



Question 48.

A, B and C were partners in a firm having capitals of ₹ 50,000 ; ₹ 50,000 and ₹ 1,00,000 respectively. Their Current Account balances were A: ₹ 10,000; B: ₹ 5,000 and C: ₹ 2,000 (Dr.). According to the Partnership Deed the partners were entitled to an interest on Capital @ 10% p.a. C being the working partner was also entitled to a salary of ₹ 12,000 p.a. The profits were to be capitals:

(a) The first ₹ 20,000 in proportion to their capitals.

(b) Next ₹ 30,000 in the ratio of 5 : 3 : 2.

(c) Remaining profits to be shared equally.

The firm earned net profit of ₹ 1,72,000 before charging any of the above items.

Prepare Profit and Loss Appropriation Account and pass necessary Journal entry for the appropriation of profits.

Solution:

Profit and Loss Appropriation Account				
Dr.			Cr.	
Particulars	Rs.		Particulars	Rs.
To Interest on Capital			By Profit and Loss A/c (Net Profit)	1,72,000
A	5,000			
B	5,000			
C	10,000	20,000		
To Salary to C A/c		12,000		
To Profit transferred to :				
A's Capital A/c	50,000			
B's Capital A/c	44,000			
C's Capital A/c	46,000	1,40,000		
		1,72,000		1,72,000



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54%



2:00 pm

Solution:

Profit and Loss Appropriation Account				
Dr.			Cr.	
Particulars	Rs.	Particulars	Rs.	
To Interest on Capital		By Profit and Loss A/c (Net Profit)	1,72,000	
A	5,000			
B	5,000			
C	10,000			
To Salary to C A/c	12,000			
To Profit transferred to :				
A's Capital A/c	50,000			
B's Capital A/c	44,000			
C's Capital A/c	46,000	1,40,000		
	1,72,000		1,72,000	

Journal Entries				
Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Interest on Capital A/c To A's Current A/c To B's Current A/c To C's Current A/c (Being Interest on partner's capital allowed to partners)	Dr.	20,000	5,000 5,000 10,000
	Salary A/c To C's Current A/c (Being Salary Allowed to C)	Dr.	12,000	12,000
	Profit and Loss Appropriation A/c To A's Current A/c To B's Current A/c To C's Current A/c (Being profit available for distribution transferred to partners' current account)	Dr.	1,40,000	50,000 44,000 46,000

Working Notes :

1. Calculation of Interest on Capital

$$\text{Interest on A's Capital} = 50,000 \times \frac{10}{100} = ₹5,000$$

$$\text{Interest on B's Capital} = 50,000 \times \frac{10}{100} = ₹5,000$$

$$\text{Interest on C's Capital} = 1,00,000 \times \frac{10}{100} = ₹10,000$$

2. Calculation of share of Profit of each Partner

Profits available for Distribution = 1,72,000 - 20,000 - 12,000 = Rs. 1,40,000

i. Distribution of first Rs. 20,000 in the Capital ratio i.e. 1:1:2

$$\text{A's Profit Share} = 20,000 \times \frac{1}{4} = ₹5,000$$

$$\text{B's Profit Share} = 20,000 \times \frac{1}{4} = ₹5,000$$

$$\text{C's Profit Share} = 20,000 \times \frac{2}{4} = ₹10,000$$

ii. Distribution of Next Rs. 30,000 in the ratio of 5: 3: 2

$$\text{A's Profit Share} = 30,000 \times \frac{5}{10} = ₹15,000$$

1. Calculation of Interest on Capital

$$\text{Interest on A's Capital} = 50,000 \times \frac{10}{100} = ₹5,000$$

$$\text{Interest on B's Capital} = 50,000 \times \frac{10}{100} = ₹5,000$$

$$\text{Interest on C's Capital} = 1,00,000 \times \frac{10}{100} = ₹10,000$$

2. Calculation of share of Profit of each Partner

Profits available for Distribution = 1,72,000 - 20,000 - 12,000 = Rs. 1,40,000

i. Distribution of first Rs. 20,000 in the Capital ratio i.e. 1:1:2

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$$\text{C's Profit Share} = 20,000 \times \frac{2}{4} = ₹10,000$$

ii. Distribution of Next Rs. 30,000 in the ratio of 5: 3: 2

$$\text{A's Profit Share} = 30,000 \times \frac{5}{10} = ₹15,000$$

$$\text{B's Profit Share} = 30,000 \times \frac{3}{10} = ₹9,000$$

$$\text{C's Profit Share} = 30,000 \times \frac{2}{10} = ₹6,000$$

iii. Remaining profit available for distribution = 1,40,000 - 20,000 - 30,000 = Rs.90,000

This profit of Rs.90,000 is to be shared equally by the partners.

$$\text{A, B and C each will get} = 90,000 \times \frac{1}{3} = ₹30,000$$

Therefore,

$$\text{Total Profit Share of A} = 5,000 + 15,000 + 30,000 = \text{Rs.}50,000$$

$$\text{Total Profit Share of B} = 5,000 + 9,000 + 30,000 = \text{Rs.}44,000$$

$$\text{Total Profit Share of C} = 10,000 + 6,000 + 30,000 = \text{Rs.}46,000$$

Accounting Treatment

Interest on loan by partner is credited to his Loan Account and not to his Capital Account. Journal entries passed are:

- (i) To provide Interest on Loan by Partner:
- | | |
|---------------------------------|--------|
| Interest on Loan by Partner A/c | ...Dr. |
| To Loan by Partner A/c | |
- (ii) To close the Interest on Loan by Partner A/c:
- | | |
|------------------------------------|--------|
| Profit and Loss A/c | ...Dr. |
| To Interest on Loan by Partner A/c | |

It is important to distinguish Loan Account and Capital Account of a partner because:

- As per the Indian Partnership Act, 1932, loan by a partner is repayable on dissolution before repayment of capital to partners; and
- In the absence of any agreement, partners get interest @ 6% p.a. on loan advanced whereas they are not entitled to interest on capital.

Illustration 3.

Amit, Bimal and Chaman are partners sharing profits and losses equally. Amit and Chaman gave loans to the firm on 1st October, 2019 of ₹ 1,00,000 and ₹ 1,50,000 respectively. It is agreed that interest @ 9% p.a. will be paid on loan. Books of account of the firm are closed on 31st March every year. Interest on loan is yet to be paid as on 31st March, 2020.

Pass Journal entries in the books of account of the firm and prepare Loan Accounts of the two partners.

Solution:

In the Books of Amit, Bimal and Chaman

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2019 Oct. 1	Bank A/c ...Dr. To Loan by Amit A/c To Loan by Chaman A/c (Loan from partners Amit and Chaman)		2,50,000	1,00,000 1,50,000
2020 March 31	Interest on Loan by Partners A/c ...Dr. To Loan by Amit A/c To Loan by Chaman A/c (Interest on loan by partners provided @ 9% p.a.)		11,250	4,500 6,750
March 31	Profit and Loss A/c ...Dr. To Interest on Loan by Partners A/c (Interest on Loan by Partners Account transferred to Profit and Loss Account)		11,250	11,250

Dr.		LOAN BY AMIT ACCOUNT				Cr.
Date	Particulars	₹	Date	Particulars	₹	
2020 March 31	To Balance c/d	1,04,500	2019 Oct. 1	By Bank A/c	1,00,000	
		1,04,500	2020 March 31	By Interest on Loan by Partners A/c	4,500	
			2020 April 1	By Balance b/d	1,04,500	