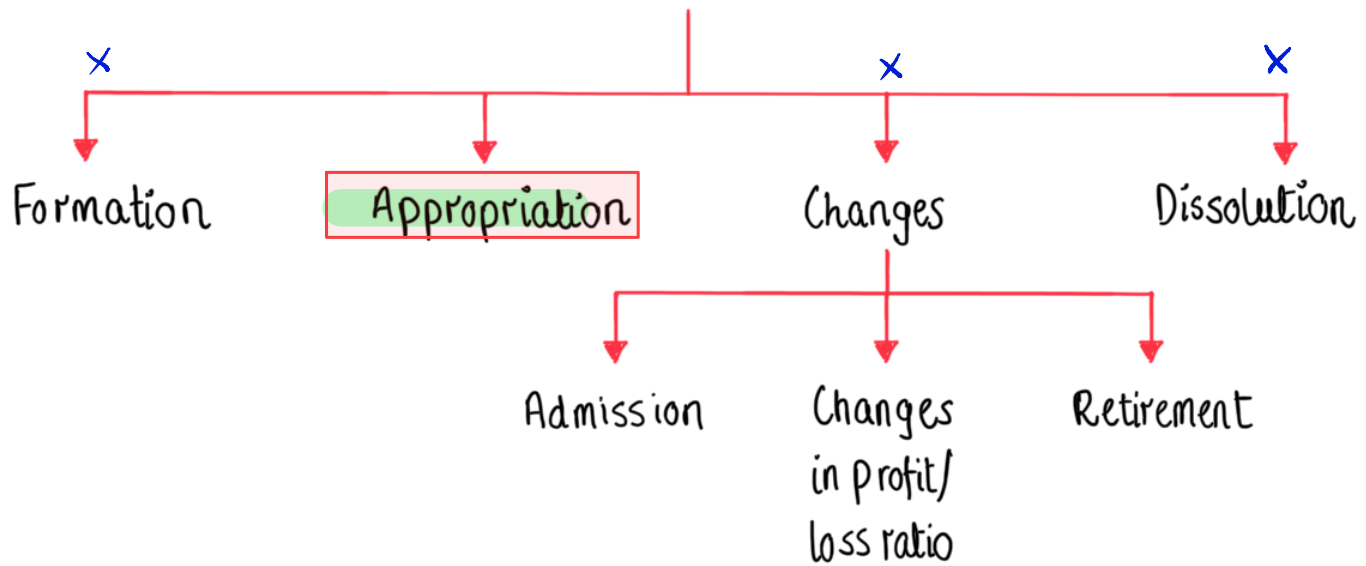


Topic 9



Partnership

PARTNERSHIP



It is a form of a business organisation where 2-20 people merge their financial resources and expertise to perform a business activity with an aim of making and sharing profit.

Characteristics of Partnership:

• Association of Persons (AOP)

→ [2-20] Non Professional firm

→ [more than 20] Professional firms

Lawyers Auditors

• Sharing of Profit and Loss

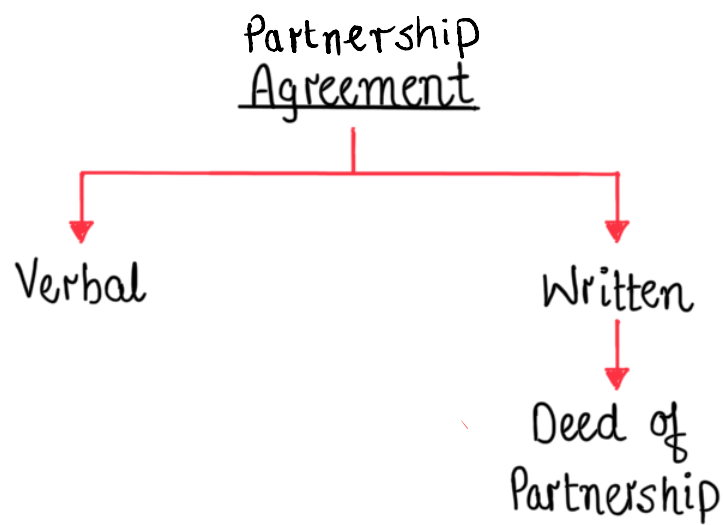
- **Unlimited Liability**: It means that the partners' liability is not restricted or limited to the amount of money invested in the business. If the business goes bankrupt or insolvent, the partners are required to settle the debts from their own personal possessions.

• No separate legal identity.

• No perpetual consistency (upon death of one partner, the partnership is dissolved)

• **Concept of Agency** (consequences of a single partner's decision will have to be borne by the entire firm.)

* **Note**: Both the sole trader and partnership firms have unlimited liability whereas the shareholder of a limited company has limited liability.



Contents of Partnership Agreement:-

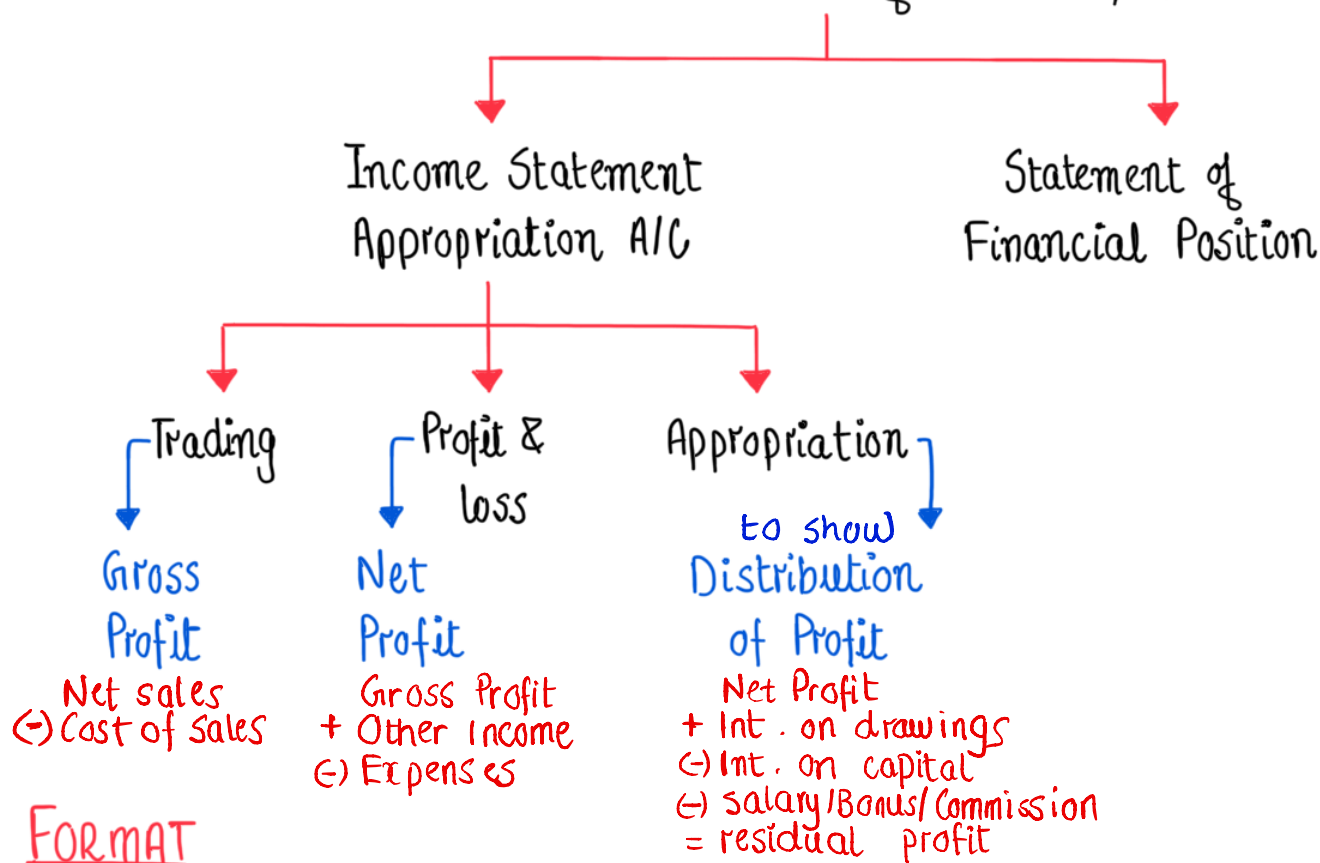
- ✓ 1. Capital contribution [fixed and floating]
- ✓ 2. Duties and rights of partners
- ✓ 3. Rules regarding admission, retirement and death of a partner
- ✓ 4. Interest on drawings → profit ↑ partner current account ↓
- ✓ 5. Interest on capital → profit ↓ partner current account ↑
- ✓ 6. Salary/Bonus/Commission etc → profit ↓ partner current account ↑
- ✓ 7. Profit/loss sharing ratios. E.g:- A : B : C
- ✓ 8. Interest on loan from partner 3 : 2 : 1
expense ↑ current account ↑

In the absence of Partnership Agreement:-

If there is no written partnership agreement, Partnership Act of 1890 is directly enforced which states the application of following provisions:-

1. No interest will be charged on drawings
2. No interest earned on capital contributed
3. No salary, bonus, commission etc.
4. Partners will share profits and losses equally
5. Interest on loan from partners @ 5% per annum.

Financial Statements of Partnership firm



Income Statement Appropriation Account

| | \$ | \$ |
|---|------------|------------|
| Net Profit | | xxx |
| <u>+ Interest on Drawings*</u> | | |
| Adeel | xxx | |
| Ahad | <u>xxx</u> | xxx |
| <u>(-) Interest on Capital</u> | | |
| Adeel | xxx | |
| Ahad | <u>xxx</u> | (xxx) |
| <u>(-) Salary/Bonus/Commission - Ahad</u> | | (xxx) |
| Residual Profit/(loss) | | <u>xxx</u> |
| <u>Share of Profit/(loss)</u> | | |
| Adeel x profit/loss sharing ratio | xxx | |
| Ahad x profit/loss sharing ratio | <u>xxx</u> | <u>xxx</u> |

Note: Fixed Capital A/c → Maintaining separate current a/c
 Floating Capital A/c → Not maintaining separate current a/c

Current Accounts → Credit nature [+ ↑ credit] [- ↓ debit]

They are part of capital accounts and records day to day transactions such as share of profit and drawings.

Note: Current accounts are part of partners' total fund.

• Total Partnership Fund = Capital Accounts + Current Accounts

• Sole Trader → Assets (-) Liabilities = Capital

Partnership → Assets (-) Liabilities = Capital Accounts + Current Accounts

Journal Entries:

1. Interest on drawings

current account ↓

dr
XXX

cr

income statement appropriation a/c (+ to profit)

XXX

2. Interest on capital

income statement appropriation a/c

current account ↑

dr
XXX

cr

→ (-) from profit

XXX

3. Salary / Bonus / Commission

income statement appropriation a/c

current account ↑

dr
XXX

cr

→ (-) from profit

XXX

4. Interest on loan from partner

income statement [Expense]

current account ↑

dr
XXX

cr

XXX

5. Share of residual profit

income statement appropriation a/c

current account ↑

dr
XXX

cr

XXX

6. Share of residual loss

current account ↓

dr
XXX

cr

income statement appropriation a/c

XXX

Changes in Fixed Capital Accounts:

Journal Entries:

1. Introduction of additional capital

cash/bank/non-current asset/inventory
capital account ↑

| | |
|-----|-----|
| dr | cr |
| XXX | |
| | XXX |

2. Withdrawal of capital [repayment from bank]

capital account ↓
bank

| | |
|-----|-----|
| dr | cr |
| XXX | |
| | XXX |

Current Account

| | Dr ↓[-] | Cr + ↑ |
|-----------------------------|------------|-----------|
| Drawings | ✓ | |
| Interest on drawings | ✓ | |
| balance b/d '+' (credit) | | ✓ |
| balance c/d '+' (credit) | ✓ | |
| interest on capital | | ✓ |
| Salary, bonus & commission | | ✓ |
| share of residual profit | | ✓ |
| share of residual loss | ✓ | |
| interest on loan by partner | | ✓ |
| balance b/d '-' (Debit) | ✓ | |
| balance c/d '-' (Debit) | | ✓ |

Dr
↓

Current Account

Cr
↑

| | \$ | | \$ |
|--------------------------|------------|--|------------|
| balance b/d [debit] (-) | xxx | balance b/d [credit] '+' | xxx |
| drawings ↓ | xxx | interest on capital ↑ | xxx |
| interest on drawings ↓ | xxx | salary/bonus/commission ↑ | xxx |
| salary drawings ↓ | xxx | residual share of profit ↑ | xxx |
| residual share of loss ↓ | xxx | interest on loan from partner ² ↑ | xxx |
| balance c/d [credit] '+' | <u>xxx</u> | balance c/d [debit] (-) | <u>xxx</u> |
| | xxx | | xxx |
| balance b/d [debit] (-) | xxx | balance b/d [credit] '+' | xxx |

INTRODUCTION TO COST AND MANAGEMENT ACCOUNTING

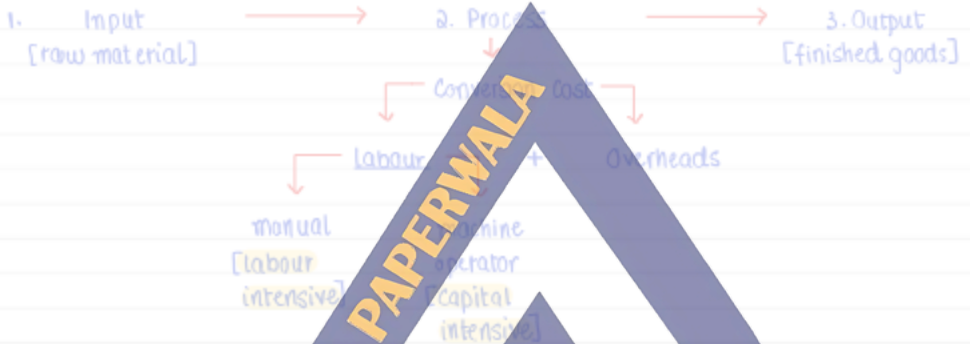
Cost/Expense: Outflow of resources.



For full content

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Stages of Manufacturing



Labour intensive business: Business organisations dependant on manual labour rather than technology or machinery.

Capital intensive business: Business organisations which are more dependant on machines rather than manual labour.

ADEEL PAPERWALA