Mangalore University

GFGC Punjalakatte Belthangady Tq.

BBA First Year – Second Semester Accounting 2

PARTNERSHIP ACCOUNTS : DISSOLUTION OF A PARTNERSHIP FIRM – PART 2

Contents:

PIECEMEAL PAYMENTS

Generally, the assets sold upon dissolution of partnership are realised only in small instalments over a period of time. In such circumstances, the choice is either to distribute whatever is collected or to wait till the whole amount is collected. Usually, the first course is adopted. In order to ensure that the distribution of cash among the partners is in proportion to their interest in the partnership concern either of the two methods described below may be followed for determining the order in which the payment should be made.

Maximum Loss Method

Each instalment realised is considered to be the final payment te., outstanding assets and claims are considered worthless and partners' accounts are adjusted on that basis each time when a distribution is made, following either Garner vs. Murray Rule or the profit-sharing ratio rule.

Proportionate Capital Method or Surplus Capital Method /Highest Relative Capital Method (*Method to be used as per Syllabus*)

According to this method, the partner who has the higher relative capital, that is, whose capital is greater in proportion to his profit-sharing ratio, is first paid off. This method is also called as proportionate capital method.

For determining the amount by which the capital of each partner is in excess of his relative capital, partners' capitals are first divided by figures that are in proportion to their profit-sharing ratio; the smallest quotient will indicate the basic capital. Having ascertained the partner who has the smallest basic capital, the amount of capital of other partners proportionate to the profit-sharing ratio of the basic capital is calculated. These may be called as their hypothetical capitals. The amount of hypothetical capital of each partner is then subtracted from the amount of his actual capital; the resultant figure will be the amount of excess capital held by him. By repeating the process once or twice, as may be necessary between the partners having excess capital, the amount by which the capital of each partner is in excess will be ascertained. The partner with the largest excess capital will be paid off first, followed by payment to the other or others who rank next to him until the capitals of partners are reduced to their profit-sharing ratio.

Problems and Solution:

1. A, B and C are partners is a firm sharing profits and losses in the proportion of 4/7th, 2/7th and 1/7th. They decided to dissolve the partnership on which date the Balance Sheet being as follows:

Liabilities	₹	**Assets**	₹
Creditors	28,500	Buildings	4,78,600
Bills Payable	81,250	Machinery	81,500
General Reserve	47,250	Furniture	12,300
Capitals:		Investments	75,000
A	2,00,000	Stock-in-trade	3,20,750
B	4,00,000	Debtors	1,13,500
C	3,25,000	Cash	350
	10,82,000		10,82,000

The partners decided that after paying outside creditors and providing ₹6,000 towards expenses of realization, all cash available should immediately be divided between them. The assets are realized as under:

	₹
First Realization:	
Machinery	70,000
Investments (Part)	6,800
Second Realization:	
Stock-in-trade (Part)	36,000
Debtors (Part)	41,500
Furniture	14,500
Third Realization:	
Buildings	4,00,000
Debtors (Part)	61,995
Investment (Balance)	70,000
Fourth and Final realization:	
Stock-in-trade	2,25,500
Debtors	6,000

Actual expenses of realization and dissolution amounted to ₹5,660. Prepare a statement showing how cash should be distributed to the partners.

Solution for problem no.1

Step 1. First calculate the surplus capital based upon the profit sharing ratio between partners

Step 2. Payment should be first made to the outsiders – Realisation expenses to be set aside, Creditors, Bills payable, Expenses outstanding etc

Step 3: Payment be made towards Partner's Loan Account if any

Step 4: Payment towards surplus capitals of partners

- Priority is given first to that partner who has highest surplus i.e.C here
- After his capital come in proportion to 2:1, B and C are paid
- After A , B, C capitals account come in proportion of 4:2:1. All the partners are paid in Profit sharing ratio

Step 5: Balance may be realization profit (excess realization) or realization loss(Balance unpaid if any)

Statement of Surplus Capital			
Particulars	A	B	C
Capital as per balance Sheet	200000	400000	325000
Add: Distribution of Gen. Reserves Rs.47250 in PSR	27000	13500	6750
A. Capital Balance	227000	413500	331750
B. Profit Sharing Ratio	4	2	1
Step A divided by B	56750	206750	331750
C. least capital contribution per share is Rs.50000 per share , so capital in PSR will be keeping A's capital as base	**227000**	**113500**	**56750**
D Surplus Capitals in their proft sharing ratio step A- Step C	**0**	**300000**	**275000**
		300000/2=150000	275000/1=275000
E. least capital contribution per share is Rs.75000 per share , so capital in PSR will be keeping B's capital as base		150000 x 2	150000 x 1
F. Capital in the Profit Sharing Ratio2:1		300000	150000
Surplus Capital (D-E)		0	125000

Statement Showing Piecemeal Distribution of Cash						
Particulars	Amount	Creditors	B/P	A's Cap	B'S Cap	C,s Cap
Balance as per Balance sheet		28500	81250	227000	413500	331750
Cash in hand	350					
Add: Amount realised on First Realisation	76800					
	77150					
Less: Realisation Exp. set aside	6000					
	71150					
Less: Payment to Creditors and Bills payable proTotal of Creditors+Bills payable= 109750 Payment to Creditors = 81250/109750x71150 Payment to Bills payable = 28500/109750x71150	52674 18476	18476	52674	0	0	0
Balance	0	10024	28576	227000	413500	331750
II Realisation Amount Received (36000+41500+14500)	92000					
Less: Paid towards Creditors and bills payable	38600	10024	28576	0	0	0
Balance	53400	0	0	227000	413500	331750
less: Amount paid to C towards surplus capital	53400		0	0	0	53400
Balance	0	0	0	227000	413500	278350
III Realisation Amount Received(400000+61995+7000)	531995					
less:Amount paid to C towards surplus capital	71600	0	0	0	0	71600
Balance	460395	0	0	227000	413500	206750
Less payment towards Surplus Capital of B And C in the ratio of 2:1	450000	0	0	0	300000	150000
Balance	**10395**	**0**	**0**	**227000**	**113500**	**56750**
Less: paid to all partners in PSR 4:2:1	10395	0	0	5940	2970	1485
Balance	0	0	0	221060	110530	55265
Final Realisation Amount and excess realisation expenses set aside (225500+6000+340)	231840	0	0			
Less: paid to all partners in PSR 4:2:1	231840	0	0	132480	66240	33120
REALISATION LOSS	0	0	0	88580	44290	22145

2. Reena, Meena and Teena are partners who shgare profits in the ration 3:2:1. Their balance sheet as on 31-03-2018 was as under –

LIABILITIES	Rs.	ASSETS	Rs.
Capital:		Sundry Assets	400000
Reena	60000		
Meena	100000		
Teena	100000		
Creditors	140000		
	400000		**400000**

The firm was dissolved and the assets were realised as under –
I Realisation – Rs.100000
II Realisation – Rs.60000
III Realisation – Rs.120000
IV Realisation – Rs.60000
Final Realisation – Rs.30000
Prepare statement of Piecemeal Distribution of Cash according to Surplus Capital Method.

Solution:

Statement of Surplus Capital			
Particulars	Reena	Meena	Teena
A.Capital Balance	60000	100000	100000
b.Profit Sharing Ratio	3	2	1
Step A divided by B	20000	50000	100000
C. least capital contribution per share is Rs.20000 per share , so cpital in nPSR will be keeping Reena's capital as base	60000	40000	20000
d. Surplus Capitals in their proft sharing ratio stepA- Step C	0	60000	80000
PSR		2	1
E. Step D/Step E		30000	80000
least capital contribution per share is Rs.30000 per share , so capital in PSR will be keeping Meena's capital as base			
F. PSR x Step E Capital in the Profit Sharing Ratio2:1		60000	30000
Surplus Capital (D-F)		0	50000

Statement Showing Piecemeal Distribution of Cash					
			Capital Account of Partners		
Particulars	Amount	Creditors	Reena	Meena	Teena
Balance as per Balance sheet		140000	60000	100000	100000
I Realisation Amount Received	100000				
Less: Payment to Creditors	100000	100000			

Balance	0	40000	60000	100000	100000
II Realisation Amount Received	60000				
Less: Amount Payable towards Creditors	40000	40000			
Balance	20000	0	60000	100000	100000
less: Amount paid toTeena towards surplus capital	20000				20000
Balance	0	0	60000	100000	80000
III Realisation Amount Received	120000				
less:Amount paid to Teena towards surplus capital	30000				30000
Balance	90000	0	60000	100000	50000
Less payment towards Surplus Capital of Meena And Teena in the ratio of 2:1	90000			60000	30000
Balance	0	0	60000	40000	20000
IV Realisation Amount Received	60000				
Less: paid to all partners in PSR 3:2:1	60000		30000	20000	10000
Balance	0	0	30000	20000	10000
Final Realisation Amount Received	30000				
Less: paid to all partners in PSR 3:2:1	30000		15000	10000	5000
REALISATION LOSS	0	0	15000	10000	5000

INSOLVENCY OF A PARTNER

A partner will be treated as insolvent partner if his liability is more than his assets.
In case of Insolvency of partner, insolvency loss of Insolvent partner should be distributed among Solvent partners

1. In their profit sharing ratio as per partnership Act, 1932.
   or
2. We have to follow the rules laid down by Garner v/s Murray

However, as per the curriculum, we will practice only the first method that is sharing of Insolvency loss by solvent partners in their profit sharing ratio.

Consequences of Insolvency of a Partner:
If a partner goes insolvent then the following are the consequences:
1. The partner adjudicated as insolvent ceases to be a partner.
2. He ceases to be a partner on the date on which the order of adjudication is made.

3. The firm is dissolved on the date of the order of adjudication unless there is a contract to the contrary.
4. The estate of the insolvent partner is not liable for any act of the firm after the date of the order of adjudication, and
5. The firm cannot be held liable for any acts of the insolvent partner after the date of the order of adjudication.

Problem and Solution:

P, Q and R were partners in a firm sharing profits and losses in the ratio of 3:2:1, No salary or interest were allowed to partners. Their Balance sheet as on 31st March 2019 stood as follows:

Liabilities	RS.	RS.	*Assets*	RS.	RS.
Fixed Capital			*Fixed assets:*		
P	*20000*		*Freehold Property*		*48000*
Q	*20000*		*Plant and Equipment*		*12,800*
R	*10000*	*50,000*	*Motor Vehicle*		*700*
Current Accounts:			*Current Assets - Stock*		*3,900*
P	*500*				
Q	9000	*9,500*			
Loan from P		*8,000*	*Trade Debtors*	*2000*	
			Less: Provision	*(100)*	*1,900*
Trade Creditors		*12400*	*Cash at Bank*		*200*
			Miscellaneous losses		
			R's Current Account		*400*
			Profit and Loss Account		*12,000*
		79,900			***79,900***

On 1st July, 2012 the partnership was dissolved. Motor Vehicle was taken over by Q at a value of 1500 but no cash passed specifically in respect of this transaction.

Sale of other assets realised the following amounts: Goodwill - nil, Freehold Property - 7,000, Plant and Equipment - 5,000, Stock - 3,000, Trade Debtors - 1,600

Trade Creditors were paid Rs. 11,700 in full settlement of their debts. The costs of dissolution amounted to Rs 1,500. The loan from P was repaid, P and Q were both fully solvent and able to bring in any cash required , but R has become insolvent and is forced into bankruptcy and was only able to bring 1/3 of the amount due.

You are required to show:

(a) Cash and Bank Account,

(b) Realisation Account, and

(c) Partners Fixed Capital Accounts (after transferring Current Accounts' balances).

SOLUTION:

Cash I Bank Account				
		Rs.		Rs.
To Balance b/d		200	By Realisation A/c- Creditors	11,700
To Realisation A/c-			By Realisation A/c- Expenses	1,500
Freehold property		7,000	By P's Loan A/c	8,000
Plant and Equipment		5,000	By P's Capital A/c	14,260
Stock		3,000	By Q's Capital A/c	24,140
Trade Debtors		1,600		
To Capital Accounts:				
P	25,500			
Q	17,000			
R	300	42.800		
		59,600		59,600

Realisation Account				
	Rs.			Rs.
To Goodwill	40,000	By Trade Creditors		12,400
To Freehold Property	8,000	By Provision for Bad Debts		100
To Plant and Equipment	12,800	By Bank:		
To Motor Vehicle	700	Freehold Property	7,000	
To Stock	3,900	Plant and Equip.	5,000	
To Sundry Debtors	2,000	Stock	3,000	
To Bank (Creditors)	11,700	Debtors	1,600	16,600
To Bank (Expenses)	1,500	By Q (Car)		500
		By Capital Accounts: (Loss)		
		P	25,500	
		Q	17,000	
		R	8,500	51,000
	80,600			80,600

Current account balances have been arrived after adjusting profit and loss account debit balance as follows:
P's Current account *Rs. 6,000- Rs. 500= Rs. 5,500
R's Current account ** Rs.2,000 + Rs. 400 = Rs. 2,400
Q's Current account *** Rs.9,000 - Rs. 4,000 = Rs. 5,000

Partners' Capital Accounts							
	P	**Q**	***R***		***P***	**Q**	***R***
To Current A/c (Transfer)	5,500*	—	2,400**	By Balance b/d	20,000	20,000	10,000
To Realisation A/c (Loss)	25,500	17,000	8,500	By Current A/c (Transfer)	—	5,000***	—
To Realisation A/c (Car)		500		By Bank			
To R's Capital A/c (Deficiency borne in PSR)	360	240	—	By Bank (realization loss)	25,500	17,000	300
To Bank	14,260	24140		ByP & Q (Deficiency)			600
	45500	42000	10900		45,500	42,000	10,900