

## Partnership Accounting: Retirement of a partner

In this worksheet, you'll prepare the partners' capital accounts, showing the retirement of a partner, and prepare the statement of financial position after the retirement. The answers are at the end.

Medina, Millie and Mirza were in partnership together, sharing profits and losses in the ratio 3:1:2 respectively. The statement of financial position for the partnership at 30<sup>th</sup> June 2022 was as follows.

	£	£
Non-Current Assets		351,000
Current Assets:		
Inventory	55,100	
Trade Receivables	49,080	
Bank	13,000	
Cash	<u>350</u>	
		<u>117,530</u>
Total Assets		<u><u>468,530</u></u>
Capital Accounts:		
Medina	226,000	
Millie	143,000	
Mirza	<u>51,000</u>	
		420,000
Current Accounts:		
Medina	21,600	
Millie	15,830	
Mirza	<u>(25,300)</u>	
		<u>12,130</u>
		432,130
Current Liabilities:		
Trade Payables		<u>36,400</u>
Total Capital and Liabilities		<u><u>468,530</u></u>

The partners agreed the following, from 1<sup>st</sup> July 2022:

1. Goodwill will be valued at £75,000 and will not remain in the books of accounts
2. Assets, and their values, are changed as follows:
  - a. Inventory that cost £18,400 is damaged, and is to be reduced in value to its net realisable value of £11,600
  - b. An irrecoverable debt, £11,200, is to be written off

- c. Mirza will take ownership of a car, currently belonging to the partnership, with a net book value of £10,000. The remaining non-current assets are to be revalued, with a new valuation of £395,000
3. Mirza will retire from the partnership on 1<sup>st</sup> July 2022. Medina and Millie will continue in partnership, sharing profits equally
4. Millie will invest £15,000 of her own savings into the business on 1<sup>st</sup> July
5. Mirza will leave £16,000 as a loan to the partnership to be repaid in full in September 2027. No loan interest will be paid to Mirza
6. The remaining balance on Mirza's capital account, taking into account the balance on his current account, will be paid from the partnership's bank account

You have been asked to:

- a) Prepare the partners' capital accounts to show Mirza's retirement
- b) Prepare the statement of financial position after Mirza's retirement

ANSWERS:

- a) Preparation of the partners' capital accounts to show the retirement

**STEP 1**

First, we'll prepare the revaluation account to take account of the changes to the asset values:

Revaluation			
Details	£	Details	£
Inventory (W1)	6,800	Non-current assets (W3)	54,000
Irrecoverable debt (W2)	11,200		
Capital: Medina (W4)	18,000		
Capital: Mille	6,000		
Capital: Mirza	12,000		
	<u>54,000</u>		<u>54,000</u>

(W1) Inventory is being reduced by £6,800 (ie £18,400 to £11,600). To reduce the inventory asset, we post a credit, and therefore a debit to the Revaluation account

(W2) The irrecoverable debt, £11,200, is posted as:

DR	Revaluation
CR	Customer account (to reduce the Customer asset by the amount of the debt)

(W3) Non-current assets are currently valued at £351,000. Removing from this the car that Mirza is taking (value £10,000), leaves a net book value of £341,000.

The non-current assets are being revalued at £395,000, an increase of £54,000 (ie 395,000 – 341,000)

This is posted as:

DR	Non-current assets (to increase their value to £395,000)
CR	Revaluation

(W4) The Revaluation account is balanced as follows:

The balancing figure is calculated as:  $54,000 - (6,800 + 11,200) = 36,000$

This is shared between the three partners in the OLD profit-sharing ratio of 3:1:2

Shares are therefore:	Medina	$3/6 \times 36,000 = £18,000$
	Millie	$1/6 \times 36,000 = £6,000$
	Mirza	$2/6 \times 36,000 = £12,000$

**STEP 2**

Next, we'll make the goodwill adjustment:

Goodwill			
Details	£	Details	£
Capital: Medina (3/6)	37,500	Capital: Medina (1/2)	37,500
Capital: Millie (1/6)	12,500	Capital: Millie (1/2)	37,500
Capital: Mirza (2/6)	25,000		
	<u>75,000</u>		<u>75,000</u>

### STEP 3

Prepare the partner's capital accounts:

Capital Accounts

Details	Medina (£)	Millie (£)	Mirza (£)	Details	Medina (£)	Millie (£)	Mirza (£)
Goodwill (AFTER) (W7)	37,500	37,500		Balance b/f (W6)	226,000	143,000	51,000
Car (note 1)			10,000	Goodwill (BEFORE) (W7)	37,500	12,500	25,000
Current Account (W9)			25,300	Revaluation (W8)	18,000	6,000	12,000
Loan (note 5)			16,000	Bank		15,000	
Bank (balancing figure)			36,700				
Balance c/f	244,000	139,000	0				
	<b>281,500</b>	<b>176,500</b>	<b>88,000</b>		<b>281,500</b>	<b>176,500</b>	<b>88,000</b>
				Balance b/f	244,000	139,000	0

(W6) The balances before the retirement are shown in the SOFP

(W7) The goodwill postings are the other part of the double entry as posted in the temporary Goodwill account

(W8) The revaluation postings are the other part of the double entry recorded when the revaluation account was balanced, with the balancing figure being shared between the partners

(W9) Mirza has a debit balance on his current account. The double entry therefore required to transfer this to his capital account is:

CR     Mirza's current account  
DR     Mirza's capital account

b) Revised statement of financial position, after the retirement, at 30<sup>th</sup> June 2022:

	£	£
Non-Current Assets (note 2c)		395,000
Current Assets:		
Inventory (55,100 – 6,800)	48,300	
Trade Receivables (49,080 – 11,200)	37,880	
Cash	<u>350</u>	
		<u>86,530</u>
Total Assets		<u><u>481,530</u></u>
Capital Accounts:		
Medina	244,000	
Millie	<u>139,000</u>	
		383,000
Current Accounts:		
Medina	21,600	
Millie	<u>15,830</u>	
		<u>37,430</u>
		420,430
Non-current liability: loan (note 4)		16,000
Current Liabilities:		
Trade Payables		36,400
Bank overdraft (13,000 – 36,700 + 15,000)		<u>8,700</u>
Total Capital and Liabilities		<u><u>481,530</u></u>