9 PARTNERS' CAPITAL ACCOUNT

Objectives
At the end of this chapter, students should be able to:

- Explain partnership capital account;
- Identify different types of capital;
- Identify capital account;
- Prepare capital account.

9.1 Introduction
Partners contribute capital to increase the initial outlay of the business. The basic books and accounts used by a sole trader are kept the same way as is done with a partnership (if there is no nominal partner). The gross and net profits are calculated using the same principles. However, with a sole trader, the net profit is transferred to capital account; in a partnership, the net profit is divided among the partners in the agreed ratio. As the drawings may not be the same for each partner, there would be variation in the accounts kept.

9.2 Partnership Capital Account
The capital of a partnership business forms an important part of the original agreement. It is necessary to preserve original capital in the books. This is an evidence of the capital contributed as directed by individual partners, that is, the original capital contributed shall not be varied as the sole trader capital varies from the addition of profit or deduction of losses from the capital account.

9.3 Types of Capital Account
The partnership capital can be maintained in any of these forms:
1. Capital account without current account is fluctuating capital.
2.. Fixed capital account with current account. These are of two types and they are as enumerated below:
(i) Fluctuating capital without current account: This exterminates the existence of different current account. It is only the agreed capital contribution that will be recorded in the capital account with periodic adjustment being made on the capital account for the partner's entitlement and change against the partners.
(ii) Fixed capital account with current account: This is the initial amount or original capital contributed by individual partners. In this account, the amount put into the business by each partners will not change as the capital will remain fixed but the current account would be prepared to show the changes in the accounts of each partners. For example, profit, losses and drawings. It varies from day to day.

9.4 Terminologies
• **Drawings:** This account records the money taken out by the individual partners. Partners may be allowed to withdraw some certain amount of money at regular intervals or occasionally in accordance with how each partner is entitled to at the end of the year. The total drawings will be credited to cash book and debited to the current account.
• **Interest on Drawings:** This is the interest charged on drawings made by each partner to discourage partners from withdrawing so much in order not to affect the capital. Meanwhile, Interest on drawings will increase the net profit of the business.
• **Share of Profits and Loss:** Whatever is left out of the profit after all other earlier deductions, these will be distributed among the partners based on the agreed profit sharing ratio. If there is no agreement, the profit will be shared equally, according to the provisions of the Partnership Act of 1890.

In this account, the appropriation account will be debited and current account will be credited when sharing profit but if it is sharing of loss the current account will be debited and appropriation account should be credited.

- **Partners Salary:** If any of the partners are authorised by the partnership deed to a salary for his efforts in the day-to-day running activities of the business, he may receive a fixed salary or be compensated in addition to a share in the profits. In this case, a debit to the appropriation account would be made and the same amount should be credited to such partner's current account.

Format:

DR Partnerís Capital Account CR

	X	Y	Z		X	Y	Z
Drawings	x	x	x	Balance b/f	x	x	x
Interest on drawings	x	x	x	Current balance	x	x	x
Balance c/d	x	x	x	Interest on capita	x	x	x
				Salary	x	x	x
				Share of profit	x	x	x
				Balance b/d	x	x	x

9.5 Preparation of Partners Capital Account Example 9.1

Rabiu Bida and Abai Katcha enter into partnership on January 1st, 2009 agreeing to share profit or loss in the ratio of 3:2 respectively. Bida invested N24,000 and Katcha N18,000. It was agreed that because Katcha would be incharge of the partnership business he should be credited with a salary of N1,500. It was as well agreed that interest at 5% per annum on capital should be allowed to each partner before divisions of profits. The net profit for the year 2009 was N11,900. During the year, Bida had withdrawn N3,150 and Katcha N2,880.Show appropriation account and current accounts of Bida and Katcha.

Solution

Profit And Loss Appropriation for
31st December 2009

	₦	₦		₦
Salary – Katcha		1, 500		
Interest on capital			Net profit b/d	11, 900
Bida	1, 200			
Katcha	900.	2,100		
Profit share				
Bida	4, 980			
Katcha	3,320	8,300		
		11,900		11, 900

Capital Accounts

	Bida	Katcha		Bida	Katcha
	N	N		N	N
Drawings	3,150	2, 880	Salary	-	1,500
Balance c/d	3,030	2, 840	Interest on capital	1,200	900
			Share of profit	4,980	3,320
	6,180	5,720		6,180.	5,720

9.6 Summary

In this chapter, students have learnt that:

1. The capital of a partnership business forms an important part of the partner's agreement and it is necessary to preserve the original capital in the books as an evidence of the capital contributed directly by individual partners.
2. The trading, profit and loss account of a partnership business are exactly the same as those of a sole trader's business except that interest is paid on a partner's loan to the business and charged to the profit and loss account.
3. A fixed capital account is shown on the liabilities section of the balance sheet.

9.7 Revision Questions

1. Define the term .partner's capital account..
2. State the difference between a fixed capital account and a current account of a partnership.
3. Explain the following terms in a partnership business:
(a) Interest on drawings
(b) Drawings
(c) Partners salary
(d) Shares of profit
4. Adam and Bida are in partnership sharing profits and losses in the ratio 3:2; their capitals are: Adam N80,000 Bida N50,000. The partnership agreement provides that interest of 5% per annum shall be paid on fixed capital and that Bida is to receive salary of N14,000 per annum and a 2% commission on the balance of trading profit after charging his salary, but before charging interest on capital. The balances on the current accounts as at January 1st, 2009 are:
Adam has a credit of N42,000, Bida has a credit of N35,000 Drawing during the year; Adam N20,000, Bida N18,000. If the trading profit for December 2009 was N54,000, prepare the current account of each partner December 31st, 2009.
5. The partnership agreement between Adara, Chike and Katcha contains the following provisions:
(a) The partner's fixed capital shall be: Adara. N21,000, Chike.N100,000 and Katchan. N180,000.
(b) Chike and Katcha are receiving salaries of N180,000 and N6, 000, respectively
(c) Interest on capital is to be calculated as 6% per annum. (d) Adara, Chike and Katcha are to share profits and losses in the ratio 3:2:1. On January 1, 2008, the balance on current accounts were Adara: Cr N7, 000, Chike: Cr N4,000 and Katcha: Cr N1,000.
During the year, the drawings were: Adara. N2,500, Chike. N1,800 and Katcha. N1,200. If the profit and loss account for the year showed a profit of N89,000 before charging interest on capital or on partner's salaries, prepare the capital and current accounts of Adara, Chike and Katcha as at December 31, 2008 after division of profit.
6. A partner who has some particular or extra task that others have not got is usually compensated in form of ________.
A. Dividend
B. discount
C. commissions
D. salaries
7. A debit balance on a partner's current account means the __________.
A. partner is in debt to the partnership for the amount

B. partnership has no working capital
C. liability of the partner has increased
D. partnership bank account is overdrawn
Use the following information to answer questions 8 -10: Pari and Kay were in partnership sharing profits and losses in the ratio 3:2. Their respective capitals were N4,000 and N2,000 and their drawings N1,800 and N1,200, after charging 5% interest on the capitals the profit was N5,400. Interest on drawings was 5%.
8. What was the partnership profit for the year before appropriation?
A. N5,250
B. N5,850
C. N5,410
D. N5,0009.
9. What was Kay's share of profit?
A. N2,160
B. N2,220
C. N2,340
D. N3,310
10. What was the balance on Pari's current account?
A. N3,130
B. N1,640
C. N3,420
D. N3,530