

# Accounting for Partnership Firms — Fundamentals

## \* Partnership : (Indian partnership Act , 1932)

It is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

## \* Essentials of partnership :

- Minimum two and maximum 50 members.
- Carrying on a business (i.e. profit motive)
- Sharing of Profits
- Agreement
- Legal objects

## \* Partnership Deed / Agreement :

Partnership agreement is the mutual understanding on which some people decide to do a legal business to earn profits. It may be oral or written. The written or registered version of the agreement is also called Partnership Deed.

It contains basically two types of matter:-

- 1. Management related matters - e.g. Name of the business, nature of the business, responsibilities of partners, ways of settlement of disputes etc

► 2. Money related matters - e.g. capitals of partners, profit sharing ratios, interest on capital and drawings, interest on overdrafts, remunerations to partners, method of valuation of goodwill and method of maintaining books of accounts etc.

\* Provisions affecting Accounting Treatment in the Absence of Partnership Deed:

- |                          |              |
|--------------------------|--------------|
| ● Sharing of Profit/loss | equal        |
| ● Interest on capital    | not allowed  |
| ● Interest on Drawings   | not charged  |
| ● Any remuneration       | not allowed  |
| ● Interest on Loan       | 6% P.a.      |
| ● Admission of Partner   | not admitted |

\* Specimen of Profit and Loss Appropriation Account:

Profit and Loss Account		
Dr.	Credit	Cs
Particulars		
To P&L A/c (Net Loss)	---	By Profit & Loss A/c*
To Interest on capitals		(Net profit)
X -		By Interest on Drawings
Y -	---	X -
To Partner's Salaries	---	Y -
To Partner's Commission	---	By Loss transferred to:
To Reserve		X's Capital A/c ---
To Profit transferred to:		Y's Capital A/c ---
X's Capital A/c	---	---
Y's Capital A/c	---	---

## \* Features of Profit and Loss Appropriation Account:

1. It is an extension of Profit and Loss A/c
2. It is prepared by partnership firms.
3. It shows the appropriation of net profit or net loss for the accounting period.
4. Entries in this account are passed giving effect to the partnership deed.

## ===== Partner's Capital Account =====

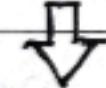
The partner's capital Accounts may be maintained by following methods:

### 1. Fixed capital Accounts Method

**Capital Account**



**Current Account**



Credit with:

Further capital  
introduced

Debit with:

Drawings against  
Capital

Credit with:

Remuneration (Salary,  
commission)

Interest on capital

Shares of profit

Debit with:

Drawings (against profit)  
Interest on Drawings

Share of loss

2.

## Fluctuating Capital Accounts Method



### Capital Account

Credit with

- Further capital introduced
- Remuneration (Salary, commission)
- Interest on Capital
- Share of Profit

Debit with

- Drawings against capital
- Drawings against profit
- Interest on Drawings
- Share of loss

\* Calculation of Interest on Drawings:

1. Product Method :

$$\Rightarrow \text{Total of Product} \times \frac{\text{Rate of Interest}}{100} \times \frac{1}{12} \frac{365}{365}$$

2. Average period Method :

$$\Rightarrow \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average period}}{12}$$

## \* Calculation of opening capital

(a) When capitals are fixed:

Calculation of opening capital		₹
Capital at the end of the year		---
Add: Withdrawal of Capital	+ (- - -)	- - -
Less: Additional capital introduced		(- - -)
Capital in the beginning of the year		---

(b) When capitals are fluctuating:

Calculation of Opening capital		₹
Capital at the end of the year		---
Add: Withdrawal of Capital	- - -	- - -
Drawings against profit	- - -	- - -
Interest on Drawings	- - -	- - -
Share of Loss for the year*	+ (- - -)	- - -
Less: Additional capital introduced ...		- - -
Partner's Remuneration	- - -	- - -
Interest on capital	- - -	- - -
Share of Profit for the year*	- - - ( - - - )	- - -
Capital in the beginning of the year		---

## \* Guarantee of Profits

Guarantee is an assurance given to the partner of the firm that at least a fixed amount shall be given to him/her irrespective of his/her share in profit of the firm.

### Case:1:

When Guarantee is given by firm (i.e. by all the partners of the firm).

\* Share in actual profit < Guaranteed Amount

Then,

Guaranteed amount is first written off against the profits and then,

→ Remaining profits are distributed among the remaining partners in the remaining ratio.

### Case:2

When Guarantee is given by a partner or partners to another partner.

1. \* calculate the share in profits of the guaranteed partner (to whom guarantee is given).

2. \* If Share in profit < Guaranteed amount

Then, find :

$$\text{Guaranteed amount} - \text{Share in profit} = ?x \text{ (let)}$$

?x → Deficiency

Deficiency is borne (contributed) by other partners in certain ratio and is subtracted from their profit share.