

PARTNERSHIPS ESTABLISHMENT & FINANCIAL STATEMENTS

Study unit 2

FAC1601

OVERVIEW

- ◉ *Reasons for formation*
- ◉ *Legal position of partners*
- ◉ *Establishment of partnership*
- ◉ *Partnership agreement*
- ◉ *Dissolution of partnership*
- ◉ **Accounting procedures**
 - ◉ Follow legal approach
- ◉ **Financial statements of a partnership**

ACCOUNTING PROCEDURES

◎ Equity

- Capital accounts
- Current accounts
- Drawings accounts
- Reserves

◎ Loan accounts

- Interest

◎ Appropriation account

- Share of profit of losses

◎ Salaries and bonuses paid to partners

CAPITAL ACCOUNTS

◎ Initial investment by each partner

- Increase → additional contribution of capital
- Decrease → drawings

Dr Bank (or other asset contributed)

Cr Capital: *Name of partner*

◎ Interest

- Stipulate in partnership agreement
 - Interest rate
 - Basis of calculation

CURRENT ACCOUNTS

- ◎ Transactions affecting partner's interest during the financial period.
 - All transactions between partners & partnership during year.
- ◎ Examples:
 - Partner's share in profits/losses
 - Interest on capital/current accounts
 - Interest on drawings
 - Salaries & bonuses due (but not yet paid) to partners
 - Drawings (if separate account is not used)
- ◎ Can be debit (partner owes partnership) or credit (partnership owes partner)

DRAWINGS ACCOUNT

◎ Partner withdrawals

- Salaries
- Interest earned
- Profit share
- Merchandise taken
- NOT capital withdrawals (directly in capital account)

◎ Record when withdrawal happens

- Dr Drawings: Partner's name
- Cr Bank/inventory/other

◎ End of financial period

- Transfer to current account of each partner

RESERVES & TOTAL INTEREST IN PARTNERSHIP

◉ Asset replacement reserve

- ◉ Profit not available for distribution to partners
- ◉ Finance replacement of PPE

◉ Total interest in partnership:

- ◉ Capital accounts
- ◉ PLUS: Credit balances on current accounts
- ◉ LESS: Debit balances on current accounts
- ◉ PLUS: Reserves

LOAN ACCOUNTS

- ◎ Partner lends money to partnership - Cr
 - Non-current or current liability
 - Interest → finance cost
- ◎ Partnership lends money to partner - Dr
 - Non-current or current asset
 - Interest → 'other income'

SALARIES & BONUSES PAYABLE TO PARTNERS

◎ Year-end (Y/e adjustment)

- Dr annual provision for partner salaries & bonuses (*Salary: Partner A & Salary: Partner B*)
- Cr Current account: Partner A
- Cr Current account: Partner B

◎ Closing journal

- Dr Appropriation account
- Cr Salary: Partner's name

APPROPRIATION ACCOUNT

◎ Final account

- Appropriate profit/loss @ y/e to partners
 - Pre-determined profit-sharing ratio
 - ◎ If not specified in written agreement → assume ratio of capital contributions
 - Capital contributions not specified → share equally

◎ If profit for the year:

- Dr Profit/loss account
- Cr Appropriation account

◎ Close of appropriation account (if profit)

- Dr Appropriation account
- Cr Current account: *Partner 1*
- Cr Current account: *Partner 2*

FINANCIAL STATEMENTS PARTNERSHIP

STATEMENT OF CHANGES IN EQUITY

Name of reporting entity							
Statement of changes in equity for the year ended _____	Capital		Current accounts		Asset replacement reserve	Appropriation	Total
	Partner 1	Partner 2	Partner 1	Partner 2			
	R	R	R	R	R	R	R
Balances as at _____ (first day of reporting period - opening balance)	XX	XX	XX	XX	XX		XX
Total comprehensive income for the year						XX	XX
Transfer to asset replacement reserve					XX	XX	
Salaries to partners			XX	XX		XX	
Interest on capital			XX	XX		XX	
Interest on current accounts			XX			XX	
Interest on drawings				XX		XX	
Partners' share of total comprehensive income			XX	XX		XX	
Drawings			XX	XX			XX
Balances at _____ (last day of reporting period - closing balance)	XX	XX	XX	XX	XX	XX	XX