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शक्तिउत्थानआश्रमलखीसरायबिहार

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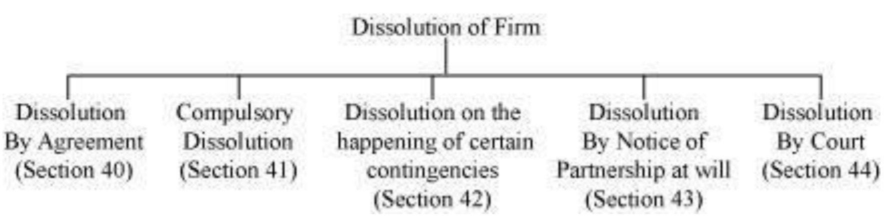
Dissolution of Partnership Firm

Question 1:

Explain the process of dissolution of a partnership firm?
ANSWER:

Dissolution of partnership firm implies discontinuation of the business of the partnership firm. According to the Section 39 of Partnership Act, dissolution of partnership between all the partners of a firm is called dissolution of partnership firm. Dissolution involves winding up of business, disposal of assets and paying off the liabilities and distribution of any surplus or borne of loss by the partners of the firm. As per the Partnership Act 1932, a partnership firm may be dissolved in the following manners:



1) **Dissolution by Agreement**

A firm may be dissolved with:

a) the consent of all the partners, or

b) the contract between the partners

2) **Compulsory Dissolution**

A firm may be dissolved by:

a) the adjudication of all the partners or of all partners but one as insolvent

b) happening of an event or change in government policies that make the business unlawful.

3) **Dissolution on the happening of Certain Contingencies**

Subject to the contract between the partners, a firm is dissolved

a) if formed for a specific period then on the expiry of the period

b) if formed for a specific purpose then on completion of the purpose

c) on the death of partner/partners

d) on insolvency of a partner/partners

4) **Dissolution by Notice**
If partnership is at will then the partnership firm is dissolved if any partner giving notice in writing to all the other partners expressing his/her intention to dissolve the firm.

5) **Dissolution by Court**
The court may order to dissolve a partnership firm when:
a) a partner becomes insane or lunatic.
b) a partner becomes permanently incapable of performing the duties.
c) a partner is guilty of misconduct and affects the business activities.
d) a partner repeatedly breaks the terms of agreement .
e) a partner transfers his interest to a third party without the consent of other partners.
f) a business persistently incurs losses.

Besides these above mentioned circumstances, a partnership firm may be dissolved if the court at any stage finds dissolution of the firm to be justified and inevitable.

The following are the rules of settlement of accounts on dissolution as per the Section 48 of Partnership Act 1932.

1. ***Application of Assets:*** Amount received by the realisation (sale) of the assets shall be used in the following order:
a) First of all the external liabilities and expenses are to be paid.
b) Then, all loans and advances forwarded by the partners should be paid.
c) Then, the capital of each partners should be paid off. If there remains any surplus after the payment of (a), (b) and (c), then it should be distributed among the partners in their profit sharing ratio.

2. ***Treatment of Loss:*** In case of loss and any deficiency of capital, then this should be paid in the following order:
a) First these should be adjusted against firm's profits.
b) Then, against the total capital of the firm.
c) If still there exists any loss and deficiencies, then it should be borne by all the partners individually in their profit sharing ratio.

Question 2:

What is a Realisation Account?

ANSWER:

On dissolution of a firm, all the books of account are closed, all assets are sold and all liabilities are paid off. In order to record the sale of assets and discharge of liabilities, a nominal account is opened named Realisation Account. The main purpose to open Realisation Account is to ascertain the profit or loss due to the realisation of assets and liabilities. Realisation profit (if credit side > debit side) or realisation loss (if debit side > credit side) are transferred to the Partner's Capital Account in their profit sharing ratio.

Concisely, following are the important objectives of preparing Realisation Account.
1) To close all the books of account.
2) To record transactions relating to the sale of assets and discharge of liabilities.
3) To determine profit or loss due to the realisation of assets and liabilities.

Accounting treatment of items related to Realisation Account

1) *For transfer of assets*

Realisation A/c	Dr.
To Sundry Assets A/c (Individually)	
(All Assets transferred to realisation account, except Cash/Bank, P and L debit balance, Loan to a Partner)	

2) *For transfer of liabilities*

Sundry Liabilities A/c (Individually)	Dr.
To Realisation A/c	
(All Liabilities transferred to Realisation account except Partner's Capitals, P and L credit balance, Loan from Partner)	

3) *For sale of assets*

Bank A/c (Amount received)	Dr.
To Realisation A/c	
(Assets sold for cash)	

4) *For payment of liabilities*

Realisation A/c	Dr.
To Bank A/c	
(Liabilities paid in cash)	

5) *For payment of realisation expenses*

Realisation A/c Dr.
To Bank A/c
(Expenses paid)

6) *For transfer of profit on realisation*

Realisation A/c Dr.
To Partner's Capital A/c
(Profit on realisation transferred to partner 's capital account)

7) *For transfer of loss on realisation*

Partner's Capital A/c Dr.
To Realisation A/c
(Loss transferred to partner's capital account)

Question 3:

Reproduce the format of Realisation Account.

ANSWER:

Format of Realisation Account

Dr. **Cr.**

Particulars	**Amount Rs**	**Particulars**	**Amount Rs**
Various Assets (Excluding Cash/Bank, fictitious assets, Debit balance of P and L A/c, partner Capital A/c, Current A/c, Loan to Partner)	–	*Various Liabilities* (Excluding Partner Capital account, reserves, P and L A/c, Current A/c, Loan to Partner)	–
Cash/Bank (Payment for realisation expenses)	–	*Provision on assets* (like, Provision for doubtful debts; Provision for depreciation)	–
Cash/Bank		*Cash/Bank* (Amount received from realisation of assets and unrecorded assets)	

(Payment to outside and unrecorded liabilities)	–	*Partner 's Capital A/c* (If any asset taken over by any partner)	–
Partner's Capital A/c (If any liability taken on expenses paid by him or remuneration payable to him)	–	Partner Capital A/c (Loss on realisation borne by all the partners in their profit sharing ratio)	–
Partner Capital A/c (Profit on realisation distributed in the profit sharing ratio among all the partners)			
	–		–

Question 4:

How deficiency of creditors is paid off?

ANSWER:

At the time of dissolution of a firm, the amount received from the sale of firm's assets are utilised to pay the creditors. If the sale receipts fall short, then partners' private assets are used for settling the dues of the firm's creditors. Even if some portion of the amount due to creditors is left unpaid, then there arises deficiency of creditors. There are generally two procedures to be followed to treat the deficiency of creditors.

1. Transferring deficiency to the Deficiency Account

2. Transferring deficiency to the Partner's Capital Account

In the former procedure, a separate account is prepared for the firm's creditors. Then in order to ascertain the firm's cash balance accruing from the sale of the firm's assets and partners' private assets, Cash Account is prepared. After ascertaining the cash availability with the firm, the creditors and the external liabilities are paid proportionately (partially). The remaining unpaid creditors or the deficiency is transferred to the Deficiency Account.

In the latter procedure, creditors are paid by the cash available with the firm including the partners individual contribution. The deficiency or unpaid creditors amount is transferred to the Partner's Capital Account. Thus the deficiency of the creditors is borne by all the partners in their profit sharing ratio. If any partner becomes insolvent and is unable to bear the deficiency, then this will be regarded as a capital loss to the firm. If the partnership deed is silent about such capital loss in the facet of insolvency of a partner, then according to the ***Garner v/s Murray*** case, such capital loss need to be borne by the solvent partners in their capital ratio.