense A/c	5,000
	3,85,000		3,85,000

On April 1st 2019, they agreed to take C as a partner on the following conditions–

(i) A will sacrifice 1/3rd of his share with B sacrifices 1/10th from his share in favour of C.

(ii) C's loan will be converted into his capital.

(iii) C brings in 60% of his share of goodwill in cash.

(iv) Land and Building was found undervalued by ₹ 25,000 and Stock was found overvalued by ₹ 35,000.

(v) All debtors are good.

(vi) AB/R of ₹ 7004 discounted with bank was dishonoured, which is to be recorded in the books of account.

(vii) Claim on account of Workmen Compensation is ₹ 5,000.

(viii) An unrecorded accrued income of ₹ 5,000 to be provided for.

(ix) A debtor whose dues of ₹ 25,000 were written off as bad debts, paid ₹ 20,000 in full settlement.

(x) Goodwill is to be valued at 2 years' purchase of super profit of last 3 completed years. Profits for year ended 31st March are as follows–

2017 – ₹ 2,40,000;

2018 – ₹ 4,65,000;

2019 – ₹ 6,90,000

The normal profit is ₹ 3,15,000.

(xi) Capital Accounts of the partners to be readjusted on the basis of their profit-sharing ratio and any excess or deficiency be adjusted by payment or receipt of amount.

Prepare Revaluation Account, Partner's Capital Account and the Balance sheet.

Solution:

Revaluation Account

Particulars		Amount ₹	Particulars	Amount ₹
To Stock A/c		35,000	By Land and Building A/c	25,000
To Gain on Revaluation transferred to–			By Provision for doubtful debt A/c	2,500
A's Capital A/c	10,500		By bad debts recovered A/c	20,000
B's Capital A/c	7000	17,500	By Accrued Income A/c	5,000
		52,500		52,500

Partner's Capital Account

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Goodwill A/c	3,000	3,000	—	By balance b/d	88,000	127000	—
Suspense A/c	2,000	2,000	—	By C's Loan A/c	—	—	150000
To Bank A/c	—	13,000	—	By Premium for Goodwill A/c	36,000	18,000	—
To balance c/d	2,00,000	1,50,000	1,50,000	By C's current A/c	24,000	12,000	—
				By Revaluation A/c (Gain	10,500	7,000	—
				By Workmen compensation Reserve A/c	3,000	2,000	—
				By Investment Fluctuation Reserve A/c	1,500	1,000	—
				By Bank A/c	43,000	—	—
	206000	167000	150000		206000	167000	150000

Balance Sheet as at 1st April 2019

Liabilities	Amount ₹	Assets	Amount ₹
Workmen Compensation Claim	5,000	Land and Building	55,000
Employee's Provident Fund	5,000	Investment	22,500
Capital A/cs		Debtors	
A 2,00,000		(47,500 + 7004)	54,504
B 1,50,000		Stock	1,15,000
C 1,50,000	5,00,000	Bank	2,21,996
		Accrued Income	5,000
		C's Current Account	36,000
	5,10,000		5,10,000

Working Note:

1. Sacrificing share = Old share – New share

$$\text{A's new share} = \frac{3}{5} - \left(\frac{1}{3} \times \frac{3}{5}\right) = \frac{3}{5} - \frac{1}{5} = \frac{2}{5} \text{ or } \frac{4}{10}$$

$$\text{B's new share} = \frac{2}{5} - \frac{1}{10} = \frac{3}{10}$$

C's new share = $\frac{1}{5}+\frac{1}{10}=\frac{3}{10}$

New Profit sharing ratio A : B : C = 4 : 3 : 3

Sacrificing ratio A : B = 2 : 1

2. Calculation of C's share of Goodwill–

Average profit = $\frac{2,40,000+4,65,000+6,90,000}{3}$

= ₹ 4,65,000

Normal Profit = 3,15,000

Super Profit = Average profit – Normal profit

= ₹ 4,65,000 – ₹ 3,15,000 = ₹ 1,50,000

Firm's Goodwill = Super Profit × No. of Year's purchase

= ₹ 1,50,000 × ₹ 3,00,000

Super Profit = Average profit – Normal profit

= ₹ 4,65,000 – ₹ 3,15,000 = ₹ 1,50,000

Firm's Goodwill = Super profit × No. of yrs' purchase

= ₹ 1,50,000 × 2 = ₹ 3,00,000

C's share of goodwill = ₹ 3,00,000 × 3/10 = ₹ 90,000

Journal

Bank A/c (60% 90,000)	Dr.	54,000	
To Premium for Goodwill A/c			54,000
Premium for Goodwill A/c	Dr.	54,000	
To A's Capital A/c			36,000
To B's Capital A/c			18,000
C's Current A/c	Dr.	36,000	
To A's Capital A/c			24,000
To B's Capital A/c			12,000

3. Adjustment of Capital

Total Capital of firm = ₹ 1,50,000 × $\frac{10}{3}$ = ₹ 5,00,000

A's new Capital = ₹ 5,00,000 × $\frac{4}{10}$ = ₹ 2,00,000

B's new Capital = ₹ 5,00,000 × $\frac{3}{10}$ = ₹ 1,50,000

C's Capital = ₹ 1,50,000

4. Dr. Bank A/C Cr.

Particulars	Amount ₹	Particulars	Amount ₹
To balance b/d	1,25,000	By B's Capital A/c	13,000
To Bad debt Recovered A/c	20,000	By dishonoured B/R paid	7,004
To Premium for Goodwill A/c	54,000	By bal. c/d	2,21,996
To A's Capital A/c	43,000		
	2,42,000		2,42,000

Adjusting Capital of New Partner on the Basis of Old Partners.

Illustration 14.

A and B are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their balance sheet was as follows on 1st January, 2019.

Balance Sheet as at 1st January 2019

Liabilities	Amount ₹	Assets	Amount ₹
Sundry Creditors	15,000	Plant	30,000
Capital A/cs		Patents	10,000
A 30,000		Stock	20,000
B 25,000	55,000	Debtors	18,000
General reserve	10,000	Bank	2,000
	80,000		80,000

C is admitted as a partner on the above date on the following terms–

(i) He will pay ₹ 10,000 as goodwill for one-fourth share in the profit of the firm.

(ii) The assets are to be valued as under:

Plant at ₹ 32,000; Stock at ₹ 18,000; Debtors at a book figure less a provision of 5 percent for bad debts.

(iii) It was found that the creditors included a sum of ₹ 1,400 which was not be paid. But it was also, found that there was a liability for compensation to workers amount into ₹ 2,000.

(iv) C was to introduce ₹ 20,000 as capital and the capitals of other partners were to be adjusted in the new profit sharing ratio for this purpose, current accounts were to be opened.

Prepare Revaluation Account, Capital Account and Balance Sheet after C's admission.

Solution:

Revaluation Account

Particulars	Amount ₹	Particulars	Amount ₹
To Stock A/c	2,000	By Plant A/c	2,000
To Provision for Doubtful Debts A/c	900	By Creditors A/c	1,400
To Outstanding liability A/c	2,000	By Capital A/c (loss) :	
		A 3/5 900	1,500
		B 2/5 600	
	4,900		4,900

Capital Account

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Revaluation	900	600	—	By balance b/d	30,000	25,000	—
To Balance c/d	41,100	32,400	20,000	By General Reserve	6,000	4,000	—
				By Bank A/c	—	—	20,000
				By Premium for Goodwill A/c	6,000	4000	
					42,000	33,000	20,000
To Current A/c	42,000	33,000	20,000	By balance b/d	41,000	32,400	20,000
	5,100	8,400					
To Balance c/d	36,000	24,000	20,000				
	41,100	32,400	20,000		41,000	32,400	20,000

Partner's Current A/c

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Balance c/d	5,100	8,400	—	By Capital A/cs	5,100	8,400	—

Working Note: (1) Calculation of New Profit sharing ratio–

Let total share of firm = 1

$$\text{C's share} = \frac{1}{4}$$

$$\text{Remaining share} = 1-\frac{1}{4}=\frac{3}{4}$$

$$\text{A's new share} = \frac{3}{4}\times\frac{3}{5}=\frac{9}{20}$$

B's new share = $\frac{3}{4} \times \frac{2}{5} = \frac{6}{20}$

New Profit sharing ratio = A : B : C

$= \frac{9}{20} : \frac{6}{20} : \frac{1}{4} = 9 : 6 : 5$

(2) New Capital of A and B on the basis of C's Capital–

Total Capital of firms based on

$= 20{,}000 \times \frac{4}{1} =$ ₹ 80,000

therefore, A's Capital = $80{,}000 \times \frac{9}{20}$

B's Capital = $80{,}000 \times \frac{6}{20}$

Balance Sheet (After C/s admission)

As on 1st January 2019

Liabilities	Amount ₹	Assets	Amount ₹
Capital A/cs		Plant	32,000
A 36,000		Patents	10,000
B 24,000		Stock	18,000
C 20,000	80,000	Debtors 18,000	
Current A/cs : R		Less : Provision for D.D	
A 5,100			17,100
B 8,400	13,500	Bank	32,000
Sundry Creditors	13,600		
Outstanding liability	2,000		
	1,09,100		1,09,100

Illustration 15.

Sahaj and Nimish are partners in a firm. They share profit and losses in the ratio 2 : 1. They decided to admit Gauri for 1/3 share. At the time of her admission, Balance sheet of Sahaj and Nimish was as under–

Liabilities	Amount ₹	Assets	Amount ₹
Capital A/cs		Machinery	1,20,000
Sahaj 20,000		Furniture	80,000
Nimish 80,000	2,00,000	Stock	50,000
General Reserve	30,000	Sundry Debtors	30,000
Creditors	30,000	Cash	20,000
Employees Provident Fund	40,000		
	3,00,000		3,00,000

Gauri brought her share of Goodwill in cash and proportionate capical. It was also agreed–

(i) Reduce the value of stock by ₹ 5000.

(ii) Depreciate furniture by 10% and appreciate machinery by 5%

(iii) ₹ 3000 of the debtors proved bad. A provision of 5% was to be created on S.debtors for doubtful debts.

(iv) Goodwill of the firm was valued at ₹ 45000.

Prepare Revaluation A/c, Partner's Capital A/cs and Balance sheet of reconstituted firm.

Solution:

Revaluation Account

Particulars	Amount ₹	Particulars	Amount ₹
To Stock A/c	5,000	By Machinery A/c	6,000
To Furniture	8,000	By Loss transferred to	
To (Sundry Debtors) Bad debts	3,000	Sahay's Capital A/c 7,567	
To provision for bad debts $(30,000 - 3000) \times \frac{5}{100}$	1,350	Nimish's Capital A/c 3,783	11,350
	17,350		17,350

Partners Capital Account

Particulars	Sahaj	Nimish	Gauri	Particulars	Sahaj	Nimish	Gauri
	₹	₹	₹		₹	₹	₹
To Revaluation A/c	7,567	3,783	—	By balance b/d	120000	80000	—
To Balance c/d	142433	91217	116825	By General Reserve A/c	20000	10000	—
				By Premium for Goodwill A/c	10000	5000	—
				By Bank A/c			116825
	150000	95000	116825		150000	95000	116825

Bank A/c

Particulars	Amount ₹	Particulars	Amount ₹
To Gauri's Capital A/c	116825	By balance c/d	131825
To Premium for Goodwill	15000		
	131825		131825

Balance Sheet of New Firm
As on 1st January 2019

Liabilities	Amount ₹	Assets	Amount ₹
Capital A/cs		Machinery	1,26,000
Sahaj 142433		Furniture	72,000
Nimish 91217		Stock	45,000
Gauri 116825	350475	Sundry Debtors	
Employees Provident Fund		30,000	
Creditors	40000	Less Bed debts	
	30000	(3,000)	
		Less Provision for D/d	
		(1,350)	25,650
		Cash	20,000
		Bank	1,31,825
	4,20,475		4,20,475

Working Note:

(1) Gauri's share of Goodwill

$$= 45000 \times \frac{1}{3} = ₹\ 15,000$$

(2) Total adjusted Capital Old

$$= ₹\ 14,2,433 + ₹\ 91,217 = ₹\ 2,33,650$$

Proportionate Capital Gauri (1/3 share)

$$= ₹\ 2,33,652 \times \frac{\cancel{3}}{2} \times \frac{1}{\cancel{3}}$$

$$= ₹\ \frac{2,33,650}{2} = ₹\ 1,16,825$$

PRACTICE EXERCISE

1. On 1-4-2016, A and B entered into partnership for sharing profits in the ratio of 4 : 3. They admitted C as a new partner on 1-4-2018 for 1/5th share which he acquired equally from A and B.

A , B and C earned profit at a higher rate than the Normal Rate of Return for 31-3-2019. Therefore, they decided to expand their business. To meet the requirements of addition at Capital they admitted D as a new partner on 1-4-2019 for 1/7th share in profits which he acquired from A and B in 7 : 3 ratio.

Calculate :

(a) New Profit Sharing Ratio of A : B : C for 2018-19.

(b) New Profit Sharing Ratio of A : B : C : D on D's admission.

2. (a) Vikram and Abhishek are partners sharing profits and Losses in the ratio of 8 : 5. They admit 'Avishi' and decide that the profit sharing ratio between Abhishek and Avishi shall be the same as existing between 'Vikram' and 'Abhishek'.

Calculate New Profit Sharing Ratio and Sacrificing Ratio.

(b) A, B and C are partners in a firm for the profit sharing ratio 4 : 3 : 1. They admitted 'D' as a new partner. 'A', sacrifice 1/3rd of his share in favour of 'D' and 'B', Sacrifice 1/4th from his share in favour of new partner C in neutral.

Calculate New Profit Sharing Ratio.

3. A and B share profits and losses in the ratio of 5 : 3. They admit Cas a partner who pays ₹ 54,000 as premium for goodwill for 1/5th share in the future profits of the firm.

Pass journal entries for goodwill and calculate new profit sharing ratio in each of the following case–

(a) If he acquires his share of profits in the Original ratio of existing partners.