MEANING OF KEY TERMS USED IN THIS CHAPTER

1. Retirement of a Partner	When a partner does not remain a partner in the firm, it is known as **retirement of a partner**.
2. Gaining Ratio	The ratio in which the remaining/continuing partners take the retiring partner's profit share is called **gaining ratio**.
3. New Profit-sharing Ratio	The ratio in which the remaining/continuing partners (*i.e.*, partners other than retiring partner) decide to share future profits and losses, is known as **new profit-sharing ratio**.

CHAPTER SUMMARY

Retirement of a Partner

- **Meaning of Retirement of a Partner:** When a partner retires from a partnership firm, it is termed as **retirement of a partner**.
- **How can a Partner Retire:** A partner may retire from the firm:
  (i) With the consent of all other partners;
  (ii) In accordance with an express agreement by the partners; or
  (iii) By giving a written notice to the remaining partners of his intention to retire, in case of '*Partnership at will*'.
- **Adjustments at the Time of Retirement of a Partner:** Accounting problems that arise and settled are: calculation of the new profit-sharing ratio and gaining ratio, revaluation of assets and reassessment of liabilities, treatment of goodwill, accumulated profits, reserves and losses, share of the retiring partner in profits or losses up to the date of retirement.
- **New Profit-sharing Ratio:** The ratio in which the continuing partners, *i.e.*, partners other than the retiring partner decide to share future profits and losses, is known as the **new profit-sharing ratio**.

  New Profit Share = Old Profit Share + Acquired Profit Share
- **Gaining Ratio:** The ratio in which the continuing partners acquire the outgoing (retired or deceased) partner's share is known as the **gaining ratio**.

  Gain of a Partner = New Profit Share – Old Profit Share
- **Accounting Treatment of Goodwill:** When a partner retires, his share of profit is taken by the remaining/continuing partners. *The remaining/*continuing *partners compensate the retiring partner in the form of goodwill in their gaining ratio.*

  The following entry is recorded for this purpose:

Remaining Partners' Capital/Current* A/cs	...Dr.	[In gaining ratio]
To Retiring Partner's Capital/Current* A/c		[Retiring Partner's Share of Goodwill]

  If goodwill exists in the Balance Sheet, it is written off by passing the following entry:

All Partners' Capital/Current* A/cs	...Dr.	[In old ratio]
To Goodwill A/c		

  *In case of Fixed Capitals

Note: Write off existing goodwill (if any) appearing in the books of the firm (Balance Sheet) by passing the following entry:

All Partners' Capital/Current A/cs	...Dr.	[In old profit-sharing ratio]
To Goodwill A/c		[With existing book value of goodwill]

When Goodwill exists in the Books

Goodwill existing in the books of account is written off by debiting all the Partners' Capital Accounts including retiring/deceased partner in their old profit-sharing ratio. The Journal entry passed is:

All Partners' Capital (or Current) A/cs	...Dr.	[In Old Profit-sharing Ratio]
To Goodwill A/c		[With Existing Value of Goodwill]
(Existing goodwill written off)		

- **Revaluation of Assets and Reassessment of Liabilities:** At the time of retirement of a partner, assets are revalued and liabilities are reassessed; the difference is recorded in the Revaluation Account. The balance in the Revaluation Account is transferred to the Capital Accounts of all the partners (including the outgoing partner) in their old profit-sharing ratio.
- **Adjustment for Reserves and Accumulated Profits/Losses:** If at the time of retirement or death of a partner, there is balance in "Reserve and Accumulated Profits/Losses", then they are transferred to Capital Accounts of all partners in their old ratio.

  However, if partners decide to record the net effect of reserves, accumulated profits and losses without affecting their old values, then an adjustment entry is passed through Capital Accounts of gaining partners and sacrificing partners.
- **Amount Due to the Retiring Partner:** The total amount due to a retiring partner may include:
  (i) Capital on the date of the last Balance Sheet.
  (ii) Loan by the Partner to the firm.
  (iii) Interest or salary, if any, payable to him.
  (iv) Share of profit or loss till the date of retirement.
  (v) Share in the gain (profit) or loss on revaluation of assets and reassessment of liabilities.
  (vi) Share in the goodwill of the firm.
  (vii) Share in the General Reserve or Profit & Loss Account appearing in the Balance Sheet.

  Out of the total of (i) to (vii), the amount of Loan to the partner, drawings and interest on drawings till the date of retirement are deducted.

  The net amount payable will be settled by paying him through cash/bank or by transferring it to a separate Loan Account.
- **Payment of Dues to the Retiring Partner:** If the question does not specify whether the amount is paid or not, the amount due to the retiring partner is transferred to his Loan Account.

  If the question specifies an amount having been paid, balance amount payable, if any, is transferred to his Loan Account.
- **Interest on Unpaid Amount to Retired Partner:** Retired partner is entitled to take interest @ 6% p.a. or share of profit based on his loan amount, as is agreed by the partners.

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