St. Lawrence High School

A Jesuit Christian Minority Institution

Study Material 2

Sub: ACCOUNTANCY Class 12

Chapter: Unit 2: Reconstitution of Partnership Date: 10/08/2020

Topic: Change in Profit Sharing Ratio (PSR) -2

As we know change in profit sharing ratio is the part of change in constitution of partnership firm and based on that the following problems and solutions can be highlighted.

Problem 1: X and Y are partners sharing profits and losses in the ratio 2:1. From 1st January ,2020, they agreed to share profits and losses equally. The different assets and liabilities are to be revalued as follows:

1. Land: Balance Sheet value Rs. 1, 00,000, revalued figure Rs.1,50,000.
2. Building: Balance Sheet value Rs. 4, 00,000, revalued figure Rs. 6 ,00,000
3. Plant & Machinery: Balance Sheet value Rs. 2,00,000, revalued figure Rs. 1,30,000

Pass necessary journal entries to give effect of the above.

Solution: In the books of the firm

Journal

Date	Particulars	L.F.	Amt. (Dr.)	Amt. (Cr.)
1st Jan,2020	Land A/C ……………………………… Dr.		50,000	
	Building A/C ……………………….. Dr.		2,00,000	
	To, Revaluation A/C			2,50,000
	(Being land and building increased)			
	Revaluation A/C ………………… Dr.		70,000	
	To, Plant & Machinery A/C			70,000
	(Being plant & machinery decreased)			
	Revaluation A/C …………………… Dr.		1,80,000	
	To, X Capital A/C			1,20,000
	To, Y Capital A/C			60,000
	(Being profit on revaluation is transferred to partners capital account in their old PSR)			

In the above problem it has been observed that profit on revaluation is distributed among the partners in their old profit sharing ratio. Though the mutual ratio of the partners is changed but the effect of that not considered in the solution. If it is stated in the problem that not to alter the book values of assets and liabilities then only we can apply the new profit sharing ratio for restoring the assets in their old values. It can be illustrated in the following problem.

Problem 2: P, Q and R are partners sharing profits and losses in the ratio 5:3:2. The following is their Balance Sheet as at 31st March, 2020.

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
P's Capital	3,00,000	Land & Building	2,00,000
Q's Capital	2,00,000	Plant & Machinery	1,80,000
R's Capital	1,50,000	Furniture	1,20,000
General Reserve	50,000	Debtors	1,00,000
Creditors	1,00,000	Bank Balance	2,00,000
	8,00,000		**8,00,000**

Additional Information:

1. Land & Building increased by Rs. 50,000
2. Plant & Machinery revalued at Rs. 2,00,000
3. Furniture reduced to Rs. 1,00,000
4. Provision for bad debt is required to maintain @ 10% on debtors.
5. Provision for damages is to be made for Rs.5,000
6. Creditors reduced their claim by Rs. 5,000
7. New profit sharing ratio among the partners is P:Q:R is 2:2:1
8. It has been decided that not to alter the book values of assets and liabilities except General Reserve.

Show the accounting treatment of the above by preparing necessary ledger account.

Solution: If the book values of assets and liabilities are unaltered we need to prepare Memorandum Revaluation Account to restore the revalued assets and liabilities at its original figures. Based on this concept Memorandum Revaluation Account is prepared as under.

Memorandum Revaluation Account

Particulars	Amount (Rs)	Particulars	Amount (Rs.)
To, Furniture A/C	20,000	By, Land & Building A/C	50,000
To, Provision for bad debt A/C	10,000	By, Plant & Machinery A/C	20,000
To, Provision for damages A/C	5,000	By, Creditors A/C	5,000
To, Partners Capital A/C -P Rs. 20,000 -Q Rs. 12,000 -R Rs. 8,000	**40,000**		
	75,000		75,000
		By, Partners Capital A/C -P Rs .16,000 -Q Rs. 16,000 -R Rs. 8,000	**40,000**

On the above problem it has been observed that the mutual ratio of the partners is changed. Therefore, profit on revaluation initially distributed among the partners in their old profit sharing ratio is written off in their new profit sharing ratio. So, the application of change in profit sharing ratio is clearly exhibited in the above problem and solution.

Problem 3: A, B and C are partners sharing profits and losses in the ratio 3:2:1. As per their Balance Sheet General Reserve is stood for Rs. 60,000. As per agreement among the partners they will share future profits and losses equally. It has also decided that General Reserve will appear in the new Balance Sheet at its original value. Show necessary journal entries for these accounting treatments.

Solution:
At first we need to distribute the amount of General Reserve among the partners in their old profit sharing ratio and there after it must be written off in their new profit sharing ratio as follows:
(a) Distribution of General Reserve:

General Reserve A/C ……………………… Dr. Rs. 60,000
To, A's Capital A/C Rs.30,000
To, B's Capital A/C Rs.20,000
To, C's Capital A/C Rs.10,000
(Being general reserve is distributed among the partners in their old profit sharing ratio)

(b) Restore the amount of General Reserve at its original value:

A's capital A/C ……………………………… Dr. Rs.20,000
B's Capital A/C …………………………….. Dr. Rs. 20,000
C's capital A/C ……………………………… Dr. Rs. 20,000
To, General Reserve A/C Rs. 60,000
(Being General Reserve restored at its original value in new profit sharing ratio)
