Class 12 Accountancy – Chapter 1 Notes
Accounting for Partnership Firms: Fundamentals

1. Partnership

Partnership is the relationship between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Features: Two or more persons, agreement between partners, lawful business, profit sharing, and mutual agency.

2. Partnership Deed

A written agreement containing the terms and conditions of the partnership.

Main contents: firm name, partner details, capital contribution, profit sharing ratio, interest on capital, interest on drawings, partner salary/commission, rights and duties.

3. Profit Sharing Ratio (PSR)

The ratio in which partners share profits and losses of the firm.

Example: A and B share profits in the ratio 3:2.

4. Capital Accounts of Partners

Two methods are used: Fixed Capital Method and Fluctuating Capital Method.

Fixed Capital Method

Capital account remains fixed. A separate Current Account is maintained.

Adjustments like interest on capital, drawings, salary, and share of profit are recorded in Current Account.

Fluctuating Capital Method

Only one Capital Account is maintained.

All adjustments such as drawings, interest, salary, and profit share are recorded in the Capital Account.

5. Interest on Capital

Interest allowed on partner’s capital contribution if mentioned in the partnership deed.

Formula: Interest = Capital × Rate × Time / 100

6. Interest on Drawings

Interest charged on drawings made by partners.

Formula: Interest = Drawings × Rate × Time / 100

7. Partner’s Salary / Commission

Partners may receive salary or commission if allowed in the partnership deed.

It is an appropriation of profit, not a business expense.

8. Profit and Loss Appropriation Account

Prepared to show distribution of profit among partners.

Items include interest on capital, partner salary, commission, interest on drawings, and profit transferred to capital accounts.

9. Guarantee of Profit

A partner may be guaranteed a minimum amount of profit.

If their actual share is less than the guaranteed amount, the deficiency is borne by other partners.

10. Past Adjustments

Adjustments made for errors or omissions of previous years such as omitted interest or salary.

These are adjusted through partner’s capital accounts.