

*In case of fixed capitals.

**Unless otherwise stated, Partners' Capitals should be assumed to be fluctuating.

Illustration 11. (When Premium for Goodwill brought in Cash by New Partner is Retained in Business). Sachin and Kapil are partners sharing profits and losses in the ratio of 2 : 1. They admit Amit into partnership who brings in ₹ 24,000 for his 1/4th share for goodwill. Pass necessary Journal entries to record the transactions.

Solution:

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Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Cash/Bank A/c ...Dr. To Premium for Goodwill A/c (Being the amount of premium for goodwill brought in by Amit)		24,000	24,000
	Premium for Goodwill A/c ...Dr. To Sachin's Capital A/c To Kapil's Capital A/c (Being the premium for goodwill brought in by Amit, shared by Sachin and Kapil in their sacrificing ratio) (Note)		24,000	16,000 8,000

Note: Since there is no change in the profit-sharing ratio between Sachin and Kapil, their old profit-sharing ratio is their sacrificing ratio, i.e., 2 : 1.

Illustration 12 (When Premium for Goodwill brought in Cash by New Partner is Retained in Business). Gyan and Govind are partners in a firm sharing profits in the ratio of 5 : 3. They admit Ganga as a new partner for 1/5th share in the profit. Ganga brought ₹ 40,000 for his 1/5th share of goodwill.

Pass necessary Journal entries in the books of the firm on Ganga's admission. New profit-sharing ratio will be 3 : 1 : 1.

Solution:

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Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Cash/Bank A/c ...Dr. To Premium for Goodwill A/c (Being the cash brought in by Ganga for his share of goodwill)		40,000	40,000
	Premium for Goodwill A/c ...Dr. To Gyan's Capital A/c To Govind's Capital A/c (Being the goodwill premium brought in by Ganga transferred to Old Partners' Capital Accounts in their sacrificing ratio, i.e., 1 : 7) (WN)		40,000	5,000 35,000

SUMMARY OF THE CHAPTER

- When the existing partners of a firm allow a person to become a partner in the firm, it is called **admission of a partner**.
- The matters that require adjustment at the time of admission of a new partner are:
 - (i) Adjustment for change in Profit-Sharing Ratio. Calculation of New Profit-sharing Ratio and Sacrificing Ratio.
 - (ii) Adjustment for goodwill.
 - (iii) Adjustment of Profit/Loss arising from the Revaluation of Assets and Reassessment of Liabilities.
 - (iv) Adjustment of Accumulated Profits, Reserves and Losses.
 - (v) Adjustment of Capital.

- Change in Profit-sharing Ratio takes place at the time of admission of a new partner in the firm.
- The ratio in which all partners including the incoming partner share the future profits and losses is known as **New Profit-Sharing Ratio**.

*Unless agreed otherwise, the **New Profit-sharing Ratio** of existing, i.e., old partners among them will be same as their old profit-sharing ratio.*

- The ratio in which the old (existing) partners have agreed to sacrifice their share in profit in favour of an incoming partner is called **Sacrificing Ratio**.

$$\text{Sacrificing Share} = \text{Old Share} - \text{New Share.}$$

*Unless agreed otherwise, **Sacrificing Ratio** of old partners will be the same as their old profit-sharing ratio.*

- The partners whose share in profit increase due to change in profit-sharing ratio are called *Gaining Partners* and the partners whose share in profit decrease are called *Sacrificing Partners*.
- **Goodwill** is the reputation of the organisation which attracts customers and increases the profit earning capacity of the business.

ACCOUNTING TREATMENT OF GOODWILL ON ADMISSION OF A PARTNER

1. Goodwill (Premium) paid Privately	No Entry
2. Goodwill brought in Cash	Cash/Bank A/c ...Dr. To Premium for Goodwill A/c
Distribution of Goodwill	Premium for Goodwill A/c ...Dr. To Sacrificing Partners' Capital A/cs [In sacrificing ratio] or To Sacrificing Partners' Current A/cs (When capitals are fixed)
3. Goodwill withdrawn by Sacrificing (Old) Partners	Sacrificing Partners' Capital A/cs ...Dr. To Cash/Bank A/c
4. Goodwill not brought in Cash	New Partner's Current A/c ...Dr. To Sacrificing Partners' Capital A/cs [In sacrificing ratio]
5. Goodwill brought in Kind	Assets A/c ...Dr. To Premium for Goodwill A/c

Note: Write off the goodwill appearing in the Old Balance Sheet by debiting the Old Partners' Capital Accounts (in case of fluctuating capitals) or Current Accounts (in case of fixed capitals) in their old profit-sharing ratio and crediting the Goodwill Account.

- Unless otherwise stated, the Partners' Capitals should be assumed to be fluctuating. Current Accounts are to be used in case of Fixed Capitals.
- When the incoming partner cannot bring premium for goodwill in cash, adjustments are to be done through the Current Account of Incoming Partner.

Admission of a Partner

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Admission of Partner or Partners

Admission of a Partner or partners means new partner or partners being admitted into partnership.

2. New Profit-sharing Ratio

New Profit-sharing Ratio is the ratio in which all the partners or partners including the new or incoming partner or partners share future profits and losses of the firm.

3. Sacrificing Ratio

Sacrificing Ratio is the ratio in which the old or existing partners forego, *i.e.*, sacrifice their share in favour of the new partner or partners.

4. Goodwill

Goodwill is an intangible asset resulting from the efforts made in the past by the existing partners of the firm which results in profits in the future years.

5. Revaluation of Assets

Revaluation of Assets means change in the value of assets, *i.e.*, present value being different from the book value of the assets.

6. Reassessment of Liabilities

Reassessment of Liabilities means reassessing the liabilities and determining the change, *i.e.*, whether the liability is more or less than that shown in the books of account.

7. Revaluation Account

It is a nominal account, prepared to ascertain gain (profit)/loss on account of revaluation of assets and reassessment of liabilities. It is credited with the increase in value of assets and decrease in the value of liabilities. It is debited with the increase the value of liabilities and decrease in the value of assets. It is closed by transferring the gain (profit) or loss to the Capital Accounts or Current Accounts of the old or existing partners in their old profit-sharing ratio.

8. Reserve

Reserve means accumulated or undistributed profits. It is created out of profits.

The reserve created is sometimes invested outside the business in instruments such as securities, which then becomes a *Reserve Fund*.

9. Workmen Compensation Reserve

It is a reserve created out of profits for payment of compensation to workers.

10. Investments Fluctuation Reserve

It is a reserve created out of profits to meet the fall in the market value of investment.

Goodwill/Premium brought in Cash by the New Partner and retained in the Business

19. X and Y are partners sharing profits and losses in the ratio of 3 : 2. They agree to admit Z into partnership who brings in ₹ 48,000 for 1/4th share for goodwill. Pass necessary Journal entries to record the transactions.
20. E and F are partners sharing profits and losses in the ratio of 4 : 1. G is admitted as a partner for which he pays ₹ 10,000 as premium for goodwill and in future E, F and G decide to share profits and losses in the ratio of 2 : 1 : 1 respectively.

You are required to pass necessary Journal entries in the books of firm.

21. X and Y are partners in a firm sharing profits in the ratio of 2 : 1. On 1st April, 2018, their capitals are ₹ 2,00,000 and ₹ 1,00,000 respectively. On that date, they admitted Z as a new partner for 1/5th share in future profits. New profit-sharing ratio of X, Y and Z will be 3 : 1 : 1. Z brought ₹ 80,000 as his capital and ₹ 30,000 as his share of premium for goodwill.

3.12

Double Entry Bookkeeping

Working Note:

CALCULATION OF SACRIFICING RATIO

Partners	Old Share	New Share	Sacrifice (Old Share - New Share)	Sacrificing Ratio
Gyan	$\frac{5}{8}$	$\frac{3}{5}$	$\frac{5}{8} - \frac{3}{5} = \frac{1}{40}$	Gyan : Govind 1 : 7
Govind	$\frac{3}{8}$	$\frac{1}{5}$	$\frac{3}{8} - \frac{1}{5} = \frac{7}{40}$	