Admission of a Partner

* Admission of a partner is the reconstitution of the firm because with the admission of partner, existing agreement ends and new agreement among all the partners comes into existence.

* According to section 31 of the Indian partnership Act, 1932, a person can be admitted as a partner:
(i) if it is so agreed in the partnership Deed.
(ii) in the absence of the agreement, if all partners agree to admit the partner.

* The amount paid by the New partner for the sacrifice of existing partner is called Goodwill or premium for Goodwill.

* Effects of Admission of A partner
- Old partnership comes to an end and new partnership comes into existence.
- New or incoming partner becomes entitled to share future profits of the firm and combined share of old Partners gets reduced.
- New or incoming partner contributes an agreed amount of capital in the firm.
- New or incoming partner acquires right in the assets and also become liable for the liabilities of the firm.

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* Adjustments required on Admission of a Partner :

(i) Change in Profit-sharing ratio : Determining new profit-sharing ratio and sacrificing ratio.

(ii) Valuation and Adjustment of Goodwill.

(iii) Adjustment of gain/loss from Revaluation of Assets and reassessment of liabilities.

(iv) Adjustment of reserves, accumulated (undistributed) profits and losses.

(v) Adjustment of capital on the basis of new profit-sharing ratio (if so agreed)

(vi) Adjustment of Deferred Revenue expenditure (Advertisement Suspense)

Chage in Profit-sharing Ratio

New or incoming partner is ~~the ratio~~ may acquire his or her share from old partners :

1. In their old profit sharing ratio
2. In a particular ratio or sacrificing ratio
3. In a particular fraction from old or existing partner.

Sacrificing share = old profit share − New profit share

Gaining share = New profit share − old profit share

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1 — Valuation and Adjustment of Goodwill

Accounting Treatment of Goodwill at the time of admission of a partner -

(i) Goodwill (Premium for goodwill is paid privately)
When goodwill is paid privately by the new or incoming partner to the sacrificing partners, journal entry is not passed in the books of account.

(ii) Goodwill (Premium for goodwill) is brought (in cash or by cheque) by the new or incoming partner and is retained in Business.

⇒ Accounting Entries :—

1. For premium for goodwill brought in cash or by cheque by the income or new partner	Cash/Bank A/c — Dr. [with share of capital] To Premium for goodwill A/c
2. For sharing of premium for goodwill by sacrificing partner	Premium for goodwill A/c — Dr. To Sacrificing partner's capital/current

(iii) Goodwill (premium for goodwill) is brought (in cash or by cheque) by new or Incoming partner and is withdrawn by sacrificing partners fully or partly:

⇒ Accounting Entries :—

For premium for goodwill brought by the New partner

Cash/Bank A/c — Dr. [Amount of Premium]
To Premium for goodwill A/c

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For sharing of premium for goodwill:

Premium for Goodwill A/C ——— Dr. [Amount of Premium

To Sacrificing partner's capital A/cs of Sacrificing Ratio]

For withdrawal of Premium amount fully/partly:

Sacrificing Partner's capital A/c ——— Dr. [Amount withdrawal]

To Cash/Bank A/c

(iv) Goodwill (Premium for Goodwill) is brought in kind:

⇒ Accounting Entries:–

For Assets brought in by the New partner:

Assets A/c ——— Dr. [Individually]

To New partner's capital A/c [with amt. of capital]

To Premium for Goodwill A/c [with share of Goodwill brought]

For crediting sacrificing partners' capital for Goodwill:

Premium for Goodwill A/c ——— Dr.

To Sacrificing partner's capital A/c [In sacrificing ratio]

(v) When a part of Goodwill (Premium for Goodwill) is brought

⇒ Accounting Entries:–

For Amount brought by the Incoming partner:

Bank A/c ——— Dr.

To Incoming partner's capital A/c [with Capital]

To Premium for Goodwill A/c [with share of Goodwill brought in]

For crediting sacrificing partners by Incoming partner's full share of Goodwill

Premium for Goodwill A/c ——— Dr. [with Premium for Goodwill brought]

Incoming partner's current A/c ——— Dr. [with unpaid share of goodwill]

To Sacrificing partner's capital A/cs [In sacrificing ratio]

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(vi) When the new Partner does not bring his share of Goodwill:
⇒ New partner's Current A/cs ——— Dr.
To Sacrificing Partner's capital/current A/c

* Hidden or Inferred Goodwill:
Calculation–

Net worth (including goodwill) = Incoming partner's capital × Reciprocal of his share

Net worth (excluding goodwill) = capital of old partners + capital of New partner

~~Value~~ Value of goodwill = Net worth (including goodwill) – Net worth (excluding goodwill)

Note: Net worth = Sundry Assets – outsiders' Liabilities
or
= Capital of all partners + Net accumulated profits & Reserves – Fictitious Assets – Non-trade investments.

Revaluation of Assets and Reassessment of Liabilities

The change in value of assets and Liabilities is adjusted through an account titled Revaluation Account or profit and Loss Adjustment Account.
The Gain/Loss of Revaluation account is transferred to old partners' capital Accounts in their old profit sharing ratio

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* Proforma of Revaluation Account :

Dr. Revaluation Account Cr.

Particulars	₹	Particulars	₹
To Assets A/c (individually)	---	By Assets A/c	
-Decrease in value	---	-Increase in value	---
To Liabilities A/c		By liabilities A/c	
-Increase in amount		-Decrease in amount	---
To unrecorded liability A/c	---	By unrecorded Asset A/c	---
To Partner's capital A/c		By Loss on revaluation	
(Remuneration)	---	debited to partner's	
To cash/Bank A/c (Expenses)	---	capital A/cs	---
To Gain (Profit on Revaluation			
transferred to Partner's capital/			
curret A/cs	---		
	---		---

Adjustment of Deferred Revenue Expenditure

It will be written off, (if exists in the books) by passing following journal Entry-

A's capital/current A/c ——— Dr. } On old sharing ratio
B's capital/ Current A/c ——— Dr. }
To Advertisement suspense A/c

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* Accounting of Reserves, Accumulated (undistributed) Profits and Losses

At the time of admission of a partner, balances in Reserves, accumulated profits and Losses are transferred to old partners capital/current A/c in their old profit-sharing ratio.

As a principle, the new partner should not benefit or be at a loss.

The Journal entry is:

Profit & Loss A/c (Cr. Balance) — Dr
General Reserve A/c — Dr
Workmen compensation Reserve A/c — Dr [Excess of reserve over liability]
Investment fluctuation Reserve A/c — Dr [Reserve > (Market value - Book value)]
To old partners capital / current A/cs
[Reserves and profits transferred to old partners in old ratio]

Old partners' capital / current A/cs — Dr [In old ratio]
To Profit & Loss A/c (Dr. Balance)

Note — Employees' provident fund and ESI payable are liabilities of the firm. Hence, they are not distributed among old partners.

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* ## Adjustment of Capital

➢ Case: 1.

Adjustment of the old partners' capital Accounts on the Basis of New or Incoming partner's capital:

Step: 1. Calculate total capital of the firm on the basis of capital of the new or incoming partner.

$$\text{Total capital of the firm} = \frac{\text{Capital of New or Incoming Partner}}{\text{Share of profit of the New or Incoming Partner}}$$

Step: 2 Determine new capital of each partner.

⇒ Total capital × New profit sharing ~~ratio~~ of each partner.

Step: 3 Ascertain present capital of the old partners (after all adjustments)

Step: 4 Find Surplus or deficit by comparing the proportionate capital and present capital

Surplus = Present capital > New capital

Deficit = Present capital < New capital

Step: 5 Pass necessary journal entry for adjusting the above surplus or deficit.

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Case : II
Calculating the capital of the new or Incoming partner on the Basis of capitals of old partners.

Step : 1 Determine total adjusted capital of old partners i.e., after giving effect of all adjustments.

Step : 2 Determine total capital of the new firm as:
Total adjusted capital
= Total adjusted capital of old partners X Reciprocal of combined new share of old partners

Step : 3 Determine capital of the incoming partner as:

Total capital x share of incoming partner.

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