CBSE Quick Revision Notes and Chapter Summary
Class-12 Accountancy
Chapter 5 – Retirement/Death of a Partner

Introduction

Like admission and change in profit sharing ratio, in case of retirement or death also the existing partnership deed comes to an end and the new one comes into existence among the remaining partners. There is not much difference in the accounting treatment at the time of retirement or in the event of death. Retirement means one or more partners may leave the firm but it does not mean the end of the business. The Remaining partners will continue the business. By agreement, a partner may retire and be permitted to withdraw assets equal to, less than, or greater than the amount of his interest in the partnership. The book value of a partner's interest is shown by the credit balance of the partner's capital account.

The balance is computed after all profits or losses have been allocated in accordance with the partnership agreement, and the books closed.

Meaning of Retirement

A Partner may retire in any of the following ways:

a) With the consent of all the partners;
b) In accordance with an express agreement by the partners
c) Where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire

-- Partnership Act 1932 (Section 32 (1))

Partnership at will

Where no provision is made by contract between the partners for the duration of their partnership, or for the determination of their partnership, the partnership is Treated as " Partnership at will"

Amount payable to a Retiring partner

(To be credited to his capital account)

1. Credit Balance of his capital.
2. Credit Balance of his current account (if any)
3. Share ofGoodwil .
4. Share of Reserves or Undistributed profits.
5. His share in the profit revaluation of assets and liabilities.
6. Share in profits upto the date of Retirement/Death.

7. Interest on capital ifinvolved.
8. Salary if any

Deductionfrom the above sum(to be debitedtothe capital account)

1. Debit balance of his current account (if any)
2. Share of Goodwil to be writ en off.
3. Share ofAccumulated loss.
4. Drawings and interest on drawings (if any)
5. Share of loss on account of Revaluation of assets and liabilities.
6. His share of business loss.

AccountingTreatement

1. Calculation of new profit sharing ratio and gaining ratio
2. Treatment of goodwill .
3. Revaluation Account preparation with the adjustment in the respect of unrecorded assets/liabilities.
4. Distribution of reserves and accumulated profits/loss.
5. Ascertainment of share of profits/loss till the date of retirement
6. Adjustment of capital ifrequired
7. Setllement of the Accounts due to Retired partner

Case 1 : Ratio of Remaining partners is known as New profit sharing ratio , in which they will share the future profits. Sometimes it is not given in the question that what will be the new ratio of remaining partners; in such a case it is assumed that the remaining partner will continue to share the profits and losses in the old ratio.

Calculation of New Profit Sharing Ratio

New share of a partner = Old Share of Partner + Acquired Share

Gaining Ratio

Meaning : Share of Retiring partner is acquired by the Remaining partners , Ratio in which they acquire the Retiring partners share is known as Gaining Ratio. In simple words, after the retirement of a partner , his share is distributed by the Remaining partners, ratio in which they distribute the share of Retiring partner, is called Gaining ratio.

Formula : Gaining Ratio = New Ratio - Old Ratio

Steps in the Calculation of Gaining Ratio

1. When New Profit sharing ratio of continuing partners is not given, in such a situation it is assumed that they will share the profit in the old ratio. For example X , Y and Z are partners with Ratio 3 : 2 : 1 . if A retires New Ratio of B and C will be 2 : 1.

2. When New Profit sharing ratio of Continuing Partners is Given , in such a situation we Calculate the Gaining Ratio by using the formula given above
   (Gaining Ratio = New Ratio – Old Ratio)

Difference Between Gaining Ratio and Sacrificing Ratio

Basis	Gaining Ratio	Sacrificing Ratio
Meaning	In this ratio continuing partners get the share from the retiring partner	In this ratio old partners sacrifices their share in favour of new partner
Time of Calculation	It is calculated at the time of	It is calculated when a new partner is admitted
Formula	New Ratio - Old Ratio	Old Ratio – New Ratio
Use	Share of Goodwill of retiring partner is adjusted in this ratio	Share of goodwill of new partner is adjusted in this ratio
Effect	Share of Remaining partners increases	Share of old partners decreases
Proof	Total Gaining share is equal to the old ratio of retired partner	Total sacrifice by old partners will be equal to the Ratio of new partner

Treatment of Goodwill

(a) When capitals are fluctuating

Gainer Partners Capital A/c Dr.
  To Retiring partners capital A/c
(Being retiring partners share of goodwill is adjusted in the gain ratio through the Capital accounts of the partners)

(b) When Capitals are Fixed
  Gainer Partners Current A/c Dr.

To Retiring partners current A/c
(being retiring partners share of goodwill is adjusted in the gain ratio through the Current accounts of the partners)

(c) When goodwill is appearing in Balance Sheet
If Goodwill is existing in the Balance sheet also. Write off this goodwill by doing the following

Journal entry :

All Partners Capital/Current A/c Dr.
To Goodwill A/c

Note : Goodwill given in Balance sheet should be write off in old ratio to all old partners.

Hidden Goodwill

When Goodwill is not given in the question (In adjustment) , In such a case follow these steps to calculate the Hidden Goodwill.

Step 1 : Total Amount paid to Retiring partner

Step 2 : Amount Actually due to the retiring partner

Step 3 : Hidden Goodwill = Step 1 - Step 2

Revaluation of Assets and Re-assessment of liabilities

Preparation of Revaluation account is same as we have done already in the admission of a partner. In the chapter of Admission of a partner , we have distributed all profits and losses only to the old partners. Now we are continue with the same concept , all profits or loss calculated in the revaluation account will be distributed to the all the partners. We do not give any profit to the new partner in case of Admission, but in the case of retirement , the partner who is going out of the firm has played role in earning these profits , that's why revaluation profit will be given to him at the time of his retirement. For this purpose we prepare Revaluation Account to Revalue the asset and to Re-assess the liabilities. Revalution account is also known as Profit and Loss Adjustment Account .

Following journal entries are recorded on Revaluation of assets and Re-assessment of liabilities at the time of retirement of a partner.

1. **For increase in the value of Assets :**

   Asset A/c Dr.
   To Revaluation A/c

2. **For Decrease in the value of Asset :**

   Revaluation A/c Dr.
   To Asset A/c

3. For increase in the value of liabilities :
   Revaluation A/c Dr.
   To Liability A/c

4. For Decrease in the value of liabilities :
   Liability A/c Dr.
   To Revaluation A/c

5. When unrecorded assets are recorded :
   Asset A/c Dr.
   To Revaluation A/c

6. When unrecorded liabilities are recorded :
   Revaluation A/c Dr.
   To Liability A/c

7. When profit on revaluation transferred to old partners :
   Revaluation A/c Dr.
   To Old partners Capital A/c's

8. When loss on revaluation transferred to old partners :
   Old partner's Capital A/c's
   To Revaluation A/c

Revaluation Account

Particulars	Amount	Particulars	Amount
To Decrease in value of asset	xxxxx	By Increase in value of asset	xxxxx

Revaluation Account

Particulars	Amount	Particulars	Amount
To Increase in value of Liability	xxxx	By Decrease in value of Liability	xxxx

Revaluation Account

Particulars	Amount	Particulars	Amount
To unrecorded Liability	xxxx	By Unrecorded Assets	xxxx

Note :

1. **Unrecorded Liabilities are those , which are given in adjustment only and will be considered as a new liability of the firm.**
2. **Unrecorded Assets are those which are given in adjustment only and will be considered as new asset of the firm.**

Complete Proforma of Revaluation Account

Particulars	Amount	Particulars	Amount
To Decrease in value of Asset To Increase in value of liabilities To unrecorded liabilities To profit on revaluation transferred to old partners in old ratio.	xxxx xxxx xxxx xxxx	By Increase in value of asset By decrease in value of liabilities By unrecorded Assets By Loss on revaluation transferred to old partners in old ratio.	xxxx xxxx xxxx xxxx
	xxxx		xxxx

Treatment of Reserve and Accumulated profits

At the time of Retirement of a partner, A firm may have Reserves and accumulated profits or losses. All free Reserves and profits given in the liabilities side should be credited to partners capital accounts or Current Accounts (if capitals are fixed) and all fictitious Assets/Accumulated losses should be debited to the partners capital account or current Account (if capitals are fixed).

Students must remember that these Reserves and profits/losses are only for old partners and should be transferred to them only, in old ratio. Following journal entries are recorded in the books of accounts:

Journal entries

Date	Particulars	L.F	Debit	Credit
	General Reserve Dr. **Profit and Loss Dr.** **Workmen's Compensation Reserve Dr.** **To Old Partners Capital A/c's** **(Being Reserves and Accumulated profits credited to old partners in their old Ratio)** **Old Partner's Capital A/c's Dr.** **To Preliminary Expense** **To Advertisement Suspense** **To Profit and Loss A/c** **To Goodwill** **(Being Accumulated losses and fictitious assets debited to old partners in their old ratio)**			

Preparation of Loan Account

if the total amount is paid to the retiring partner at once , it will affect the financial position of the business. That's why the full amount is not paid to the retiring partner and his due amount is kept in the business as loan. This loan may be paid by the firm in the following ways :

1. **Payment of full amount**
2. **Payment in Equal Installments**
3. **Payment in unequal installments**

Note : When Interest on Loan is not mentioned in the question , it will be taken as 6% p.a.

Adjustment of Partners Capital

When a partner retires , Remaining partners may take decision regarding the adjustment of their capitals , in their profit sharing ratio. Capitals may be adjusted through the cash or current account. If nothing is mentioned in the questions cash account should be used to adjust the difference. In such a case some partner may bring the cash into the business or some partner may withdrew the cash (excess capital) from the business. Students must remember that only capitals of remaining partners will be changed.

Now we will discuss the following cases of adjustment of capitals :

Case 1 : Retiring partner is paid in cash , brought by the remaining partners.

Case 2 : Retiring partner is paid in cash , brought by the remaining partners and effect of Cash/Bank Balance .

Case 3 : Adjustment of Remaining partner's Capital , Without using the Retiring partners Capital or when old partners capital is treated as total capital.

Case 4 : Adjustment Through Current Account.

Steps :

1. Ratio
2. Goodwill
3. Revaluation
4. Distribute reserves and profits/losses
5. Partners capital account

after 5th step :

add closing capital of all partners to calculate the total capital of firm.

(closing capital of continuing partners + closing capital of Retiring partner)

= Total capital of firm

Now distribute this total capital in continuing partners new ratio

Now put the calculated amount as balance c/d in partners capital A/c Dr. side.

Now see the difference of debit and credit side and adjust it through cash A/c.

6. Prepare cash/Bank A/c
7. Prepare Balance Sheet

Note:

After preparing the partners capital account , Calculate Total Capital of the firm and distribute this Total capital in the new ratio of remaining partners and put this new capital as Balance c/d in partners capital account , now adjust the difference through cash.

Total Capital = Closing Capital of All partners (Including Retiring partners closing Capital)

Death of a Partner

Introduction

In the case of death of a partner, Partnership will come to an end immediately. In such a case Reaming partners may continue the business. All amounts due to the Deceased partner will be paid to his legal heirs. The legal heir or executor of the deceased partner may also be added as a partner in the business by the remaining partners.

Who is an Executor?

Executor is the person who is entitled to all rights or amounts due to the deceased partner. The Executor will be entitled to the balance of capital account (Capital Balance , share of profit , Interest on capital , Reserves and Accumulated profits etc. , and he will be debited for Drawings and Interest on drawings)

Amounts to be Credited in the Decease partners capital Account :

i) Balance of Capital
ii) Share in Revaluation Profit
iii) Interest on Capital
iv) Accumulated profits/ Reserves etc.
v) P/L Suspense A/c (Profit)
vi) Commission/ Salary etc.
vii) Any Liability taken over

Amounts to be Debited in the Decease partners capital Account :

i) Accumulated losses
ii) Goodwill A/c
iii) Interest on Drawings
iv) Drawings
v) Any Asset taken over
vi) Revaluation loss (if any)
vii) P/L Suspense A/c (Loss)

Proforma of Deceased partners capital A/c

Particulars	Amount	Assets	Amount
To Accumulated losses	xxxx	By Balance b/d	xxxx
To Goodwill A/c	xxxx	By Revaluation A/c	xxxx
To Interest on Drawings	xxxx	By Interest on Capital	xxxx
To Drawings	xxxx	By Accumulated profits/Reserves	xxxx
To Asset taken over	xxxx	By P/L Suspense A/c (Profit)	xxxx
To Revaluation loss (if any)	xxxx	By Commission/ Salary	xxxx
To P/L Suspense A/c (Loss)	xxxx	By Liability taken over	xxxx
To Executor A/c (Bal.figure)	xxxx		

Calculation of Profits/Loss for the Intervening Period

It is calculated by any one of the two methods given below:-

a) **On Time Basis:** - in this method proportionaly profit for the time period is calculated either on the basis of last year's profit or on the basis of average profits of last few years and then deceased partner's share is calculated based on his share of profits.

b) **On Turnover or Sales Basis-** In this method the profits upto the date of death for the current year are calculated on the basis of current year's sales upto the date of death by using the formula.

Profits for the current year upto the date of death =

(Sales of the current year upto the date of death/total sales of last year) x Profit for

the last year.

Then from this profit the deceased partner's share of profit is calculated.

Journal Entry for the Profit of deceased partner will be :

Profit and Loss Suspense A/c Dr.
To Deceased Partner's Capital/current A/c
(Being amount of profit transferred in deceased partners capital/current account)