

PARTNERSHIPS LIQUIDATION

Study unit 4

FAC1601

OVERVIEW

- Key concepts
- Liquidation methods
 - Simultaneous
 - Piecemeal
- Liquidation account
- Accounting procedures
 - Simultaneous liquidation
 - Piecemeal liquidation

KEY CONCEPTS

- Dissolution
- Liquidation
 - Dissolution of solvent partnership
 - Assets converted to cash, liabilities settled & balance transferred to partners' capital accounts
- Liquidation account
- Simultaneous liquidation
- Piecemeal liquidation
- Loss-absorption-capacity method

LIQUIDATION METHODS

◉ Simultaneous

- ◉ Partnership assets are sold simultaneously or over brief period
- ◉ Discontinue operations
- ◉ Single liquidation account → Net profit/loss on liquidation

◉ Piecemeal

- ◉ Partnership continues operations - steadily decrease
- ◉ Liquidate partnership at best possible price
- ◉ More than one liquidation account
 - Net profit/loss on each portion of partnership liquidated
 - Close each liquidation account off to partners' capital account in profit-sharing ratio

LIQUIDATION ACCOUNT SIMULTANEOUS - METHOD 1

- ◉ Date liquidation process commence
 - ◉ Close-off following accounts to liquidation account:
 - All assets (excluding Bank)
 - Contra-assets (e.g. accumulated depreciation & allowance for credit losses)
 - Liability accounts
 - ◉ Record the following in the liquidation account
 - Liquidation of assets (Amounts received for assets)
 - Settlement of debt
 - Further income received/expenses paid
 - ◉ Balancing amount = net profit/loss on liquidation
 - Close off to partners' capital accounts
 - ◉ Profit-sharing ratio

LIQUIDATION ACCOUNT SIMULTANEOUS - METHOD 2

- Similar to method 1 EXCEPT:
 - Only liability accounts where settlement discount is expected are closed off to liquidation account
 - Settlement of other liabilities
 - Cr Bank account, NOT liquidation account
 - Subsequent settlement discount received
 - Dr Liability (full amount)
 - Cr Bank (Amount actually paid)
 - Cr Liquidation account (Settlement discount)

ACCOUNTING PROCEDURES SIMULTANEOUS LIQUIDATION

1. Drawings and current accounts → capital accounts
2. Goodwill & reserves → capital accounts in
 - Profit-sharing ratio
3. Prepare liquidation account
 - Close off assets, contra assets & liabilities
 - Record liquidation of assets (excl Bank)
 - Partner take over asset → Dr Capital, Cr Liquidation
 - Sell for cash → Dr Bank, Cr Liquidation account
 - Record income received → Dr Bank, Cr Liquidation
 - Record liquidation costs paid → Dr Liquidation, Cr Bank
 - Record payments of liabilities → Dr Liquidation, Cr Bank
 - Record payment of further expenses → Dr Liquidation, Cr Bank
 - Close off balance to capital accounts in profit-sharing ratio
 - Profit → Dr Liquidation account, Cr Capital:A, Capital:B
 - Loss → Dr Capital A, Capital:B, Cr Liquidation account
4. Record settlement of capital accounts
 - Dr Capital Account:A, B, Cr Bank
 - Ratio of capital balances NOT profit-share ratio.

SIMULTANEOUS LIQUIDATION: GOLDEN RULES

Step 1

- Close off balances of the drawings & current accounts to capital accounts

Step 2

- Close off balances of goodwill & reserves to capital accounts using profit share ratio

Step 3

- Prepare liquidation account
- Transfer balance to capital accounts using profit share ratio

Step 5

- Record settlement of capital accounts
- Balance in capital accounts = Balance in bank account

ACCOUNTING PROCEDURES PIECEMEAL LIQUIDATION

1. Drawings & current accounts → capital
2. Goodwill & reserves → Capital
 - Profit-sharing ratio
3. Payment of expenses, settlement of debts
 - Dr Liquidation account, Cr Bank
4. Liquidation of assets, receipt of further cash
5. Interim payments made to partners
 - After debt and expenses are paid
 - Partial settlement of capital accounts
 - Calculation
 - Surplus-capital method
 - Loss-absorption-capacity method
6. Settlement to partners - Final repayment
 - Capital account

PIECEMEAL LIQUIDATION: GOLDEN RULES

Step 1

- Close off balances of the drawings & current accounts to capital accounts

Step 2

- Close off balances of goodwill & reserves to capital accounts using profit share ratio

Step 3

- Prepare liquidation account
- Apply loss-absorption-capacity method

Step 5

- Record settlement of capital account


INTERIM PAYMENTS

LOSS-ABSORPTION METHOD


1. Determine actual GL on date cash becomes available for distribution
2. Debit contingent/budgeted expenses to capital accounts - profit share ratio
 - NOT accounting entry - calculation only
3. Close off unsold assets to capital accounts
 - Assume no value
 - NOT accounting entry - calculation only
4. Close off anticipated capital deficit to favourable capital accounts
 - Profit share ratio
 - Assume partners with final anticipated deficits are insolvent
 - NOT accounting entry - calculation only

LOSS-ABSORPTION-CAPACITY METHOD

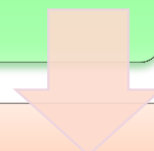
Determine the actual general ledger account balances on the date that cash becomes available for interim repayments.



Debit any budgeted/contingent expenses to the partners' capital accounts - profit-sharing ratio



Close of all unsold assets to the capital accounts - profit-sharing ratio



Close off any anticipated deficit to the capital accounts of the partners who have favourable anticipated capital account balances - profit-sharing ratio