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Partnerships

DEMONSTRATION PROBLEM

On August 1 of this year, Ryan W. Cloud and Tracy L. Rider form a partnership, Cloud and Rider. Rider agrees to invest \$25,000 in cash and merchandise inventory with an agreed-upon value of \$45,000. Cloud owns an existing business, which he plans to invest in the partnership, including assets agreed upon by the partners. He also plans to transfer the liabilities to the new firm and to contribute cash to bring total capital to \$110,000. Details regarding Cloud's business assets and liabilities, and the agreed valuations, are presented below.

	Cloud's Ledger Balance	Agreed Valuations
Accounts Receivable	\$26,725	\$24,625
Allowance for Doubtful Accounts	925	1,120
Merchandise Inventory	43,554	52,150
Equipment	66,700	35,300
Accumulated Depreciation, Equipment	45,100	—
Notes Payable	8,200	8,200
Accounts Payable	9,800	9,800

The partnership agreement stipulates salary allowances as follows: Cloud, \$24,000; Rider, \$19,000. The agreement also allows interest at 11 percent on the balances on the Capital accounts at the beginning of the year. The remainder (after salary and interest allowances) is divided equally between the two partners.

Instructions

1. In general journal form, give the entries to record the investments of Cloud and Rider.
2. Prepare a balance sheet as of August 1, the date the partnership is formed.
3. At the end of the first full year of operations, after adjustments and the closing of revenue and expense accounts, Income Summary has a credit balance of \$44,000. Prepare the section of the income statement that deals with division of net income.
4. At the end of the first full year of operations, the Drawing accounts have debit balances of \$20,000 for Cloud and \$17,500 for Rider. Give the entries to close Income Summary and the Drawing accounts.

SOLUTION

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	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	
1	20 —					1
2	Aug. 1	Cash		17,045.00		2
3		Accounts Receivable		24,625.00		3
4		Merchandise Inventory		52,150.00		4
5		Equipment		35,300.00		5
6		Allowance for Doubtful Accounts			1,120.00	6
7		Notes Payable			8,200.00	7
8		Accounts Payable			9,800.00	8
9		Ryan W. Cloud, Capital			110,000.00	9
10		Original investment.				10
11						11
12	1	Cash		25,000.00		12
13		Merchandise Inventory		45,000.00		13
14		Tracy L. Rider, Capital			70,000.00	14
15		Original investment.				15
16						16

Cloud and Rider

Balance Sheet

August 1, 20—

<i>Assets</i>			
<i>Current Assets:</i>			
Cash		\$ 42,045.00	
Accounts Receivable	\$24,625.00		
Less Allowance for Doubtful Accounts			
Accounts	1,120.00	23,505.00	
Merchandise Inventory		97,150.00	
Total Current Assets			\$162,700.00
<i>Plant and Equipment:</i>			
Equipment			35,300.00
Total Assets			\$198,000.00
<i>Liabilities</i>			
<i>Current Liabilities:</i>			
Notes Payable		\$ 8,200.00	
Accounts Payable		9,800.00	\$ 18,000.00
Total Liabilities			
<i>Partners' Equity</i>			
Ryan W. Cloud, Capital		\$110,000.00	
Tracy L. Rider, Capital		70,000.00	180,000.00
Total Liabilities and Partners' Equity			\$198,000.00

SOLUTION (concluded)

	<i>Net Income</i>			\$ 44,000.00
	<i>Division of Net Income:</i>	<i>R. W. Cloud</i>	<i>T. L. Rider</i>	<i>Total</i>
	<i>Salary Allowances</i>	\$24,000.00	\$19,000.00	\$43,000.00
	<i>Interest Allowances</i>	12,100.00	7,700.00	19,800.00
	<i>Excess of Allowances over Income</i>			
	<i>Allocated Equally</i>	(9,400.00)	(9,400.00)	(18,800.00)
	<i>Net Income</i>	\$26,700.00	\$17,300.00	\$ 44,000.00

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	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	
1	20 —	<i>Closing Entries</i>				1
2	July 31	<i>Income Summary</i>		44,000.00		2
3		<i>R. W. Cloud, Capital</i>			26,700.00	3
4		<i>T. L. Rider, Capital</i>			17,300.00	4
5						5
6		<i>R. W. Cloud, Capital</i>		20,000.00		6
7		<i>R. W. Cloud, Drawing</i>			20,000.00	7
8						8
9		<i>T. L. Rider, Capital</i>		17,500.00		9
10		<i>T. L. Rider, Drawing</i>			17,500.00	10
11						11