COURSE-4

BLOCK 2

Unit-1

RETIREMENT AND DEATH OF A PARTNER

Learning objectives:

The meaning of retirement of a partner; How calculate new profit sharing ratio and gaining ratio; Adjustment relating to goodwill, reserves andundistributed profits at the time of retirement; The need for revaluation of assets and reassessment of liabilities at the time of retirement The revaluation account relating to retirement.

Structure:

1.1Introduction

1.2Meaning of Retirement of a partner. .

1.3Partner's sacrificing ratio

1.4Partner gaining ratio

1.5Details of Goodwill

1.6Problem and Solution

1.1Introduction:

When one or more partners leave the firm and the remaining partners continue to do the business of the firm, it is known as retirement of a partner. Amit, Sunil and Ashu are partners in a firm. Due to some family problems, Ashu wants to leave the firm. The other partners decide to allow him to withdraw from the partnership. Thus, due to some reasons like old age, poor health, strained relations etc., an existing partner may decide to retire from the partnership. Due to retirement, the existing partnership comes to an end and the remaining partners form a new agreement and the partnership firm is reconstituted with new terms and conditions. At the time of retirement the retiring partner's claim is settled. A partner retires either:

(i) With the consent of all partners, or

(ii) As per terms of the agreement; or

(iii) At his or her own will.

The terms and conditions of retirement of a partner are normally provided in the partnership deed. If not, they are agreed upon by the partners at the time of retirement. At the time of retirement the following accounting issues are dealt:

(a) New profit sharing ratio and gaining ratio.

(b) Goodwill
(c) Adjustment of changes in the value of Assets and liabilities
(d) Treatment of reserve and accumulated profits.
(e) Settlement of retiring partners dues,
(f) New capital of the continuing partners.

New profit sharing ratio and gaining ratio:
As soon as a partner retires the profit sharing ratio of the continuing partners get changed. The share of the retiring partner is distributed amongst the continuing partners. In the absence of information, the continuing partners take the retiring partner's share in their profit sharing ratio or in an agreed ratio. The ratio in which retiring partner's share is distributed amongst
Continuing partners is known as gaining ratio. It is
Gaining Ratio = New Ratio – Existing Ratio

A retiring partner, however, continues to be liable to third parties even If the liability Is taken over by the remaining partners (s. 32) Therefore in a deed of retirement it is necessary to provide that In the event of the retiring partner being held liable by a third party, the remaining partners shall indemnify him to that extent, when the liabilities are taken over by the remaining partners.

Insolvency of a partner also causes compulsory retirement of an insolvent partner (s. 35). It is, therefore, generally provided in a deed of partnership when there are more than two partners that the insolvency of any partner will not dissolve the partnership. If a partner retires, unless there is contract.to the contrary, the retiring partner cannot use the firm name, represent himself as carrying on the business of the firm or solicit the customers of the Firm. (s. 36).

Therefore, in a deed of retirement It is generally not necessary to make explicit that the retiring partner shall not do any of these things. But if he is to be restrained from carrying on similar business for a specified period or in a specified area, such condition can be provided in she deed of retirement and it is legal (s. 36(2)).

Sacrificing Ratio vs Gaining Ratio

1. Meaning

It is the ratio in which old partners agree to sacrifice their share of profit in favour of new partners/partner

It is the ratio in which continuing partner acquires the share of profit from outgoing partner/partner

2. Calculation

Sacrificing Ratio = Old Ratio – New Ratio

Gaining Ratio = New Ratio – Old Ratio

3. Time

It is calculated at the time of admission of new partner/partners.

It is calculated at the time of retirement/death of old partner/partners.

4. Objective

It is calculated to ascertain the share of profit and loss given up by the existing partners in favour of new partners/partner.

It is calculated to ascertain the share of profit and loss acquired by the remaining partners (of the new firm in case of retirement) from the retiring or deceased partner.

5. Effect

It reduces the profit share of the existing partners.

It increases the profit share of the remaining partners.

Revaluation account:

It is prepared to record the changes in the value of assets & liabilities at time of admission, retirement, death and change in profit ratio of existing partners. Balance of this account represents the net profit and loss on revaluation. The profit and loss on revaluation is transferred to old partners capital account in the profit sharing ratio.

Retirement of a Partner:

illustration.

A, B and C are three partners sharing profits in the ratio of 5 : 4 : 3 respectively. C retires and the goodwill of the firm is valued at Rs 60,000. Assuming that A and B agree to share future profits in the ratio of 7 : 5 respectively, pass an adjustment entry to credit retiring partner with his share of goodwill. Show calculations clearly.

Journal Dr Cr

Date	Particulars	L.F.	Amount	Amount
	A`s Capital Account -------Dr B`s Capital Account -------Dr To C`s Capital Account ------ (Being retiring partners share of goodwill credited		10000	15

	to his account and the same is debited to remaining partners capital account as per the ratio --------------------------------- -------------------------		5 0 0 0	0 0 0

Working Ratio: value of firm`s goodwill = Rs 60000

C`s share of goodwill =Rs 60000* 3/12 = Rs 15000

A`s gain on C`s retirement 7/12—5/12= 2/12

B`s gain on C`s retirement 5/12---4/12= 1/12

Gaining Ratio A:B = 2: 1.

Hence A`s Capital account will be debited with Rs 15000* 2/3=Rs 10000

B`s capital account will be debited with Rs 15000* 1/3 = Rs 5000.

The Balance Sheet of A, B and C on 31st March, 2011 was as follows:

Liabilities	Rs	Assets	Rs
Capital Accounts		Sundry Assets	1,35,000
A	60,000		
B	40,000		
C	10,000		
Sundry Creditor	25,000		
	1,35,000		1,35,000

On March 31, 2011 A retired. Under the terms of the partnership deed, he was entitled to receive for the year succeeding his retirement one-half of the share of profits which he was receiving at the time of his retirement as a consideration for leaving his capital in the firm as a loan.

On 1st April, 2011 D was admitted a partner and he paid into the firm Rs 30,000 of which Rs 10,000 was for goodwill to be retained in the firm. D was to receive one-fourth share of net profits remaining after charging A's proportion as stated above. All the partners were entitled to interest at the rate of 10% per annum.

The profit for the year ended 31st March, 2012 was Rs 49,000. Prepare the Profit and Loss Appropriation Account showing the distribution of the profit.

Profit and loss appropriation account

Dr For the year ended 31st march ,2012 Cr

Date	Particulars	Rs	Date	Particulars	Rs
	To interest on A`S loan	6,000		By Net Profit	49,000
	To,interest on Capital				
	B 4,500	8,000			
	C 1,500	5,000			
	D 2,000				
	To.				

	A`s loan A/c 1/7th of 35000 (Rs 49,000 — 6,000— 8,000) To share of profit B 11,250 C 11,250 D 7,500	30,000 49,000				49,000

Notes:

(1) Since the problem is silent regarding the profit-sharing ratio, A. B and C must have been equal partners. After retirement, therefore. A is entitled to half of 1/3 or 1/6 share of profits.

(2) It is assumed that /i's share is a charge against profits. Hence, his share is 1/7 of profits after charging interest but before charging A's share.

(3) D gets 1/4 share leaving 3/4 for B and C who are equal partners. Hence, both B and C get 3/8 share of profits each.

Note:

If A's share is to be treated as an appropriation of profits, he will get 1/6 of Rs 35,000 or Rs 5,833.

Illustration: 8

A, B and C sharing profits and losses equally, had been trading for many years. C decided to retire on 31st Dec. 02 on which date the balance sheet of the firm was as follows:

Liabilities	Rs.	Assets	Rs.
Capital account			
A	50,000	Cash	15,000
B	40,000	Debtors	30,000
C	30,000	Stock	25,000
Creditors	40,000	Plant and machinery	50,000
		Land and building	40,000
	1,60,000		1,60,000

The value of the goodwill was agreed at Rs. 40,500. The land and building had increased in value, the value being agreed at Rs. 55,000. Plant and machinery was re-valued at Rs. 44,000 and it was also agreed to provide 5% in respect of debtors. Prepare memorandum revaluation account, Capital account and balance sheet.

[When it desired not to alter the values of assets and liabilities in the books, then a Memorandum Revolution account will be prepared. The first part of this account will be exactly the same as in case of Revolution account but in the second part entries shall be reversed and the profit or loss of this part shall be divided among the continuing partners in their new profit sharing ratio.]

Solution:

Memorandum revolution a/c

Dr.

Cr.

Particulars	Rs.	Particulars	Rs.
To plant machinery	6,000	By land and building	15,000
To provision for bad and Doubtful	1,500		

debts Profit A	7,500		
	15,000		15,000
2,500 B	15,000	Reversal of entries on the debit side	7,500 7,500
2,500 C 2,500 Reversal of entries on the credit side	15,000	Loss transferred to A 3,750 B 3,750	15,000

Capital Account

Particulars	A Rs.	B Rs.	C Rs.	Particulars	A Rs.	B Rs.	C Rs.
To good	20,250-	20,250-	--46,00	By bala	50,000	40,000	30,000

willTo C’sLoan To memorandum RevaluationTo balance	- 3,75042,000	- 3,75032,000	0 ----	nce b/dBy memorandum revaluation a/cBy goodwill	2,50013,500	2,50013,500	2,50013,500
	66,000	56,000	46,000		66,000	56,000	46,000

c / d							

Balance sheet

Liabilities	Rs.	Assets	Rs.
Creditor C's loan Capitals A 42,000 B 32,000	40,000 46,000 74,000	Cash Debtors Stock Plant and Machinery Land and building	15,000 30,000 25,000 50,000 40,000
	1,60,000		1,60,000

Illustration: 9

A, B and C are partners in a firm sharing profit and loss in the ratio of 1/3 : 1/2 : 1/6 respectively. Their balance sheet as on 31st Dec. 03 was as follows

Liabilities		Rs.	Liabilities	Rs.
Sundry creditor Loans payable Reserve fund Capital	 A B C	25,000 15,000 16,000 30,000 40,000 25,000	Building Machinery Furniture Stock Debtors 1 Provision Cash	50,000 40,000 10,000 25,000 17,500 8,500
		1,51,000		1,51,000

C Retires on 31.12.03 subject to the following conditions
(a) A goodwill is created in the book for Rs. 24,000
(b) Machinery to be depreciated by 10%
(c) Furniture to be depreciated by 5%
(d) Stock to be appreciated by 15% and building to be appreciated by 10%
(e) Reserve for doubtful debts to be raised to Rs. 2,000. Prepare necessary ledger accounts and show the Balance sheet of the new firm.

Solution:

Revaluation a/c

Dr. **Cr.**

Particulars	Rs.	Particulars	Rs.
To machinery To furniture To provision for bad debts To profit (transferred) A's capital (2,750 × 1/3) B;s capital (2,750 ×1/2) C;s capital (2,750 × 1/6)	4,000 500 1,500 917 1,375 458	By stock By buildings	3,750 5,000
	8,750		8,750

Capital a/c

Dr. **Cr.**

Particulars	A Rs.	B Rs.	C Rs.	Particulars	A Rs.	B Rs.	C Rs.
To C's loa	--44,250	--61,375	32,125--	By balance	30,0005,33	40,0008,00	25,0002,66

n a/cTo balance a/c				b/dBy reserve fund By goodwill By revaluation (Prof	38,000 917	012,000 1,375	74,000 458
	44,250	61,375	32,125		44,250	61,375	32,125
					44,250	61,375	--

				it) By balance b/d			

Balance sheet of A and B as on 31.12.03

Liabilities	Rs.	Assets	Rs.
Capital Accounts A B C's loan Sundry creditor Loan Payable	44,250 61,375 32,125 25,000 15,000	Goodwill Building 50,000 Add: 10% appropriation 5,000 Machinery 40,000 Less: 10% Depreciation 4,000 Furniture 10,000 Less: 5% Depreciation 500 Stock 25,000 Add: 15% Appreciation 3,700 Debtors 18,000 Less: Provision 2,000 Cash	24,000 55,000 36,000 9,500 28,750 16,000 8.500
	1,77,750		1,77,750

Calculation of total amount due to a retiring partner

The total amount due to a retiring partner may include

(i) Capital on the date of last balance sheet

(ii) Interest on salary if any payable to him.

(iii) Share of profit or loss to the date of retirement

(iv) Share in the goodwill of the firm

(v) Share in the profit or loss on revaluation of assets and liabilities

(vi) Share in the general reserve or profit and loss account appearing in the balance sheet.

The total amount calculated will be transferred to the retiring partner's loan account. The entry will be:

Retiring partner's capital a/c ....Dr.

To retiring partner's loan a/c

PARTNERSHIP ACCOUNTS: DEATH OF A PARTNER

Learning objectives:

After studying this lesson, you will be able to know: what happens after the death of a partner in partnership firm, representative of the deceased partner is entitlement for which items. How do you calculate the share of profit for deceased partner? How deceased executor account is settled.

Structure:

Introduction

Calculation of share of profit up to the date of death

Deceased partner`s share of goodwill

Accounting treatment at the time of death of a partner

Settlement of deceased executor account

Problem &solution

Introduction:

When a partner dies, subject to any contract to the contrary, partnership is dissolved. Section 42 of the Indian Partnership Act, 1932 ("**Act**") provides for dissolution of partnership on occurrence of certain contingencies which includes 'death of the partner' as one of those contingencies. Death of a partner dissolves the partnership and the rights of the representatives of the deceased partner would depend on the provisions of the partnership deed. Usually, the surviving partners carry on the business, purchasing the share of the deceased partner after determining the amount due to him and then treating it as a loan to the firm. The executors of the deceased partner would be entitled to the decreased partner's share of profits arising after the last closing up of accounts to the date of accounts death.

When an informal partnership exists without formal documentation, the partnership dissolves upon the death of a partner. The partnership itself may not die, but changes into a different partnership. When a partnership agreement exists, the agreement generally supersedes the default state statutes. The agreement may have provisions allowing for the continuation of the general partnership after the death of a general partner. If it does, it must specify what happens to the partnership interests of the deceased partner and if the partner or his heir can sell his interests to someone else. The agreement must also include procedures on how to pay out the deceased partner’s capital, remove his name from all partnership materials and contracts, and how to pay out the deceased partner’s share.

On the death of a partner, the accounting treatment regarding goodwill, revaluation of assets and reassessment of liabilities, accumulated reserves and undistributed profit are similar to that of the retirement of a partner, When the partner dies the amount payable to him/her is paid to his/her legal representatives. The representatives are entitled to the followings :

(a) The amount standing to the credit to the capital account of the deceased partner

(b) Interest on capital, if provided in the partnership deed upto the date of death:

(c) Share of goodwill of the firm;

(d) Share of undistributed profit or reserves;

(e) Share of profit on the revaluation of assets and liabilities;

(f) Share of profit upto the date of death;

(g) Share of Joint Life Policy.

The following amounts are debited to the account of the deceased partner’s legal representatives: (i) Drawings

(ii) Interest on drawings

(iii) Share of loss on the revaluation of assets and liabilities;

(iv) Share of loss that have occurred till the date of his/her death.

The above adjustments are made in the capital account of the deceased partner and then the balance in the capital account is transferred to an account opened in the name of his/her executor. The payment of the amount of the deceased partner depends on the agreement. In the absence of an agreement, the legal representative of a deceased partner is entitled to interest @ 6% p.a. on the amount due from the date of death till the date of final paymentU/S 37.

Calculation of Share of Profit Upto the Date of Death

A retirement is usually arranged to be taken place at the end of an accounting year whereas, death may take place on a date some time after the date of which the last balance sheet and accounts were made up. Hence, the representatives of the deceased partner will be entitled to his share of profits accrued upto the date of death. To avoid the necessity of preparing final accounts till the date of death, it is frequently provided in the partnership deed that in the event of the death of a partner his share of the accruing profits upto the date of death is to be arrived at on the basis of either profits of the last year/ last few years or on the basis of turnover. In some cases, it is agreed to wait until the next annual accounts are prepared.

We have seen that the deceased partner's share of profit earned till the date of his death has to be given to his executors. The correct amount of profit earned can be calculated only if the books are closed till the date of death. This may be inconvenient. Profit may, therefore, be calculated by any of the following two methods.

(i) On the basis of time.

(ii) On the basis of turnover

(i) **On the basis of time :** If the time basis is used, the profit will be assumed to accrue evenly over the year. According to this method, profit may be estimated by any of the following two methods :

(a) On the basis of last year's profit : The proportionate profit of the firm is computed from the last accounting period to the date of death on the basis of profit earned during last year. Thereafter, share of profit of deceased partner is computed.

Illustration : 1. R dies on 31st March, 2002 in partnership of P, Q and R sharing in the ratio of 2 : 2 : 1. The profit for the year ending 31st March, 2016 was Rs.36,000. Calculate R's share of profit.

Solution :

(i) Last year's Profit = Rs.36,000

(ii) Period Between last final accounts to the date of C's death =

January 1, 2002 to March 31, 2002 = 3 months.

(iii) 3 months' profit of the firm on the basis of last year's profit.

$$= \frac{36,000}{12} \times 3 = \text{Rs.}9,000$$

(iv) C's Share of Profit = $9,000 \times \frac{1}{5} = \text{Rs..}1,800$

(b) **On the basis of average profit** : In certain cases, partners may agree to calculate deceased partner's share of profit on the basis of average profit. This is worked out as under :

i) Take the total profits of the required number of past years;

(ii) Calculate the average profit (i.e., Total profit + No. of years)

(iii) Reduce average profit for the period upto date of death,

(iv) Find out the share of the deceased partner.

Illustration 2. Sachin, Sourav and Rahul were partners in a firm. Sourav died on 28th February, 2002. Sourav's share of profit from the closure of the last accounting year till the date of death was to be calculated on the basis of the average of three completed years profits before death. Profits for 2008, 2009 and 2010 were Rs.70,000, Rs.80,000 and Rs.90,000 respectively. The firm closes its books on 31st March every year.

Calculate Sourav's share of profit till the date of her death.

Solution :

(i) Total Profits = Rs.70,000 + Rs.80,000 + Rs.90,000 = Rs.2,40,000

(ii) Average Profit = $\frac{\text{Total Profits}}{\text{No. of Years}} = \times \frac{2{,}40{,}000}{3}$ = Rs.80,000

(iii) Two months' profit (1st Jan. 2002 to 28th Feb. 2002)

(iv) Sourav's share of profit till the date of her death

$$13{,}333 \times \frac{1}{3} = Rs.4{,}444$$

Note : In the absence of an agreement, partners will share profits equally.

(ii) On the basis of turnover (or sales) : If profits till the date of death is to be calculated on the basis of turnover, on such arrangement last year's profit and sales are given together with the sale of the current year upto the date of death of the partner. The profit is ascertained proportionately and the share of deceased partner is calculated.

Illustration 3.M, N and S are partners in the ratio of 4 : 3 : 3. N dies on 20th Sept., 2012. The sales and profit during the year 2000 Rs.1,20,000/- and Rs.20,000 respectively. The sale upto 20thsEPT. 2012 during current year amounted to rs.30,000. Calculate N's share of profit.

Solution

If sales is worth Rs.1,20,000, the profit = Rs.20,000

If sale sis worth Rs. 1, the profit = $\frac{20{,}000}{1{,}20{,}000}$

If sales is worth Rs. 30,000, the profit =

$\frac{20{,}000}{1{,}20{,}000}$ x 30,000 = Rs.5,000

N's share of profit = Rs.5,000 x $\frac{3}{10}$ = Rs.1,500

Accounting Treatment of outgoing Partner's Share in Profits

The outgoing partner's share in the profits may be readjusted in either of the following ways :-

i.	In case of profit	Profit & Loss Suspense A/c Dr. (Share of Profit)
		To Outgoing Partner's Capital A/c
ii.	In case of Loss	Outgoing Partner's Capital A/c Dr. (Share of Profit) To Profit & Loss Suspense A/c

Illustration 4. A, B and C are partners in a firm sharing profits as 4 : 3 : 2 C died on 31.03.2002. Estimated profit upto date of death is Rs.18,000. C's share in the firm is purchased by A and B in their profit sharing ratio. Give the necessary journal entry to record the C's share of profit to the date of death.

Solution

Journal

	Profit & Loss Suspense A/c To C's Dr. (For deceased partner's share of profit transferred to his capital (A/c)		Rs.4,000	Rs.4,000

Note : (1) C's share of profit = Rs.18,000 x 2/9 = Rs.4,000

(2) This entry is appropriate only when the new profit sharing ration of continuing partners does not differ from their old profit sharing ratio.

2. **Through capital transfer** : This method is used only, when the new profit sharing ration of continuing partners differ from their old profit sharing ratio. In this case, the following entries will be passed :

(i) (ii)	In case of Profit In case of Loss	Gaining Partner's Capital A/c To Outgoing Partner's Capital A/c Outgoing Partner's /Capital A/c	Dr. (Gaining Ratio) (Share of Profit) Dr. (Share of loss) (Gaining Raio)

Note : If a partner is retired during the year, the above same rules will be applicable for calculating his share of profit.

Illustration 5. (Accounting treatment of deceased partner's share of profit) A, B and C are partners sharing profits and losses in the ratio of 3 : 2 : 1 respectively. B died on 31st March, 2002. The profits from 01.01.2002 to 31.03.2002 amounted Rs.45,000. A and C decided to share the future profits the B's share of profit to the date of death.

Solution

Journal **Dr** **Cr**

	A's Capital A/c Dr. C's Capital A/c Dr. To B's Capital A/c (For B's share of profit to the date of death adjusted in the capital accounts of A & C in their gaining ration 3 :7)		Rs.4,500 Rs.10,500	Rs.15,000

Note : (1) B's share of profit = 45,000 x 2/6 = Rs.15,000

(2) Gaining Ratio = New Ratio – Old Ratio

$$A = \frac{3}{5} - \frac{3}{6} = \frac{18-15}{30} = \frac{3}{30}$$

$$C = \frac{2}{5} - \frac{1}{6} = \frac{12 - 5}{30} = \frac{7}{30}$$

Gaining ratio between A and C = 3 : 7

(3) In case the new profit sharing ratio of continuing partners differ from their old sharing ratio, outgoing partner's share of profit must be adjusted through the capital transfer.

Accounting Treatment of Deceased Partner's Share of Goodwill

The executors of the deceased partners are also entitled to receive the share of goodwill the firm. Goodwill for this purpose will be valued according to the provisions of partnership deed. The amount of deceased partner's share of good will ascertained will be credited to his capital account and will be debited to gaining partner's capital account in the gaining ratio.

Illustration 6. Ram Mohan an Sohan were partners in a firm sharing profits in the ratio of 2 : 2 : 1. On 28.02.2002, Mohan die and the new profit sharing profits in the ratio of Ram and Sohan was equal. On Mohan's death, the goodwill on Mohan's death for the treatment of goodwill without opening goodwill account.

Solution

(i) Calculation of Gaining Raio :

Gaining Raio = New Ratio – Old Ratio

$$\text{Ram} = \frac{1}{2} - \frac{2}{5} = \frac{5 - 4}{10} = \frac{1}{10}$$

$$\text{Sohan} = \frac{1}{2} - \frac{1}{5} = \frac{5 - 2}{10} = \frac{3}{10}$$

Gaining ratio between Ram &Sohan = 1 : 3

(ii) Mohan's Share of Goodwill = Rs. 1,50,000 x $\frac{2}{5}$ = Rs.60,000

(iii) Journals

	Ram's Capital A/c (1/4 of Rs.60,000)	Dr.		Rs.15,000	Rs.15,000
	Sohan;s Capital A/c (3/4 of Rs.60,000) To Mohan's	Dr.		Rs.45,000	Rs.60,000

	Capital A/c			
	[For Mohan's share of goodwill adjusted to continuing partners' capital accounts in their gaining ratio 1:3].			

Proforma of Capital Account

Let us now see how deceased partner's capital will appear :

Deceased Partner's Capital Account

Dr. **Cr.**

To Accumulated Losses (Share in such losses)	Rs.	By Balance b/d	Rs.
To Revaluation A/c (Share of loss)	---	By Interest on Capital A/c	----
To Good will A/c (Share of deceased partner in goodwill written off)	---	By Salary and Commission A/c	-----
	---	By Accumulated Profit (Share in such profit)	----
To Drawings A/c	----	By Gaining Partner's Capital A/c (Share of goodwill)	----
To Interest of Drawings A/c	----	By Joint Life Policy A/c (Share of J.L.P)	----
To P/L Suspense A/c (Share of loss)	----	By Profit and Loss Suspense A/c (Share of Profit)	----
To P/L Suspense A/c (Share of Loss)	----	By Gaining Parnter's Capital A/c (Share of Profit)	----

To Gaining Partner Capital A/c (Share of Loss)	----	(Share in profits till death)	----
To Deceased Partner Executor's A/c (Balancing Figure)	----		
Total	**----**	**Total**	**----**

Accounting Treatment at the time of Death of a Partner

As discussed earlier on the death of a partner, the account of deceased partner is maintained in the same way as is maintained on the retirement of a partner. But the only difference is that the amount due to a deceased partner as revealed by his capital account is transferred to his executor's account. The journal entry will be :

Deceased Partner's Capital A/c ---------------------Dr

To Deceased partner`s executors Account --------

(For amount due to deceased partner transferred to his executor's a/c)

Illustration 7: A, B and C were partners in a firm sharing profits in the ratio of 3 :2 :1. The balance, sheet as on 31.03.2003 was as follows :-

Liabilities	**Rs.**	**Assets**	**Rs.**
Creditors	4,000	Building	20,000
Reserve	6,000	Plant & Machinery	16,000
A's Capital	24,000	Stock	5,100
B's Capital	12,000	Debtors	6,000
C's Capital	8,000	Cash of Bank	6,900
	54,000		**54,000**

A died on 30.09.2003. Under the Partnership agreement, the executors of a deceased partner were entitled to :-

(a) Amount standing to the credit of partner's capital account.
(b) Interest on capital at 12% p.a.
(c) Share of goodwill on the basis of four years purchase of last three years average profit.
(d) Share of profit from the closing of the last financial year to the date of death on the basis of last year's profit. Profits for the year 2001, 2002 and 2003 were Rs.8,000, 12,000 and Rs.7,000 respectively.

Prepare A's capital account to be rendered to his executors.

Solution

A's Capital Account

To A's Executor's A/c	Rs.48,190	By Balance b/d	24,000
		By General Reserve A/c	3,000
		By Interest on Capital A/c	1,440
		By B's Capital A/c (Good will)	12,000
		By Profit & Loss Suspense A/c	6,000
			1,750
	48,190		48,190

Note : (1) General Reserve = Rs.6,000 $\times \frac{3}{6}$ = Rs.3,000

(2) Interest on Capital = Rs. 24,000 $\times \frac{12}{100} \times \frac{6}{12}$ = Rs.1,440

(3) A's share of Goodwill = $\frac{Rs.27,000}{3} \times 4 \times \frac{3}{6}$ = Rs.18,000 will be adjusted between B and C in the gaining ratio of 2 : 1.

(4) A's share of profit = Rs. 7,000 $\times \frac{6}{12} \times \frac{3}{6}$ = Rs.1,750

Settlement of Deceased Executors Account

Deceased partner's executors account will be settled as per the agreement between the firm and executor's of the deceased partner.

(a) When full amount is paid in cash/ cheque, the following entry is recorded :

Deceased Partner's Executor's A/c : Dr.

To Cash / Bank A/c.

(b) When the settlement is made in instalments the following entries are recorded :

(i) For interest due to Deceased Partner Executor's A/c

Interest on Deceased Partner Executor's A/c

To Deceased Partner's Executor's A/c

(ii) When payment is made in instalment :

Deceased Partner's Executor's A/c Dr.

To Cash/ Bank A/c

To amount due to executor's of deceased partner is paid off immediately or is paid instalments with or without interest as per agreement. In the absence of an agreement in the paid off or a share of the profit which has been earned by the firm using the amount due to the as per Section 37 of the partnership Act.

Illustration 8. A, B and C were Partners sharing profits in the ratio of 2 : 1 : 1 individual policies of Rs.20,000, Rs.10,000 on the lives of A, B and C respectively were taken and premium paid was charged Profit & Loss A/c which is prepared on 31st March each year.

C died on 31st March, 2009. On this date surrender values are 20% of the amount of police. Under the partnership deed, the executors of deceased partner were entitled to :

(i) His capital according to the last balance sheet ;
(ii) Interest on the above capital @9% p.a. till the date of death ;
(iii) His share of profit to the date of death, calculated on the basis of last year's profit;
(iv) His share of life insurance policies;
(v) Interest on drawings is to be charged at an average rate of 3%

C's capital as per balance sheet on 31st march, 2008 was Rs.60,000. During the year withdrew Rs.8,000 till his death. Last year's profit was Rs.40,000.

Prepare C's Capital Account.

Solution

Dr. **C's Capital Account**

To Drawings A/c	Rs. 8,000	By Balance b/d (1.1.99)	60,000
To Interest on Drawings A/c (8000 x 3/100)	Rs.240.00	By Interest on Capital A/c (60,000 x 9/100 x 3/12)	1,350.00
To C's Executor's A/c (Amount Payable)	59,610.00	By P/L Suspense A/c (40,000 x 3/12 x ¼)	2,500.00
		By Joint Life Police A/c	4,000.00
	67,850.00		**67,850.00**

Note : (1) Calculation of C's share in life policies.

Surrender value of A's policy = Rs.20,000 x 20/100 = 4,000.00

Surrender value of B's policy = Rs.10,000 x 20/100 = 2,000.00

Full sum assured of C's policy received due to his death = 10,000.00

Total valuation of life policies = 16,000.00

C's share in life policies = Rs.16,000 x ¼ = Rs. 4,000

Sum up: A partner or partners may retire from the firm due to the various reasons like old age, better opportunity, ill health, conflict between the partners and so on. The retirement of a partner extinguishes his interest in the Partnership firm and this leads to dissolution of the firm or reconstitution of the Partnership. A partner, who goes out of a firm, is called retiring partner or outgoing partner. Causes for the retirement may be that a retiring partner may be too old or he may have better opportunity in a different line or he may dislike the co-partners' attitude or any other reasons

Keyword: Deceased Partner, Executor, Goodwill, New ratio, Old ratio and Gaining ratio.

Self assessmentquestions :

Problem: P, R and S are is partnership sharing profits 4 : 3 : 1 respectively. It is provided under the partnership deed that on the death of a partner, his share of goodwill is to be valued at one half of the net profits credited to his account during the last 4 completed years (books of accounts are closed on 31st December).

R died on 1st January 2002. The firm's profits for the last 4 years were as follows :-

1998	Profits	Rs.1,20,000.00
1999	Profits	Rs.60,000.00
2000	Losses	Rs.20,000.00
2001	Profits	Rs.80,000.00

(i) Determine the amount that should be credited to R in respect of his share of goodwill.

(ii) Pass a journal entry for adjustment of goodwill assuming that profits sharing ratio between P and S in future will be 3:2. Show your working clearly.

Problem:P, Q are R were partners sharing profits in the ratio of 5 : 3 : 2 respectively.

On 31st March, 2010 their balance sheet stood as follows:

Balance Sheet as at 31st March 2016

Liabilities	**Rs**	**Assets**	**Rs**
A`s Capital	**5,00,000**	**Machinery**	**6,30,000**
B`s Capital	**3,00,000**	**Furniture**	**2,60,000**
C`S Capital	**2,00,000**	**Stock**	**4,00,000**
	4,50,000	**Debtors**	**1,80,000**
Creditors	**20,000**		
	14,70,00		**14,70,00**

Bank overdraft	**0**		**0**

Q retired as on the abovementioned date. It was agreed that:

(i) The firm's goodwill was worth Rs 250 thousand and Q was entitled to the credit for his share of goodwill

(ii) P and R would continue to be partners but would share profits in future in the ratio of 7 : 3 respectively, and

(iii) The amount due to Q would be paid immediately and for this purpose P and R would bring in cash in such a manner that the total capital of the reconstituted firm was Rs 1,000 thousand and the capital accounts of the partners were in their new profit sharing ratio.

Assuming that all the above-mentioned conditions were fulfilled pass journal entries in the boobs of the firm for all the transactions. Also, prepare the capital accounts of all the partners. **Problem:**L, M and N were partners sharing profits and losses in the ratio of 2 : 2 : 1 respectively. On 1st April, 2012 L retired when his capital account showed a credit balance of Rs 8,00,000. In the ledger, goodwill account appeared at Rs 1,00,000 but the partners agreed that the fair value of firm's goodwill on the abovementioned date was Rs 4,75,000.

Apart from capital of Rs 8,00,000, the retiring partner's share of goodwill was also to be paid. Assuming that M and N continue to share profits in ratio of 2 : 1 respectively and L's capital account is immediately settled in cash, pass journal entries for all the transactions relating to partner's retirement.

Problem: C, D and E were partners sharing profits in the proportions of $^1/_2$: $^1/_3$:$^1/_6$ respectively.

The Balance sheet of the firm on 31st March, 2012 was as follows:

Liabilities	**Rs**	**Assets**	**Rs**
Capital Accounts		**Building**	**9,00,000**
	8,00,000	**Machinery**	**7,00,000**
C	**6,00,000**	**Furniture**	**160,000**
D	**5,00,000**	**Stock**	**5,00,000**

E	**3,80,000**	**Debtors**	**3,10,000**
Creditors	**1,00,000**	**Bank**	**50,000**
Bills Payble	**2,40,000**		**26,20,000**
Reserve	**26,20,000**		

D retired on that date subject to the following conditions:

(1) The goodwill of the firm to be valued at Rs 180 thousand and d be given credit for his share of goodwill.

(2) Plant to be depreciated by 10% and furniture by 15%.

(3) Stock to be appreciated by 20% and Buildings by 10%.

(4) The Provision for Bad Debts to be increased by Rs 20 thousand; and

(5) Liability for workmen's compensation to the extent of Rs 16 thousand to be brought into account. It was agreed that c and e will share profits in future in the ratio of C 3/5 and e 2/5.

Pass journal entries, prepare revaluation account, capital accounts and balance sheet (1) when the change in the values is to be recorded in the books, and (2) when the assets and liabilities are to continue to appear at their old figures.

Model questions:

1.State the treatment of goodwill on retirement of a partner.

2.Distinguish between sacrificing ratio and gearing ratio.

3.What are the procedures for calculation of profit up to death?

4.What is the treatment of deceased partner`s share of goodwill.

5.What is the accounting treatment at the time of death of a partner?

6. What are the procedures of deceased executors account?

Further Readings:

1. Modern Accountancy: Hanif and Mukherjee, volume –I, Tata Mcgrewhill.

2. Higher secondary Accounting: Biswal and Sharma.

3. Financial Accounting: P.C. Tulsian, Pearson.

4. An Introduction to Accountancy: S.N. Maheshwari, S.K. Maheshwari. Vikas.