1. Details of Module and its structure

Module Detail	
Subject Name	Accountancy
Course Name	Accountancy 03 (Class XII, Semester - 1)
Module Name/Title	Reconstitution of Partnership Firm-Admission of a Partner – Part 4
Module Id	leac_10304
Pre-requisites	Knowledge about Partnership form of Business Organisation.
Objectives	After going through this lesson, the learners will be able to understand recording of business transactions in the journal. • Accounting Treatment of Hidden Goodwill • Treatment of Accumulated Profits / Losses • Revaluation of Assets & Liabilities
Keywords	Hidden Goodwill, Accumulated Profits / Losses, Revaluation of Assets & Liabilities

2. Development Team

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Table of Contents:

1. Hidden Goodwill

Sometimes, the value of Goodwill is hidden in the question. In such cases, the amount of goodwill is calculated on the basis of total capital of the firm and the profit sharing ratio of the partners. To understand, let's take an example.

For example, A and B are partners with capitals of Rs.30,000 and Rs.20,000 respectively. They admit C as a partner with 1/4th share. C is to contribute Rs.24,000 as his capital. In such a case, the total capital of the firm, based on C's share will be Rs.24,000 × 4/1 = Rs.96,000. But the combined capital of A, B and C is only Rs.74,000 (Rs.30,000 + Rs.20,000 + Rs.24,000). As such the value of Goodwill of the firm should be Rs.22,000[Rs.96,000 Rs.74,000]. This method is used, when the new partner is unable to bring his share of goodwill in cash.

Example

A and B are partners in a firm sharing profits in the ratio of 3:2. Their capitals were Rs. 80,000 and Rs. 50,000 respectively. They admitted C on Jan. 1, 2020 as a new partner for 1/5 share in the future profits. C brought Rs.60,000 as his capital. Calculate the value of goodwill of the firm and record necessary journal entries on C admission.

Solution

Value of Firm's Goodwill

C's capital = Rs. 60,000 and C's share =1/5

Based on this Data, Total capital of new firm = 5 × Rs.60,000 = Rs. 3,00,000

A+B+C Capital = Rs.80,000 + Rs. 50,000 + Rs.60,000= Rs.1,90,000

Therefore, **Goodwill of the firm = Rs.1,10,000 (Rs. 3,00,000 – Rs.1,90,000)**

C's share =1/5 x 1,10,000= 22,000

1. Bank A/c Dr. 60,000

To C's Capital A/c 60,000

(Cash brought by C for his capital)

2. Goodwill A/c Dr. 1,10,000

To A's Capital A/c 66,000

To B's Capital A/c 44,000
(Credit given for goodwill to A and B on C's admission)

Alternatively, if goodwill account is not to be raised, the entry no. 2 shall be as follows:

C's Capital A/c Dr. 22,000

To A's Capital A/c 13,200

To B's Capital A/c 8,800

2. Adjustment for Accumulated Profits and Losses on Admission of New Partner

Sometimes a firm may have **accumulated profits** (existing in the Balance sheet) . It means they are not yet transferred to capital accounts of the partners. These are in the form of general reserve, reserve fund and/or Profit and Loss Account (Credit balance).

Obviously, these Profits/Reserves are due to the Efforts of Old Partners. So, the new partner is not entitled to have any share in such accumulated profits. So, very correctly, these are distributed among the old partners in their capital accounts in **old profit sharing ratio**.

General Reserve A/c	Dr.
Reserve Fund A/c	Dr.
Profit and Loss A/c	Dr.
Investment Fluctuation Reserve A/c	**Dr.**
Contingency Reserve A/c	Dr.
Workmen Compensation Reserve A/c	Dr.
To Old Partners' Capital A/c	

(Being distribution of accumulated profits among old partners in old ratio)

Similarly, if there are some **accumulated losses** in the form of a debit balance of profit and loss account appearing in the balance sheet of the firm, the same are transferred to the Debit side of old partners' capital accounts in **old ratio.**

Old Partners' Capital A/c Dr.

To Profit and Loss A/c

To Advertisement Suspense A/c

To Deferred Revenue Expenditure A/c

(Being distribution of undistributed losses among old partners in old ratio))

Example

X and Y are partners in a firm sharing profits in the ratio of 4:1. They admit Z as a new partner. On that date there was a balance of Rs. 20,000 in general reserve and a debit balance of Rs. 10,000in the profit and loss account of the firm.

Pass necessary journal entries regarding adjustment of accumulated profit or loss.

Solution

General Reserve A/c Dr. 20,000

To X’s capital A/c 16,000

To Y’s capital A/c 4,000

(General Reserve balance transferred to the capital account of X and Y on Z’s admission)

X’s Capital A/c Dr. 8,000

Y’s Capital A/c Dr. 2,000

To Profit and Loss A/c 10,000

(Debit balance of Profit and Loss A/c transferred to old partners’ capital accounts)

3. Our Next topic is Revaluation of Assets and Reassessment of Liabilities

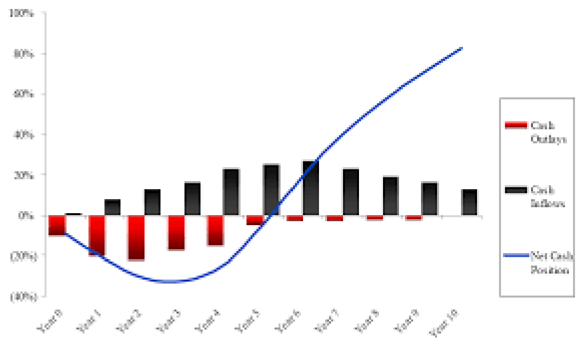

Image 6 (Downward/ Upward)

At the time of admission of a new partner, it is always desirable to ascertain whether the assets of the firm are shown in books at their current values. In case the assets are overstated or understated, these are revalued.

Similarly, assessment of the liabilities is also done so that these are brought in the books at their correct values.

There may also be some unrecorded assets and liabilities of the firm. These also have to be brought into the books of the firm.

For this purpose, the firm has to prepare the Revaluation Account. All the gains or losses on revaluation of each asset and liability is transferred to this account and finally in the end PROFIT or LOSS on REVALUATION is transferred to the capital accounts of the old partners in their old profit sharing ratio.

Moreover, It should not be given to the new partner as it is due to efforts of the old partners.

Revaluation account is credited with Gains, Increase in the value of asset and Decrease in value of liabilities and

It is **debited with Losses, like** Decrease in the value of assets and Increase in its liabilities.

Similarly, unrecorded assets are credited (Being Gain) and unrecorded liabilities are debited (Being Losses)

The journal entries for Revaluation of Assets and Reassessment of Liabilities are:

(i) **For increase in the value of an asset**

Asset A/c Dr.

To Revaluation A/c (Gain)

(ii**) For reduction in the value of an asset**

Revaluation A/c Dr.

To Asset A/c (Loss)

(iii) **For appreciation in the amount of a liability**

Revaluation A/c Dr.

To Liability A/c (Loss)

(iv) **For reduction in the amount of a liability**

Liability A/c Dr.

To Revaluation A/c (Gain)

(v) **For an unrecorded asset realised**

Cash A/c Dr.

To Revaluation A/c (Gain)

(vi) **For an unrecorded liability being paid**

Revaluation A/c Dr.

To Cash A/c (Loss)

(vii) **For transfer of gain on Revaluation if credit balance**

Revaluation A/c Dr.

To Old Partners Capital A/cs (Old ratio)

(viii) **For transferring loss on revaluation**

Old partner's Capital A/cs Dr.(Old ratio)

To Revaluation A/c

Format of Revaluation Account :-

Particulars	***Rs.***	**Particulars**	Rs.
To Increase in liabilities	XXX	By Decrease in liabilities	XXX
To Decrease in assets	XXX	By Increase in assets	XXX
To Unrecorded liabilities	XXX	By Unrecorded assets	XXX
To Profit(old partners)		By Loss (old Partners)	

Q1. The following was the Balance Sheet of Anurag and Bhawna, who were sharing profits in the ratio of 2/3 and 1/3 on 31st December,2020:

	Rs.		**Rs.**
Creditors	65,900	Cash	1,200
Capitals :		Sundry Debtors	9,700
Anurag	30,000	Stock	20,000
Bhawna	20,000	Plant & Mach.	35,000
		Building	50,000
	1,15,900		1,15,900

They agreed to admit Monika into partnership on the following terms:

i) Monika was to be given 1/3 share in profits, and was to bring Rs.15,000 as capital and Rs.6,000 as share of goodwil.

ii)Thatthevalueofstockandplant&machineryweretobereducedby10%.

iii)That a provision of 5% was to be created for doubtful debts.

iv)That the building account was to be appreciated by20%.

v)Investments Rs.1400 (not mentioned in the Balance Sheet) were to be taken into account.

vi)That the amount of goodwill was to be withdrawn by the old partners.

Prepare **a)** Revaluation Account **b**) Capital accounts **c)** Balance sheet after admission

Solution

First of all we will make Revaluation account. All Losses will be debited & Gains will be credited. Let us start with Point no.1. Monika will bring 21,000, Rs. 15,000 for Capital and Rs. 6,000 for Premium for Goodwill. Monika Capital will increase by 15,000 and 6,000 Premium will be distributed among Sacrificing (Old) Partners.

As regard Point no. 2, Stock, It is reduced by 10% of 20,000= Rs. 2,000. This will be debited to Revaluation Account, being a loss and similar will be the case with Plant & Machinery, reduced by 10%= Rs. 3,500

And Similarly for Point no.3, Prov. For doubtful debts will be made at 5% of 9,700= 485. All of them are being debited to Revaluation account, being a nominal account where all losses are debited and gains are credited.

Coming to Point no.4, Buildings will be increased by 20% of 50,000= Rs. 10,000.

And in Point no. 5, Unrecorded Investment, being a Gain will be recorded on the credit side of Revaluation Account, being a Gain.

As regard Point no. 6, Goodwill will be withdrawn by Partners, on the Debit side of their Capital Accounts & Cash Account, Credit side.

Now, the final picture of Revaluation account, Capital account & Balance sheet will be like this:

Revaluation Account

Particulars	***Rs.***	**Particulars**	Rs.
To Stock To Plant & Machinery	2,000 3,500	By Building By Investment	10,000 1.400

To Prov. For doubtful debt To Anurag(Profit) 3,610 To Bhawna (Profit) 1,805	485 5,415 11,400		 11,400

Dr. Partners' capital Accounts Cr.

Particulars	Anurag	Bhawna	**Monika**	Particulars	Anurag	Bhawna	**Monika**
To Cash	4,000	2,000	------	By Balance b/d	30,000	20,000	-
				By Revaluation A/c	3,610	1,805	-
To Balance c/d	33,610	21,805	15,000	By Cash A/c By Premium	------- 4,000	------- 2,000	15,000 --------
	37,610	23,805	15,000		37,610	23,805	15,000

Balance Sheet as at 31.12.2020

Liabilities	Rs.	**Assets**		Rs.
Creditors	65,900	Cash		16,200
		Debtors Less: Provision	9,700 (485)	 9,215
Anurag Capital	33,610	Stock		18,000
Bhawna Capital	21,805	Investment		1,400
Monika Capital	15,000	Plant and Machinery Building		31,500 60.000
	1,36,315			1,36,315

Working Notes:

Dr. Cash Account Cr.

Particulars	Rs.	**Particulars**	Rs.
To Balance b/d	1,200	By Anurag	4,000
To Monika's Capital A/c	15,000	By Bhawna	2,000
To Premium for Goodwill A/c	6,000	By bal. c/d	16,200
	22,200		22,200