Dissolution of Partnership Firm

5

LEARNING OBJECTIVES

After studying this chapter, you will be able to :

- *State the meaning of dissolution of partnership firm;*
- *Differentiate between dissolution of partnership and dissolution of a partnership firm;*
- *Describe the various modes of dissolution of the partnership firm;*
- *Explain the rules relating to the settlement of claims among all partners;*
- *Prepare Realisation Account;*
- *Record journal entries and prepare the necessary ledger accounts to close the books of the firm and settlement of partners' claim.*

You have learnt about the reconstitution of a partnership firm which takes place on account of admission, retirement or death of a partner. In such a situation while the existing partnership is dissolved, the firm may continue under the same name if the partners so decide. In other words, it results in the dissolution of a partnership but not that of the firm. According to Section 39 of the partnership Act 1932, the dissolution of partnership between all the partners of a firm is called the dissolution of the firm. That means the Act recognises the difference in the breaking of relationship between all the partners of a firm and between some of the partners; and it is the breaking or discontinuance of relationship between all the partners which is termed as the dissolution of partnership firm. This brings an end to the existence of firm, and no business is transacted after dissolution except the activities related to closing of the firm as the affairs of the firm are to be wound up by selling firm's assets and paying its liabilities and discharging the claims of the partners.

5.1 Dissolution of Partnership

As stated earlier dissolution of partnership changes the existing relationship between partners but the firm may continue its business as before. The dissolution of partnership may take place in any of the following ways:

(1) Change in existing profit sharing ratio among partners;

(2) Admission of a new partner;

(3) *Retirement of a partner;*
(4) *Death of a partner;*
(5) *Insolvency of a partner;*
(6) *Completion of the venture, if partnership is formed for that; and*
(7) *Expiry of the period of partnership, if partnership is for a specific period of time;*

5.2 Dissolution of a firm

Dissolution of a partnership firm may take place without the intervention of court or by the order of a court, in any of the ways specified later in this section. It may be noted that dissolution of the firm necessarily brings in dissolution of the partnership.

Dissolution of a firm takes place in any of the following ways:

1. *Dissolution by Agreement:* A firm is dissolved :
   (a) with the consent of all the partners or
   (b) in accordance with a contract between the partners.
2. *Compulsory Dissolution:* A firm is dissolved compulsorily in the following cases:
   (a) when all the partners or all but one partner, become insolvent, rendering them incompetent to sign a contract;
   (b) when the business of the firm becomes illegal; or
   (c) when some event has taken place which makes it unlawful for the partners to carry on the business of the firm in partnership, e.g., when a partner who is a citizen of a country becomes an alien enemy because of the declaration of war with his country and India.
3. *On the happening of certain contingencies:* Subject to contract between the partners, a firm is dissolved :
   (a) if constituted for a fixed term, by the expiry of that term;
   (b) if constituted to carry out one or more ventures, by the completion thereof;
   (c) by the death of a partner;
   (d) by the adjudication of a partner as an insolvent.
4. *Dissolution by Notice:* In case of partnership at will, the firm may be dissolved if any one of the partners gives a notice in writing to the other partners, signifying his intention of seeking dissolution of the firm.
5. *Dissolution by Court:* At the suit of a partner, the court may order a partnership firm to be dissolved on any of the following grounds:
   (a) when a partner becomes insane;
   (b) when a partner becomes permanently incapable of performing his duties as a partner;
   (c) when a partner is guilty of misconduct which is likely to adversely affect the business of the firm;

(d) *when a partner persistently commits breach of partnership agreement;*
(e) *when a partner has transferred the whole of his interest in the firm to a third party;*
(f) *when the business of the firm cannot be carried on except at a loss; or*
(g) *when, on any ground, the court regards dissolution to be just and equitable.*

Distinction between Dissolution of Partnership and Dissolution of Firm

Basis	*Dissolution of Partnership*	*Dissolution of Firm*
1. *Termination of business*	*The business is not terminated.*	*The business of the firm is closed.*
2. *Settlement of assets and liabilities*	*Assets and liabilities are revalued and new balance sheet is drawn.*	*Assets are sold and liabilities are paid-off.*
3. *Court's intervention*	*Court does not intervene because partnership is dissolved by mutual agreement.*	*A firm can be dissolved by the court's order.*
4. *Economic relationship*	*Economic relationship between the partners continues though in a changed form.*	*Economic relationship between the partners comes to an end.*
5. *Closure of books*	*Does not require because the business is not terminated.*	*The books of account are closed.*
6. *Other dissolution*	*It may or may not involve dissolution of the firm.*	*It necessarily involves dissolution of partnership.*

Test your Understanding – I

State giving reasons, which of the following statements are true or false:
1. *Dissolution of a partnership is different from dissolution of a firm,*
2. *A partnership is dissolved when there is a death of a partner,*
3. *A firm is dissolved when all partners give consent to it.*
4. *A firm is compulsorily dissolved when a partner decide to retire.*
5. *Dissolution of a firm necessarily involves dissolution of partnership.*
6. *A firm is compulsorily dissolved when all partners or when all except one partner become involvent.*
7. *Court can order a firm to be dissolved when a partner becomes insane.*
8. *Dissolution of partnership can not take place without intervention of the court.*

5.3 Settlement of Accounts

In case of dissolution of a firm, the firm ceases to conduct business and has to settle its accounts. For this purpose, it disposes off all its assets for satisfying all the claims against it. In this context it should be noted that, subject to agreement among the partners, the following rules as provided in Section 48 of the Partnership Act 1932 shall apply.

(a) Treatment of Losses

Losses, including deficiencies of capital, shall be paid :

(i) first out of profits,

(ii) next out of capital of partners, and

(iii) lastly, if necessary, by the partners individually in their profits sharing ratio.

(b) Application of Assets

The assets of the firm, including any sum contributed by the partners to make up deficiencies of capital, shall be applied in the following manner and order:

(i) In paying the debts of the firm to the third parties;

(ii) In paying each partner proportionately what is due to him/her from the firm for advances as distinguished from capital (i.e. partner' loan);

(iii) In paying to each partner proportionately what is due to him on account of capital; and

(iv) the residue, if any, shall be divided among the partners in their profit sharing ratio.

Thus, the amount realised from assets along with contribution from partners, if required, shall be utilised first to pay off the outside liabilities of the firm such as creditors, loans, bank overdraft, bill payables, etc. (it may be noted that secured loans have precedence over the unsecured loans); the balance should be applied to repay loans and advances made by the partners to the firm. (in case the balance amount is not adequate enough to pay off such loans and advances, they are to be paid propartionately); and surplus, if any is to be utilised in settlement of the capital account balances, after adjusting all profits and losses.

Private Debts and Firm's Debts: *Where both the debts of the firm and private debts of a partner co-exist, the following rules, as stated in Section 49 of the Act, shall apply.*

(a) The property of the firm shall be applied first in the payment of debts of the firm and then the surplus, if any, shall be divided among the partners as per their claims, which can be utilised for payment of their private liabilities.

(b) The private property of any partner shall be applied first in payment of his private debts and the surplus, if any, may be utilised for payment of the firm's debts, in case the firm's liabilities exceed the firm's assets.

It may be noted that the private property of the partner does not include the personal properties of his wife and children. Thus, if the assets of the firm are not adequate enough to pay off firm's liabilities, the partners have to contribute out of their net private assets (private assets minus private liabilities).

Inability of a Partner to Contribute Towards Deficiency

In the context of settlement of accounts among the partners there is still another important aspect to be noted, i.e., when a partner is unable to contribute towards the deficiency of his capital account (the account finally showing a debit balance), he/she is said to be insolvent, and the sum not recoverable is treated as capital loss for the firm. In the absence of any agreement, to the contrary, such a capital loss is to be borne by the remaining solvent partners in accordance with the principle laid down in Garner vs. Murray case, which states that the solvent partners have to bear such loss in the ratio of their capitals as on the date of dissolution. However, the accounting treatment relating to dissolution of partnership on account of insolvency of partners is not being taken up at this stage.

5.4 Accounting Treatment

When the firm is dissolved, its books of account are to be closed and the profit or loss arising on realisation of its assets and discharge of liabilities is to be computed. For this purpose, a Realisation Account is prepared to ascertain the net effect (profit or loss) of realisation of assets and payment of liabilities which may be is transferred to partner's capital accounts in their profit sharing ratio. Hence, all assets (other than cash in hand bank balance and fictitious assets, if any), and all external liabilities are transferred to this account. It also records the sale of assets, and payment of liabilities and realisation expenses. The balance in this account is termed as profit or loss on realisation which is transferred to partners' capital accounts in thier profit sharing ratio (see figure 5.1)

Dr. **Realisation Account** *Cr.*

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
Assets :		Liabilities :	
Land and Building	xxx	Sundry creditors	xxx
Plant and Machinery	xxx	Bills payables	xxx
Furniture and Fittings	xxx	Bank overdraft	xxx
Bills receivables	xxx	Outstanding expenses	xxx
Sundry debtors	xxx	Provision for doubtful debts	xxx
Cash/Bank	xxx	Cash/Bank (sale of assets)	xxx
(payment of liabilities)		Partner's capital account	xxx
Cash/Bank	xxx	(assets taken by the partner)	
(payment of unrecorded liabilities)		Loss (transferred to partners	xxx
Partner's capital account	xxx	capital accounts)	
(liability assumed by the partner)			
Profit (transferred to partners' capital account in their profit sharing ratio)	xxx		
Total	**xxxxx**	**Total**	**xxxxx**

Fig. 5.1: *Format of Realisation Account*

Illustration 1

Supriya and Monika are partners, who share profit in the ratio of 3:2. Following is the balance sheet as on March 31, 2007.

Balance Sheet of Supriya and Monika as on March 31, 2007

Liabilities	Amount (Rs.)	Assets		Amount (Rs.)
Supriya's Capital	32,500	Cash and Bank		40,500
Monika's Capital	11,500	Stock		7,500
Sundry Creditors	48,000	Sundry debtors	21,500	
Reserve fund	13,500	Less: Provision for doubtful debts	500	21,000
		Fixed Assets		36,500
	1,05,500			**1,05,500**

The firm was dissolved on March 31, 2007 . Close the books of the firm with the following information:

(i) *Debtors realised at a discount of 5%,*
(ii) *Stock realised at Rs.7,000,*
(iii) *Fixed assets realised at Rs.42,000,*
(iv) *Realisation expenses of Rs.1,500,*
(v) *Creditors are paid in full.*

Prepare necessary ledger accounts.

Solution

Books of Supriya and Monika
Realisation Account

Dr. Cr.

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
Assets transferred:			Provision for doubtful debts		500
Stock		7,500	Sundry Creditors		48,000
Sundry debtors		21,500	Bank		
Fixed assets		36,500	Debtors	20,425	
Bank			Stock	7,000	
Creditors		48,000	Fixed assets	42,000	69,425
Realisation expenses		1,500			
Profit transferred to:					
Supriya Capital	1,755				
Monika Capital	1,170	2,925			
		1,17,925			**1,17,925**

Partners Capital Accounts

Dr. Cr.

Date	Particulars	J.F.	Supriya (Rs.)	Monika (Rs.)	Date	Particulars	J.F.	Supriya (Rs.)	Monika (Rs.)
	Bank		42,355	18,070		Balance b/d		32,500	11,500
						Reserve fund		8,100	5,400
						Realisation (Profit)		1,755	1,170
			42,355	**18,070**				**42,355**	**18,070**

Cash and Bank Account

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		40,500		Realisation		48,000
	Realisation		69,425		Realisation		1,500
					Supriya's Capital		42,355
					Monika's Capital		18,070
			1,09,925				**1,09,925**

5.4.1 Journal Entries

1. *For trnasfer of assets*

   All asset accounts excluding cash, bank and the fictitious assets, if any are closed by transfer to the debit of Realisation Account at their book values. It may be noted that sundry debtors are transferred at gross value and the provision for doubtful debts is transferred to the credit side of Realisation Account along with liabilities. The same thing will apply to fixed assets, if provision for depreciation account is maintained.

   Realisation A/c Dr.
   To Assets (Individually) A/c

2. *For transfer of liabilities*

   All external liability accounts including provisions, if any, are closed by transferring them to the credit of Realisation account.

   Liabilities (individually) Dr.
   To Realisation A/c

3. *For sale of assets*

   Bank A/c Dr.
   To Realisation A/c

4. *For an asset taken over by a partner*

   Partner's Capital A/c Dr.
   To Realisation A/c

5. *For payment of liabilities*

   Realisation A/c Dr.
   To Bank A/c

6. *For a liability which a partner takes responsibility to discharge*

   Ralisation A/c Dr.
   To Partner's Capital A/c

7. *For settlement with the creditor through transfer of assets when a creditor accepts an asset in full and final settlement of his account, journal entry needs to be recorded. But, if the creditor accepts an asset only as part payment of his/her dues, the entry will be made for cash payment only. For example, a creditor to whom Rs. 10,000 was due accepts office equipment worth Rs. 8,000 and is paid Rs. 2,000 in cash, the following entry shall be made for the payment of Rs. 2,000 only.*

   Realisation A/c Dr.
   To Bank A/c

However, when a creditor accepts an asset whose value is more than the amount due to him, he/she will pay cash to the frim for the difference for which the entry will be:

   Bank A/c Dr.
   To Realisation A/c

8. *For payment of realisation expenses*

   (a) *When some expenses are incurred and paid by the firm in the process of realisation of assets and payment of liabilities:*

   Realisation A/c Dr.
   To Bank A/c

   (b) *When realisation expenses are paid by a partner on behalf of the firm:*

   Realisation A/c Dr.
   To Partner's Capital A/c

   (c) *When a partner has agreed to undertake the dissolution work for an agreed remuneration bear the realisation expenses:*

   (i) *if payment of realisation expenses is made by the firm*

   Partner's Capital A/c Dr.
   To Bank A/c

   (ii) *if the partner himself pays the realisation expenses, no entry is required*

   (iii) *For agreed remuneration to such partner*

   Realisation A/c Dr.
   To Partner's Capital A/c

9. *For realisation of any unrecorded assets including goodwill, if any*

   Bank A/c Dr.
   To Realisation A/c

10. *For settlement of any unrecorded liability*

   Realisation A/c Dr.
   To Bank A/c

11. *For transfer of profit and loss on realisation*

   (a) In case of profit on realisation
   Realisation A/c Dr.
   To Partners' Capital A/c (individually) A/c

   (b) In case of loss on realisation
   Partners' Capital A/c (individually) Dr.
   To Realisation A/c

12. *For transfer of accumulated profits in the form of reserve fund or general reserve:*

   Reserve Fund/General Reserve A/c Dr.
   To Partners' Capital A/c (individually)

13. *For transfer of fictitious assets, if any, to partners' capital accounts in their profit sharing ratio:*

   Partners' Capital A/c (individually) Dr.
   To Fictitious Asset A/c

14. *For payment of loans due to partners*

   Partner's Loan A/c Dr.
   To Bank A/c

15. *For settlement of partners' accounts*

   If the partner's capital account shows a debit balance, he brings in the necessary cash for which the entry will be:

   Bank A/c Dr.
   To Partner's Capital A/c

   The balance is paid to partners whose capital accounts show a credit balance and the following entry is recorded.

   Partners' Capitals A/cs (individually) Dr.
   To Bank A/c

It may be noted that the aggregate amount finally payable to the partners must equal to the amount available in bank and cash accounts. Thus, all accounts of a firm are closed in case of dissolution.

Test your Understanding – II

Tick (✓) the Correct Answer

1. *On dissolution of a firm, bank overdraft is transferred to :*
   (a) Cash Account
   (b) Bank Account
   (c) Realisation Aaccount
   (d) Partner's capital Account.
2. *On dissolution of a firm, partner's loan account is transferred to:*
   (a) Realisation Account
   (b) Partner's Capital Account
   (c) Partner's Current Account
   (d) None of the above.
3. *After transferring liabilities like creditors and bills payables in the Realisation Account, in the absence of any information regarding then payment, such liabilities are treated as:*
   (a) Never paid
   (b) Fully paid
   (c) Partly paid
   (d) None of the above.
4. *When realisation expenses are paid by the firm on behalf of a partner, such expenses are debited to:*
   (a) Realisation Account
   (b) Partner's Capital Account
   (c) Partner's Loan Account
   (d) None of the above.
5. *Unrecorded assets when taken over by a partner are shown in :*
   (a) Debit of Realisation Account
   (b) Debit of Bank Account
   (c) Credit of Realisation Account
   (d) Credit of Bank Account.
6. *Unrecorded liabilities when paid are shown in:*
   (a) Debit of Realisation Account
   (b) Debit of Bank Account
   (c) Credit of Realisation Account
   (d) Credit of Bank Account.
7. *The accumulated profits and reserves are transferred to :*
   (a) Realisation Account
   (b) Partners' Capital Accounts
   (c) Bank Account
   (d) None of the above.
8. *On dissolution of the firm, partner's capital accounts are closed through:*
   (a) Realisation Account
   (b) Drawings Account
   (c) Bank Account
   (d) Loan Account.

Illustration 2

Sita, Rita and Meeta are partners sharing profit and losses in the ratio of 2:2:1 Their balance sheet as on March 31, 2007 is as follows:

Balance Sheet of Sita, Rita and Meeta as on March 31, 2007

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Reserve fund		2,500	Cash at bank	2,500
Creditors		2,000	Stock	2,500
Capitals:			Furniture	1,000
Sita	5,000		Debtors	2,000
Rita	2,000		Plant and Machinery	4,500
Meeta	1,000	8,000		
		12,500		**12,500**

They decided to dissolve the business. The following amounts were realised: Plant and Machinery Rs.4,250, Stock Rs.3,500 and Debtors Rs.1850.

Sita agreed to bear all realisation expenses. For the service Sita is paid Rs.60.

Actual expenses on realisation amounted to Rs.450.Creditors paid 2% less. There was an unrecorded assets of Rs.250, which was taken over by Rita at Rs.200.

Prepare the necessary accounts to close the books of the firm.

Solution

Books of Sita, Rita and Meeta

Dr. **Realisation Account** *Cr.*

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
			Creditors		2,000
Stock		2,500	Rita's capital		200
Furniture		1,000	[Unrecorded assets]		
Debtors		2,000	Bank [assets realised]:		
Plant and Machinery		4,500	Plant and Machinery	4,250	
Bank [Creditors]		1,960	Debtors	1,850	
Sita's capital		60	Stock	3,500	
(realisation expenses]			Furniture	1,850	10,350
Profit transferred to:					
Sita's capital	212				
Rita's capital	212				
Meeta's capital	106	530			
		12,550			**12,550**

Dr. **Partner's Capital Accounts** Cr.

Date	Particulars	J.F.	Sita (Rs.)	Rita (Rs.)	Meeta (Rs.)	Date	Particulars	J.F.	Sita (Rs.)	Rita (Rs.)	Meeta (Rs.)
	Bank		450				Balance b/d		5,000	2,000	1,000
	Realisation (asset)			2,000			Reserve fund		1,000	1,000	500
	Bank		5,822	3,012	1,606		Realisation [profit]		212	212	106
							Realisation (expenses)		60	—	—
			6,272	**3,212**	**1,606**				**6,272**	**3,212**	**1,606**

Dr. **Bank Account** Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		2,500		Realisation (Creditor)		1,960
	Realisation (assets realised)		10,350		Sita's Capital [expenses]		450
					Sita's Capital		5,822
					Rita's Capital		3,012
					Meeta's capital		1,606
			12,850				**12,850**

llustration 3

Nayana and Arushi were partners sharing profits equally Their Balance Sheet as on March 31, 2007 was as follows:

Balance Sheet of Nayana and Arushi as on March 31, 2007

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capitals:			Bank	30,000
Nayana	1,00,000		Debtors	25,000
Arushi	50,000	1,50,000	Stock	35,000
Creditors		20,000	Furniture	40,000
Arushi's current account		10,000	Machinery	60,000
Workmen Compensation Fund		15,000	Nayana's current account	10,000
Bank overdraft		5,000		
		2,00,000		**2,00,000**

The firm was dissolved on the above date:

1. *Nayana took over 50% of the stock at 10% less on its book value, and the remaining stock was sold at a gain of 15%. Furniture and Machinery realised for Rs.30,000 and Rs.50,000 respectively;*
2. *There was an unrecorded investment which was sold for Rs. 25,000;*

3. *Debtors realised 90% only and Rs.1,200 were recovered for bad debts written-off last year;*
4. *There was an outstanding bill for repairs which had to be paid for Rs.2,000.*

Record necessary journal entries and prepare ledger accounts to close the books of the firm.

Solution

Books of Nayana and Arushi
Journal

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Realisation A/c Dr.		1,60,000	
	To Debtors			25,000
	To Stock A/c			35,000
	To Furniture A/c			40,000
	To Machinery A/c			60,000
	(Assets transferred to Realisation Account)			
	Creditors A/c Dr.		20,000	
	Bank overdraft A/c Dr.		5,000	
	To Realisation A/c			25,000
	(Liabilities transferred to Realisation Account)			
	Realisation A/c Dr.		27,000	
	To Bank A/c			27,000
	(Creditors, Bank overdraft, Outstanding repair bill paid)			
	Bank A/c Dr.		1,57,825	
	To Realisation A/c			1,57,825
	(Assets sold and bad debts recovered)			
	Nayana's Capital A/c Dr.		15,750	
	To Realisation A/c			15,750
	(Half stock take over by Nayana at 10% less)			
	Realisation A/c Dr.		15,575	
	To Nayana's Current A/c			5,788
	To Arushi's Current A/c			5,787
	(Realisation profit transferred to partner's current account)			
	Workman Compensation Fund A/c Dr.		15,000	
	To Nayana's Current A/c			7,500
	To Arushi's Current A/c			7,500
	(Compensation fund transfered to partners Current accounts)			

	Arushi Current A/c *Dr.* *To Arushi's Capital A/c* *(Current account balance transferred to Capital account)*		23,287	23,287
	Nayana Capital A/c *Dr.* *To Nayana's Current A/c* *(Current account balance transferred to Capital account)*		12,462	12,462
	Nayana's Capital A/c *Dr.* *Arushi's Capital A/c* *Dr.* *To Bank A/c* *(Final amounts due to partners paid)*		87,538 73,287	1,60,825

Realisation Account

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*		*Amount (Rs.)*
			Creditors		20,000
Debtors	25,000		Bank overdraft		5,000
Stock	35,000		Bank:		
Furniture	40,000		Investment	25,000	
Machinery	60,000	1,60,000	Furniture	30,000	
Bank:			Machinery	50,000	
Creditors	20,000		Debtors (90%)	31,500	
Bank overdraft	5,000		Stock :	20,125	
Outstanding bill	2,000	27,000	Bad debts		
Profit transferred to :			recovered	1,200	1,57,825
Nayana's capital	5,788		Nayana's capital		
Arushi's capital	5,787	11,575	(stock taken over)		15,750
		1,98,575			**1,98,575**

Partners' Current Accounts

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Nayana (Rs.)*	*Arushi (Rs.)*	*Date*	*Particulars*	*J.F.*	*Nayana (Rs.)*	*Arushi (Rs.)*
	Balance b/d		10,000			Balance b/d			10,000
	Realisation		15,750			Workmen		7,500	7,500
	Arushi's capital			23,287		Compensation			
						Fund			
						Realisation (profit)		5,788	5,787
						Nayana's Capital		12,462	
			25,750	**23,287**				**25,750**	**23,287**

Partner's Current Accounts

Dr. Cr.

Date	Particulars	J.F.	Nayana (Rs.)	Arushi (Rs.)	Date	Particulars	J.F.	Nayana (Rs.)	Arushi (Rs.)
	Nayana's current account		12,462			Balance b/d		1,00,000	50,000
	Bank		87,538	73,287		Arushi's current account			23,287
			1,00,000	**73,287**				**1,00,000**	**73,287**

Bank Account

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		30,000		Realisation		27,000
	Realisation		1,57,825		Nayana's capital		87,538
					Arushi's capital		73,287
			1,87,825				**1,87,825**

Test your Understanding – III

Fill in the Correct Word(s):

1. *All assets (except cash/bank and fictitious assets) are transferred to the ———— (Debit/Credit) side of ———— Account (Realisation/Capital).*
2. *All ———— (internal/external) liabilities are transferred to the ———— (Debit/Credit) side of ————acccount (Bank/Realisation).*
3. *Accumulated losses are transferred to ———— (Current/Capital Accounts) in ———— (equal ratio/profit sharing ratio).*
4. *If a liability is assumed by a partner, such Partner's Capital Account is ———— (debited/credited).*
5. *If a partner takes over an asset, such (Partner's Capital Account) is ———— (debited/credited).*
6. *No entry is required when a ———— (partner/creditor) accepts a fixed asset in payment of his dues.*
7. *When creditor accepts an asset whose value is more than the amount due to him, he will ———— (pay/not pay) the excess amount which will be credited ———— Account.*
8. *When the firm has agreed to pay the partner a fixed amount for realisation work irrespective of the actual amount spent, such fixed amount is debited to (Realisation/Capital) Account and Credited to (Capital/Bank) Account.*
9. *Partner's loan is ———— (recorded/not recorded) in the (Realisation Account).*
10. *Partner's current accounts are transferred to respective ———— Partners' (Loan/Capital) Accounts.*

Illustration 4

Following is the Balance Sheet of Ashwani and Bharat on March 31, 2007.

Balance Sheet Ashwani and Bharat as on March 31, 2007

Liabilities		Amount (Rs.)	Assets		Amount (Rs.)
Creditors		76,000	Cash at bank		17,000
Mrs.Ashwani's loan		10,000	Stock		10,000
Mrs.Bharat loan		20,000	Investments		20,000
Investment fluctuation fund		2,000	Debtors	40,000	
Reserve fund		20,000	Less: Provision		
Capitals:			for doubtful debts	4,000	36,000
Ashwani	20,000		Buildings		70,000
Bharat	20,000	40,000	Goodwill		15,000
		1,68,000			**1,68,000**

The firm was dissolved on that date. The following was agreed transactions took place.

(i) *Aswhani promised to pay Mrs. Ashwani's loan and took away stock for Rs.8,000.*

(ii) *Bharat took away half of the investment at 10% less. Debtors realised for Rs.38,000. Creditor's were paid at less of Rs.380. Buildings realised for Rs.1,30,000, Goodwill Rs.12,000 and the remaining Investment were sold at Rs.9,000. An old typewriter not recorded in the books was taken over by Bharat for Rs. 600. Realisation expenses amounted to Rs. 2,000.*

Prepare Realisation Account, Partner's Capital Account and Bank Account.

Solution

Books of Ashwani and Bharat

Realisation Account

Dr. Cr.

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
Investment	20,000		Provision for doubtful debts		4,000
Debtors	40,000		Creditors		76,000
Buildings	70,000		Mrs. Ashwani loan		10,000
Stock	10,000		Mrs. Bharat loan		20,000
Goodwill	15,000	1,55,000	Investment fluctuation fund		2,000
Ashwani's Capital		10,000	Ashwani's Capital[stock]		8,000
(Mrs.Ashwani's loan}			Bharat's capital (Typewriter)		600
Bank (Mrs. Bharat's loan)		20,000	Bharat's capital (Investment)		9,000
Bank (creditors)		75,620	Bank:		
Bank (realisation expenses)		2,000	Investment	9,000	
Profit transferred to:			Debtors	38,000	
Ashwani's Capital	27,990		Buildings	1,30,000	
Bharat's Capital	27,990	55,980	Goodwill	12,000	1,89,000
		3,18,600			**3,18,600**

Partner's Capital Accounts

Dr. Cr.

Date	Particulars	J.F.	Ashwani (Rs.)	Bharat (Rs.)	Date	Particulars	J.F.	Ashwani (Rs.)	Bharat (Rs.)
	Realisation (stock)		8,000	—		Balance b/d		20,000	20,000
	Realisation [sale of typewriter]			600		Reserve fund		10,000	10,000
	Realisation [investment]			9,000		Realisation [Mrs. Ashwini's loan]		10,000	—
	Bank		59,990	48,390		Realisation (profit)		27,990	27,990
			67,990	**57,990**				**67,990**	**57,990**

Bank Account

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		17,000		Realisation [creditors]		75,620
	Realisation		1,89,000		Realisation [expenses]		2,000
					Realisation (Mrs.Bharat's loan)		20,000
					Ashwani's capital		59,990
					Bharat's capital		48,390
			2,06,000				**2,06,000**

Do it Yourself

Give the journal entry(ies) to be recorded for the following, in case of the dissolution of a partnership firm.

1. *For closure of assets accounts.*
2. *For closure of liabilities accounts.*
3. *For sale of assets.*
4. *For settlement of a creditor by transfer of fixed assets to him.*
5. *For expenses of realisation when actual expenses are paid by the partner on behalf of the firm.*
6. *When a partner discharges the liability of the firm.*
7. *For payment of partner's loan.*
8. *For settlement of capital accounts.*

Illustration 5

Sonia, Rohit and Udit are partners sharing profits in the ratio of 5:3:2. Their Balance Sheet as on March 31, 2007 was as follows:

Balance Sheet of Sonia, Rohit and Udit as on March 31, 2007

Liabilities		*Amount (Rs.)*	*Assets*	*Amount (Rs.)*
Creditors		30,000	Buildings	2,00,000
Bills payable		30,000	Machinery	40,000
Bank loan		1,20,000	Stock	1,60,000
Sonia's husband's loan		1,30,000	Bills receivable	1,20,000
General reserve		80,000	Furniture	80,000
Capitals:			Cash at bank	60,000
Sonia	70,000			
Rohit	90,000			
Udit	1,10,000	2,70,000		
		6,60,000		**6,60,000**

The firm was dissolved on that date. Close the books of the firm with following information:

1. *Buildings realised for Rs.1,90,000, Bills receivable realised for Rs.1,10,000; Stock realised Rs.1,50,000; and Machinery sold for Rs.48,000 and furniture for Rs. 75,000,*
2. *Bank loan was settled for Rs.1,30,000. Creditors and Bills payable were settled at 10% discount,*
3. *Rohit paid the realisation expenses of Rs.10,000 and he was to get a remuneration of Rs.12,000 for completing the dissolution process.*

Prepare necessary ledger accounts.

Solution

Books of Sonia, Rohit and Udit

Dr. **Realisation Account** *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*		*Amount (Rs.)*
Buildings	2,00,000		Creditors		30,000
Machinery	40,000		Bills payable		30,000
Stock	1,60,000		Bank loan		1,20,000
Bills receivable	1,20,000		Sonia's husband's loan		1,30,000
Furniture	80,000	6,00,000	Bank:		
Bank (Bank Loan)		1,30,000	Buildings	1,90,000	
Bank			Bills receivable	1,10,000	
[creditors and Bills payable]		54,000	Stock	1,50,000	
Bank [Sonia's husbands loan]		1,30,000	Machinery	48,000	
Rohit's capital		12,000	Furniture	75,000	5,73,000
(reslisation expenses)			Loss transferred to		
			capital accounts:		
			Sonia	21,500	
			Rohit	12,900	
			Udit	8,600	43,000
		9,26,000			**9,26,000**

Partner's Capital Accounts

Dr. Cr.

Date	Particulars	J.F.	Sonia (Rs.)	Rohit (Rs.)	Udit (Rs.)	Date	Particulars	J.F.	Sonia (Rs.)	Rohit (Rs.)	Udit (Rs.)
	Realisation (Loss)		21,500	12,900	8,600		Balance b/d		70,000	90,000	1,10,000
	Bank		88,500	1,13,100	1,17,400		Realisation (expenses)		—	12,000	—
							General reserve		40,000	24,000	16,000
			1,10,000	**1,26,000**	**1,26,000**				**1,10,000**	**1,26,000**	**1,26,000**

Bank Account

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		60,000		Realisation [bank loan]		1,30,000
	Realisation (assets realised)		5,73,000		Realisation [creditors and bills payable]		54,000
					Realisation (Sonia's husband loan)		1,30,000
					Sonia's capital		88,500
					Rohit's capital		1,13,100
					Udit's capital		1,17,400
			6,33,000				**6,33,000**

Note: *No entry has been recorded in firm's books for the actual realisation expenses incurred by Rohit because he gets Rs. 12,000 as his remuneration which has been duly accounted for.*

Illustration 6

Romesh and Bhawan were in partnership sharing profit and losses as 3:2. Their Balance Sheet as on March 31, 2007, was as follows:

Balance Sheet of Romesh and Bhawan as on March 31, 2007

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Bank loan		60,000	Cash at bank	30,000
Creditors		80,000	Debtors	70,000
Bills payables		40,000	Stock	2,00,000
Bhawan loan		20,000	Investments	1,40,000
Capitals:			Buildings	60,000
Romesh	1,00,000			
Bhawan	2,00,000	3,00,000		
		5,00,000		**5,00,000**

They decided to dissolve the firm. The following information is available:

1. *Debtors were recovered 5% less. Stock was realised at books value and building was sold for Rs.51,000,*
2. *It is found that investment not recorded in the books amounted to Rs.10,000. The same were accepted by one creditor for this amount and other Creditors were paid at a discount of 10%. Bills payable were paid full,*
3. *Romesh took over some of the Investments at Rs.8,100 (book value less 10%). The remaining investment were taken over by Bhawan at 90% of the book value less Rs.900 discount,*
4. *Bhawan paid bank loan along with one year interest at 6% p.a,*
5. *An unrecorded liability of Rs.5,000 paid.*

Close the books of the firm and prepare necessary ledger accounts.

Solution

Books of Romesh and Bhawan
Realisation Account

Dr. *Cr.*

Particulars		*Amount (Rs.)*	*Particulars*		*Amount (Rs.)*
			Bank loan		*60,000*
Debtors	*70,000*		*Creditors*		*80,000*
Stock	*2,00,000*		*Bills payable*		*40,000*
Investments	*1,40,000*		*Romesh's Capital (investment)*		*8,100*
Buildings	*60,000*	*4,70,000*	*Bhawan's Capital (investment)*		*1,17,000*
Bank (bills payable)		*40,000*	*Bank:*		
Bank (creditors)		*63,000*	*Debtors*	*66,500*	
Bhawan's capital		*63,600*	*Stock*	*2,00,000*	
(loan with interest)			*Buildings*	*51,000*	*3,17,500*
Bank (unrecorded liabilities)		*5,000*	*Loss transferred to :*		
			Romesh capital	*11,400*	
			Bhawan capital	*7,600*	*19,000*
		6,41,600			**6,41,600**

Partner's Capital Accounts

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Romesh (Rs.)*	*Bhawan (Rs.)*	*Date*	*Particulars*	*J.F.*	*Romesh (Rs.)*	*Bhawan (Rs.)*
	Realisation [investment]		*8,100*	*1,17,000*		Balance b/d		*1,00,000*	*2,00,000*
	Realisation [loss]		*11,400*	*7,600*		Realisation [bank loan]			*63,600*
	Bank		*80,500*	*1,39,000*					
			1,00,000	**2,63,600**				**1,00,000**	**2,63,600**

Bank Account

Dr. *Cr.*

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		30,000		Realisation[creditor]		63,000
	Realisation (assets realised)		3,17,500		Realisation [unrecorded liability]		5,000
					Bhawan loan		20,000
					Realisation (bills payable]		40,000
					Romesh's capital		80,500
					Bhawan's capital		1,39,000
			3,47,500				**3,47,500**

Note: No entry has been made for acceptance of unrecorded investments by a creditor as part payment of his dues as per rules.

Illustration 7

Sonu and Ashu sharing profits as 3:1 and they agree upon dissolution. The Balance Sheet as on March 31, 2006 is as under:

Balance Sheet of Sonu and Ashu as on March 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Loan		12,000	Cash at bank	25,000
Creditors		18,000	Stock	45,000
Capital			Furniture	16,000
Sonu	1,10,000		Debtors	70,000
Ashu	68,000	1,78,000	Plant and Machinery	52,000
		208,000		**2,08,000**

Sonu took over plant and machinery at an agreed value of Rs.60,000. Stock and Furniture were sold for Rs.42,000 and Rs.12,000 respectively. Debtors were took over by Ashu at Rs.69,000. Creditors were paid subject to discount of Rs.900. Sonu agrees to pay the loans. Realisation expenses were Rs.1,600.

Prepare Realisation Account, Bank Account and Capital Accounts of the Partners.

Solution

Books of Sonu and Ashu
Realisation Account

Dr. *Cr.*

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
Stock		45,000	Loan		12,000
Furniture		16,000	Creditors		18,000
Debtors		70,000	Sonu's capital (plant& machinery)		60,000
Plant and Machinery		52,000	Ashu's capital (debtors)		69,000
Bank (creditors)		17,100	Bank:		
Sonu's capital (loan)		12,000	Stock	42,000	
Bank (realisation expenses)		1,600	Furniture	13,900	55,900
Profit transferred to :					
Sonu's capital	900				
Ashu's capital	300	1,200			
		2,14,900			**2,14,900**

Partners Capital Accounts

Dr. *Cr.*

Date	Particulars	J.F.	Sonu (Rs.)	Ashu (Rs.)	Date	Particulars	J.F.	Sonu (Rs.)	Ashu (Rs.)
	Realisation [plant and machinery]		60,000			Balance b/d		1,10,000	68,000
	Realisation [debtors]			69,000		Realisation [loan]		12,000	
	Bank		62,900			Realisation [profit]		900	300
						Bank			700
			1,22,900	**69,000**				**1,22,900**	**69,000**

Bank Account

Dr. *Cr.*

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		25,000		Realisation [creditor]		17,100
	Realisation (assets realised)		55,900		Realisation [expenses]		1,600
	Ashu's capital		700		Sonu's capital		62,900
			81,600				**81,600**

Illustration 8

Anju, Manju and Sanju sharing profit in the ratio of 3:1:1 decided to dissolve their firm. On March 31, 2006 their position was as follows:

Balance Sheet Anju, Manju and Sanju as on March 31, 2006

Liabilities		Amount (Rs.)	Assets		Amount (Rs.)
Creditors		60,000	Cash at bank		35,000
Loan		15,000	Stock		83,000
Capitals:			Furniture		12,000
Anju	2,75,000		Debtors	2,42,000	
Manju	1,10,000		*Less:* Provision for		
Sanju	1,00,000	4,85,000	doubtful debts	12,000	2,30,000
			Buildings		2,00,000
		5,60,000			**5,60,000**

It is agreed that:

1. *Anju takes over the Furniture at Rs.10,000 and Debtors amounting to Rs.2,00,000 at Rs.1,85,000. Anju also agrees to pay the Creditors,*
2. *Manju is to take over Stock at book value and Buildings at book value less 10%,*
3. *Sanju is to take over remaining Debtors at 80% of book value and responsibility for the discharge of the loan,*
4. *The expenses of dissolution amounted to Rs.2,200.*

Prepare Realisation Account, Bank Account and Capital Accounts of the partners.

Solution

Books of Anju, Manju and Sanju

Dr. **Realisation Account** Cr.

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
			Provision for doubtful debts		12,000
Stock	83,000		Creditors		60,000
Furniture	12,000		Loan		15,000
Debtors	2,42,000		Anju's capital :		
Buildings	2,00,000	5,37,000	Furniture	10,000	
Anju capital (creditors)		60,000	Debtors	1,85,000	1,95,000
Sanju capital (loan)		15,000	Manju's capital :		
Bank (realisation expenses)		2,200	Stock	83,000	
			Buildings	1,80,000	2,63,000
			Sanju's capital :		
			(remaning debtors less		
			20% of book value)		33,600
			Loss transferred to :		
			Anju's capital	21,360	
			Manju's capital	7,120	
			Sanju's capital	7,120	35,640
		6,14,200			**6,14,240**

Dr. **Partner's Capital Accounts** Cr.

Date	Particulars	J.F.	Anju (Rs.)	Manju (Rs.)	Sanju (Rs.)	Date	Particulars	J.F.	Anju (Rs.)	Manju (Rs.)	Sanju (Rs.)
	Realisation (assets)		1,95,000	2,63,000	33,600		Balance b/d		2,75,000	1,10,000	1,00,000
	Realisation (loss)		21,360	7,120	7,120		Realisation (creditors)		60,000		
	Bank		1,18,640		74,280		Realisation (loan)				15,000
							Bank			1,60,120	
			3,35,000	**2,70,120**	**1,15,000**				**3,35,000**	**2,70,120**	**1,15,000**

Dr. **Bank Account** Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		35,000		Sita's capital (expenses)		2,200
	Manju's capital		1,60,120		Anju's capital		1,18,640
					Sanju's capital		74,280
			1,95,120				**1,95,120**

Illustration 9

Sumit, Amit and Vinit are partners sharing profit in the ratio of 5:3:2. Their Balance Sheet as on March 31, 2007 was as follows:

Balance Sheet of Sunit, Amit and Vinit as on March 31, 2007

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capitals:			Machinery	80,000
Sumit	40,000		Investments	1,50,000
Amit	50,000		Stock	10,000
Vinit	60,000	1,50,000	Debtors	35,000
Profit and Loss		10,000	Cash at bank	15,000
Mrs. Amit's loan		40,000		
Sundry creditors		90,000		
		2,90,000		**2,90,000**

The firm was dissolved on that date. Amit took over his wife's loan. One of the Creditors for Rs.2,600 was not claim the amount. Other assets realised as follows:

1. *Machinery was sold for Rs.70,000,*
2. *Investments with book value of Rs.1,00,000 were given to Creditors in full settlement of their account. The remaining Investments were took over by Vinit at an agreed value of Rs.45,000,*

3. *Stock was sold for Rs.11,000 and Debtors for Rs.3,000 proved to be bad,*
4. *Realisation expenses were Rs.1,500.*

Prepare ledger accounts to close the books of the firm.

Solution

Books of Amit, Sumit and Vinit
Realisation Account

Dr. Cr.

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
Machinery	80,000		Sundry Creditors		90,000
Investments	1,50,000		Mrs.Amit's loan		40,000
Stock	10,000		Bank :		
Debtors	35,000	2,75,000	Machinery	70,000	
Amit's Capital (wife's loan)		40,000	Stock	11,000	
Bank (realisation expenses)		1,500	Debtors	32,000	1,13,000
			Vinit's capital (investment)		45,000
			Loss transferred to :		
			Amit's capital	14,250	
			Sumit's capital	8,550	
			Vinit's capital	5,700	28,500
		3,16,500			**3,16,500**

Partners Capital Accounts

Dr. Cr.

Date	Particulars	J.F.	Amit (Rs.)	Sumit (Rs.)	Vinit (Rs.)	Date	Particulars	J.F.	Amit (Rs.)	Sumit (Rs.)	Vinit (Rs.)
	Realisation (assets)				45,000		Balance b/d		40,000	50,000	60,000
	Realisation (loss)		14,250	8,550	5,700		Realisation (Mrs. Vinit's loan)		40,000		
	Bank		70,750	44,450	11,300		Profit and Loss		5,000	3,000	2,000
			85,000	**53,000**	**62,000**				**85,000**	**53,000**	**62,000**

Bank Account

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs.)	Date	Particulars	J.F.	Amount (Rs.)
	Balance b/d		15,000		Realisation (expenses)		1,500
	Realisation (assets realised)		1,13,000		Amit's capital		70,750
					Sumit's capital		44,450
					Vinit's capital		11,300
			1,28,000				**1,28,000**

Note: No entry has been made for the investments taken over by the creditors as per rules.

Illustration 10

Meena and Tina are partners in a firm and sharing profit as 3:2. They decided to dissolve their firm on March 31, 2007 when their Balance Sheet was a follows:

Balance Sheet Meena and Tina as on March 31, 2007

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capital :			Machinery	70,000
Meena	90,000		Investments	50,000
Tina	80,000	1,70,000	Stock	22,000
Sundry Creditors		60,000	Sundry Debtors	1,03,000
Bills payable		20,000	Cash at bank	5,000
		2,50,000		**2,50,000**

The assets and liabilities were disposed off as follows :

(a) *Machinery were given to creditors in full settlement of their account and Stock were given to bills payable in full settlement.*

(b) *Investment were took over by Tina at book value. Sundry debtors of book value Rs. 50,000 took over by Meena at 10% less and remaining debtors realised Rs. 51,000.*

(c) *Realisation expenses amount to Rs. 2,000.*

Prepare necessary ledger accounts to close the book of the firm.

Solution

Books of Meena and Tina – Realisation Account

Particulars		Amount (Rs.)	Particulars		Amount (Rs.)
Assets transferred :			Sundry Creditors		60,000
Machinery	70,000		Bills payable		20,000
Investments	50,000		Tina's Capital (investment)		50,000
Stock	22,000		Meena's Capital (debtors of books value Rs. 50,000 less 10%)		45,000
Sundry Debtors	1,03,000	2,45,000	Bank		
Bank (realisation expenses)		2,000	Debtors		51,000
			Loss transferred to :		
			Mena's capital	12,600	
			Tena's capital	8,400	21,000
		2,47,000			**2,47,000**

Partner's Capital Accounts

Dr. *Cr.*

Particulars	Mena (Rs.)	Tina (Rs.)	Particulars	Mena (Rs.)	Tina (Rs.)
Realisation (investment)		50,000	Balance b/d	90,000	80,000
Realisation (debtors)	45,000				
Realisation (loss)	12,600	8,400			
Bank	32,400	21,600			
	90,000	**80,000**		**90,000**	**80,000**

Bank Account

Dr. *Cr.*

Particulars	*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
Balance b/d	5,000	Realisation (expenses)	2,000
Realisation (assets realised)	51,000	Mena's capital	32,400
		Tina's capital	21,600
	56,000		**56,000**

Terms Introduced in the Chapter

1. Dissolution of Partnership
2. Dissolution of Partnership Firm
3. Partnership at Will
4. Compulsory Dissolution
5. Dissolution by Notice
6. Realisation Expenses
7. Realisation Account

Summary

1. *Dissolution of Partnership Firm :* The dissolution of a firm implies the discontinuance of partnership business and separation of economic relations between the partners. In the case of a dissolution of a firm, the firm closes its business altogether and realises all its assets and pays all its liabilities. The payment is made to the creditors first out of the assets realised and, if necessary, next out of the contributions made by the partners in their profit sharing ratio. When all accounts are settled and the final payment is made to the partners for the amounts due to them, the books of the firm are closed.
2. *Dissolution of Partnership :* A partnership gets terminated in case of admission, retirement death, etc. of a partner. This does not necessarily involve dissolution of the firm.
3. *Realisation Account :* The Realisation Account is prepared to record the transactions relating to sale and realisation of assets and settlement of creditors. Any profit or loss arising act of this process is shared by partners' in their profit sharing ratio. Partners' accounts are also settled and the Cash or Bank account is closed.

Questions for Practice

Short Answer Questions

1. State the difference between dissolution of partnership and dissolution of partnership firm.
2. State the accounting treatment for:
   i. Unrecorded assets ii. Unrecorded liabilities
3. On dissolution, how will you deal with partner's loan if it appears on the (a) assets side of the balance sheet, (b) liabilities side of balance sheet.

4. *Distinguish between firm's debts and partner's private debts.*
5. *State the order of settlement of accounts on dissolution.*
6. *On what account Realisation Account differs from Revaluation Account.*

Long Answer Questions

1. *What is meant by dissolution of partnership firm?*
2. *What is a Realisation Account?*
3. *Reproduce the format of Realisation Account.*
4. *How deficiency of Crditors is paid off?*

Numerical Questions

1. *Journalise the following transactions regarding realisation expenses :*
   [a] *Realisation expenses amounted to Rs.2,500.*
   [b] *Realisation expenses amounting to Rs.3,000 were paid by Ashok, one of the partners.*
   [c] *Realisation expenses Rs.2,300 borne by Tarun, personally.*
   [d] *Amit, a partner was appointed to realise the assets, at a cost of Rs.4,000. The actual amount of realisation amounted to Rs.3,000.*
2. *Record necessary journal entries in the following cases:*
   [a] *Creditors worth Rs.85,000 accepted Rs.40,000 as cash and Investment worth Rs.43,000, in full settlement of their claim.*
   [b] *Creditors were Rs.16,000. They accepted Machinery valued at Rs.18,000 in settlement of their claim.*
   [c] *Creditors were Rs.90,000. They accepted Buildings valued Rs.1,20,000 and paid cash to the firm Rs.30,000.*
3. *There was an old computer which was written-off in the books of accounts in the pervious year. The same has been taken over by a partner Nitin for Rs.3,000. Journalise the transaction, supposing. That the firm has been dissolved.*
4. *What journal entries will be recorded for the following transactions on the dissolution of a firm:*
   [a] *Payment of unrecorded liabilities of Rs.3,200.*
   [b] *Stock worth Rs.7,500 is taken by a partner Rohit.*
   [c] *Profit on Realisation amounting to Rs.18,000 is to be distributed between the partners Ashish and Tarun in the ratio of 5:7.*
   [d] *An unrecorded asset realised Rs.5,500.*
5. *Give journal entries for the following transactions :*
   1. *To record the realisation of various assets and liabilities,*
   2. *A Firm has a Stock of Rs. 1,60,000. Aziz, a partner took over 50% of the Stock at a discount of 20%,*
   3. *Remaining Stock was sold at a profit of 30% on cost,*
   4. *Land and Buildging (book value Rs. 1,60,000) sold for Rs. 3,00,000 through a broker who charged 2%, commission on the deal,*
   5. *Plant and Machinery (book value Rs. 60,000) was handed over to a Creditor at an agreed valuation of 10% less than the book value,*
   6. *Investment whose face value was Rs. 4,000 was realised at 50%.*

6. *How will you deal with the realisation expenses of the firm of Rashim and Bindiya in the following cases:*
   1. *Realisation expenses amounts to Rs. 1,00,000,*
   2. *Realisation expenses amounting to Rs. 30,000 are paid by Rashim, a partner.*
   3. *Realisation expenses are to be borne by Rashim for which he will be paid Rs. 70,000 as remuneration for completing the dissolution process. The actual expenses incurred by Rashim were Rs. 1,20,000.*

7. *The book value of assets (other than cash and bank) transferred to Realisation Account is Rs. 1,00,000. 50% of the assets are taken over by a partner Atul, at a discount of 20%; 40% of the remaining assets are sold at a profit of 30% on cost; 5% of the balance being obsolete, realised nothing and remaining assets are handed over to a Creditor, in full settlement of his claim.*

   You are required to record the journal entries for realisation of assets.

8. *Record necessary journal entries to record the following unrecorded assets and liabilities in the books of Paras and Priya:*
   1. *There was an old furniture in the firm which had been written-off completely in the books. This was sold for Rs. 3,000,*
   2. *Ashish, an old customer whose account for Rs. 1,000 was written-off as bad in the previous year, paid 60%, of the amount,*
   3. *Paras agreed to takeover the firm's goodwill (not recorded in the books of the firm), at a valuation of Rs. 30,000,*
   4. *There was an old typewriter which had been written-off completely from the books. It was estimated to realize Rs. 400. It was taken away by Priya at an estimated price less 25%,*
   5. *There were 100 shares of Rs. 10 each in Star Limited acquired at a cost of Rs. 2,000 which had been written-off completely from the books. These shares are valued @ Rs. 6 each and divided among the partners in their profit sharing ratio.*

9. *All partners wishes to dissolve the firm. Yastin, a partner wants that her loan of Rs. 2,00,000 must be paid off before the payment of capitals to the partners. But, Amart, another partner wants that the capitals must be paid before the payment of Yastin's loan. You are required to settle the conflict giving reasons.*

10. *What journal entries would be recorded for the following transactions on the dissolution of a firm after various assets (other than cash) on the third party liabilities have been transferred to Reliasation account.*
    1. *Arti took over the Stock worth Rs. 80,000 at Rs. 68,000.*
    2. *There was unrecorded Bike of Rs. 40,000 which was taken over By Mr. Karim.*
    3. *The firm paid Rs. 40,000 as compensation to employees.*
    4. *Sundry creditors amounting to Rs. 36,000 were settled at a discount of 15%.*
    5. *Loss on realisation Rs. 42,000 was to be distributed between Arti and Karim in the ratio of 3:4.*

11. *Rose and Lily shared profits in the ratio of 2:3. Their Balance Sheet on March 31, 2006 was as follows:*

Balance Sheet of Rose and Lily as on March 31, 2006

Liabilities	Amount (Rs.)	Assets		Amount (Rs.)
Creditors	40,000	Cash		16,000
Lily's loan	32,000	Debtors	80,000	
Profit and Loss	50,000	Less: Provision for		
Capitals:		doubtful debts	3,600	76,400
Lily	1,60,000	Inventory		1,09,600
Rose	2,40,000	Bills receivable		40,000
		Buildings		2,80,000
	5,22,000			**5,22,000**

Rose and Lily decided to dissolve the firm on the above date. Assets (except bills receivables) realised Rs. 4,84,000. Bills Receivable were taken over by Rose at Rs. 30,000. Creditors agreed to take Rs. 38,000. Cost of realisation was Rs. 2,400. There was a Motor Cycle in the firm which was bought out of the firm's money, was not shown in the books of the firm. It was now sold for Rs. 10,000. There was a contingent liability in respect of outstanding electric bill of Rs. 5,000 Bill Receivable taken over by Rose at Rs. 33,000.

Show Realisation Account, Partners Capital Acount, Loan Account and Cash Account.

(**Ans :** *Realisation Profit Rs. 15,600, Total of Cash Account Rs. 5,10,000)*

12. *Shilpa, Meena and Nanda decided to dissolve their partnership on March 31,2006. Their profit sharing ratio was 3:2:1 and their Balance Sheet was as under:*

Balance Sheet of Shilpa, Meena and Nanda as on March 31, 2006

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Capitals:		Land	81,000
Shilpa	80,000	Stock	56,760
Meena	40,000	Debtors	18,600
Bank loan	20,000	Nanda's capital	23,000
Creditors	37,000	Cash	10,840
Provision for doubtful debts	1,200		
General reserve	12,000		
	1,90,200		**1,90,200**

The stock of value of Rs. 41,660 are taken over by Shilpa for Rs. 35,000 and she agreed to discharge bank loan. The remaining stock was sold at Rs. 14,000 and debtors amounting to Rs. 10,000 realised Rs. 8,000. land is sold for Rs. 1,10,000. The remaining debtors realised 50% at their book value. Cost of realisation amounted to Rs. 1,200. There was a typewriter not recorded in the books worth Rs. 6,000 which were taken over by one of the Creditors at this value. Prepare Realisation Account.

(**Ans :** *Profit on Realisation Rs. 20,940, Total of Cash Account Rs. 1,64,650)*

13. *Surjit and Rahi were sharing profits (losses) in the ratio of 3:2, their Balance Sheet as on March 31, 2004 is as follows:*

Balance Sheet of Surjit and Rahi as on March 31, 2004

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Creditors	38,000	Bank	11,500
Mrs. Surjit loan	10,000	Stock	6,000
Reserve	15,000	Debtors	19,000
Rahi's loan	5,000	Furniture	4,000
Capital's:		Plant	28,000
Surjit	10,000	Investment	10,000
Rahi	8,000	Profit and Loss	7,500
	86,000		**86,000**

The firm was dissolved on March 31, 2006 on the following terms:

1. *Surjit agreed to take the investments at Rs. 8,000 and to pay Mrs. Surojit's loan.*
2. *Other assets were realised as follows:*

Stock	Rs. 5,000
Debtors	Rs. 18,500
Furniture	Rs. 4,500
Plant	Rs. 25,000

3. *Expenses on realisation amounted to Rs. 1,600.*
4. *Creditors agreed to accept Rs. 37,000 as a final settlement.*

   You are required to prepare Realisation account, Partner's Capital account and Bank account.

(**Ans :** *Loss on Realisation Rs. 6,600, Total of Cash Account Rs. 64,500)*

14. *Rita, Geeta and Ashish were partners in a firm sharing profits/losses in the ratio of 3:2:1. On March 31, 2006 their balance sheet was as follows:*

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capitals:			Cash	22,500
Rita	80,000		Debtors	52,300
Geeta	50,000		Stock	36,000
Ashish	30,000	1,60,000	Investments	69,000
Creditors		65,000	Plant	91,200
Bills payable		26,000		
General reserve		20,000		
		2,71,000		**2,71,000**

On the date of above mentioned date the firm was dissolved:

1. *Rita was appointed to realise the assets. Rita was to receive 5% commission on the rate of assets (except cash) and was to bear all expenses of realisation,*
2. *Assets were realised as follows:*

	Rs.
Debtors	30,000
Stock	26,000
Plant	42,750

3. *Investments were realised at 85% of the book value,*
4. *Expenses of realisation amounted to Rs. 4,100,*
5. *Firm had to pay Rs. 7,200 for outstanding salary not provided for earlier,*
6. *Contingent liability in respect of bills discounted with the bank was also materialised and paid off Rs. 9,800,*

Prepare Realisation account, Capital Accounts of Partner's and Cash Account.

(**Ans :** *Loss on Realisation Rs. 1,29,455, Total of Cash Account Rs. 1,65,705)*

15. *Anup and Sumit are equal partners in a firm. They decided to dissolve the parntership on December 31, 2006. When the balance sheet is as under :*

Balance Sheet of Anup and Sumit as on December 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Sundry Creditors		27,000	Cash at bank	11,000
Reserve fund		10,000	Sundry Debtors	12,000
Loan		40,000	Plants	47,000
Capital			Stock	42,000
Anup	60,000		Lease hold land	60,000
Sumit	60,000	1,20,000	Furniture	25,000
		1,97,000		**1,97,000**

The Assets were realised as follows :

	Rs.
Lease hold land	72,000
Furniture	22,500
Stock	40,500
Plant	48,000
Sundry Debtors	10,5000

The Creditors were paid Rs. 25,500 in full settlement. Expenses of realisation amount to Rs. 2,500.

Prepare Realisation Account, Bank Account, Partners Capital Accounts to close the books of the firm.

(**Ans :** *Realisation Profit Rs. 46,500)*

16. *Ashu and Harish are partners sharing profit and losses as 3:2. They decided to dissolve the firm on December 31, 2006. Their balance sheet on the above date was:*

Balance Sheet of Ashu and Harish as on December 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capitals:			Building	80,000
Ashu	1,08,000		Machinery	70,000
Harish	54,000	1,62,000	Furniture	14,000
Creditors		88,000	Stock	20,000
Bank overdraft		50,000	Investments	60,000
			Debtors	48,000
			Cash in hand	8,000
		3,00,000		**3,00,000**

Ashu is to take over the building at Rs. 95,000 and Machinery and Furniture is take over by Harish at value of Rs. 80,000. Ashu agreed to pay Creditor and Harish agreed to meet Bank overdraft. Stock and Investments are taken by both partner in profit sharing ratio. Debtors realised for Rs. 46,000, expenses of realisation amounted to Rs. 3,000. Prepare necessary ledger account.

(**Ans** : *Loss on Realisation Rs. 14,000, Cash/Bank Total Rs. 59,600)*

17. *Sanjay, Tarun and Vineet shared profit in the ratio of 3:2:1. On December 31,2006 their balance sheet was as follows :*

Balance Sheet of Sanjay, Tarun and Vineet as on December 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capitals:			Plant	90,000
Sanjay	1,00,000		Debtors	60,000
Tarun	1,00,000		Furniture	32,000
Vineet	70,000	2,70,000	Stock	60,000
Creditors		80,000	Investments	70,000
Bills payable		30,000	Bills receivable	36,000
			Cash in hand	32,000
		3,80,000		**3,80,000**

On this date the firm was dissolved. Sanjay was appointed to realise the assets. Sanjay was to receive 6% commission on the sale of assets (except cash) and was to bear all expenses of realisation.
Sanjay realised the assets as follows : Plant Rs. 72,000, Debtors Rs. 54,000, Furniture Rs. 18,000, Stock 90% of the book value, Investments Rs. 76,000 and Bills receivable Rs.31,000. Expenses of realisation amounted to Rs.4,500. Prepare Realisation Account, Capital Accounts and Cash Account

(**Ans** : *Loss on Realisation Rs.61,300, Total of Cash Account Rs.3,37,000)*

18. *The following is the Balance Sheet of Gupta and Sharma as on December 31,2006:*

Balance Sheet of Gupta and Sharma as on December 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Sundry Creditors		38,000	Cash at bank	12,500
Mrs.Gupta's loan		20,000	Sundry Debtors	55,000
Mrs.Sharma's loan		30,000	Stock	44,000
Reserve fund		6,000	Bills receivable	19,000
Provision of doubtful debts		4,000	Machinery	52,000
Capital			Investment	38,500
Gupta	90,000		Fixtures	27,000
Sharma	60,000	1,50,000		
		2,48,000		**2,48,000**

The firm was dissolved on December 31, 2006 and asset realised and settlements of liabilities as follows:

(a) The realisation of the assets were as follows:

	Rs.
Sundry Debtors	52,000
Stock	42,000
Bills receivable	16,000
Machinery	49,000

(b) Investment was taken over by Gupta at agreed value of Rs.36,000 and agreed to pay of Mrs. Gupta's loan.

(c) The Sundry Creditors were paid off less 3% discount.

(d) The realisation expenses incurred amounted to Rs.1,200.

Journalise the entries to be made on the dissolution and prepare Realisation Account, Bank Account and Partners Capital Accounts.

(**Ans :** *Loss on Realisation Rs.19,660, Total of Cash Account Rs.1,88,500)*

19. *Ashok, Babu and Chetan are in partnership sharing profit in the proportion of 1/2, 1/3, 1/6 respectively. They dissolve the partnership of the December 31, 2006, when the balance sheet of the firm as under:*

Balance Sheet of Ashok, Babu and Chetan as on December 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Sundry Creditors		20,000	Bank	7,500
Bills payable		25,500	Sundry Debtors	58,000
Babu's loan		30,000	Stock	39,500
Capital's :			Machinery	48,000
Ashok	70,000		Investment	42,000
Babu	55,000		Freehold property	50,500
Chetan	27,000	1,52,000		
Current accounts :				
Ashok	10,000			
Babu	5,000			
Chetan	3,000	18,000		
		2,45,500		**2,45,500**

The Machinery was taken over by Babu for Rs.45,000, Ashok took over the Investment for Rs.40,000 and Freehold property took over by Chetan at Rs.55,000. The remaining Assets realised as follows: Sundry Debtors Rs.56,500 and Stock Rs.36,500. Sundry Creditors were settled at discount of 7%. A Office computer, not shown in the books of accounts realised Rs.9,000. Realisation expenses amounted to Rs.3,000.

Prepare Realisation Account, Partners Capital Account, Bank Account.

(**Ans :** *Profit on Realisation Rs.1,200, Total of Cash Account Rs.1,34,100)*

20. *The following is the Balance sheet of Tanu and Manu, who shares profit and losses in the ratio of 5:3, On December 31,2006:*

Balance Sheet of Tanu and Manu as on December 31, 2006

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Sundry Creditors		62,000	Cash at bank	16,000
Bills payable		32,000	Sundry Debtors	55,000
Bank loan		50,000	Stock	75,000
Reserve fund		16,000	Motor car	90,000
Capital			Machinery	45,000
Tanu	1,10,000		Investment	70,000
Manu	90,000	2,00,000	Fixtures	9,000
		3,60,000		**3,60,000**

On the above date the firm is dissolved and the following agreement was made: Tanu agree to pay the bank loan and took away the sundry debtors. Sundry creditors accepts stock and paid Rs.10,000 to the firm. Machinery is taken over by Manu for Rs.40,000 and agreed to pay of bills payable at a discount of 5%.. Motor car was taken over by Tanu for Rs.60,000. Investment realised Rs.76,000 and fixtures Rs.4,000. The expenses of dissolution amounted to Rs.2,200.
Prepare Realisation Account, Bank Account and Partners Capital Accounts.
(**Ans :** *Loss on Ralisation Rs.37,600, Total of Cash Account Rs.1,06,000)*

Check-list to Check your Understanding

Test your Understanding – I
1. True, 2 True, 3. True, 4. False, 5. True, 6. True, 7. True, 8. False.

Test your Understanding – II
1. (c), 2. (d), 3. (b), 4. (d), 5. (c), 6. (a), 7. (b), 8. (c)

Test your Understanding – III
1. Debit, Realisaton, 2. External, Credit, Realisation, 3. Capital Accounts, Profit sharing ratio. 4. Credited, 5. Debited, 6. Creditor, 7. Pay, Realisation, 8. Realisation, Capital, 9. Not recorded, 10. Capital.