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Accounting for Partnership Firm- FUNDAMENTALS



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Accounting for Partnership Firm- FUNDAMENTALS- Part- 4

Interest on Partners' Drawings



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Interest on Partners' Drawings



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Drawings



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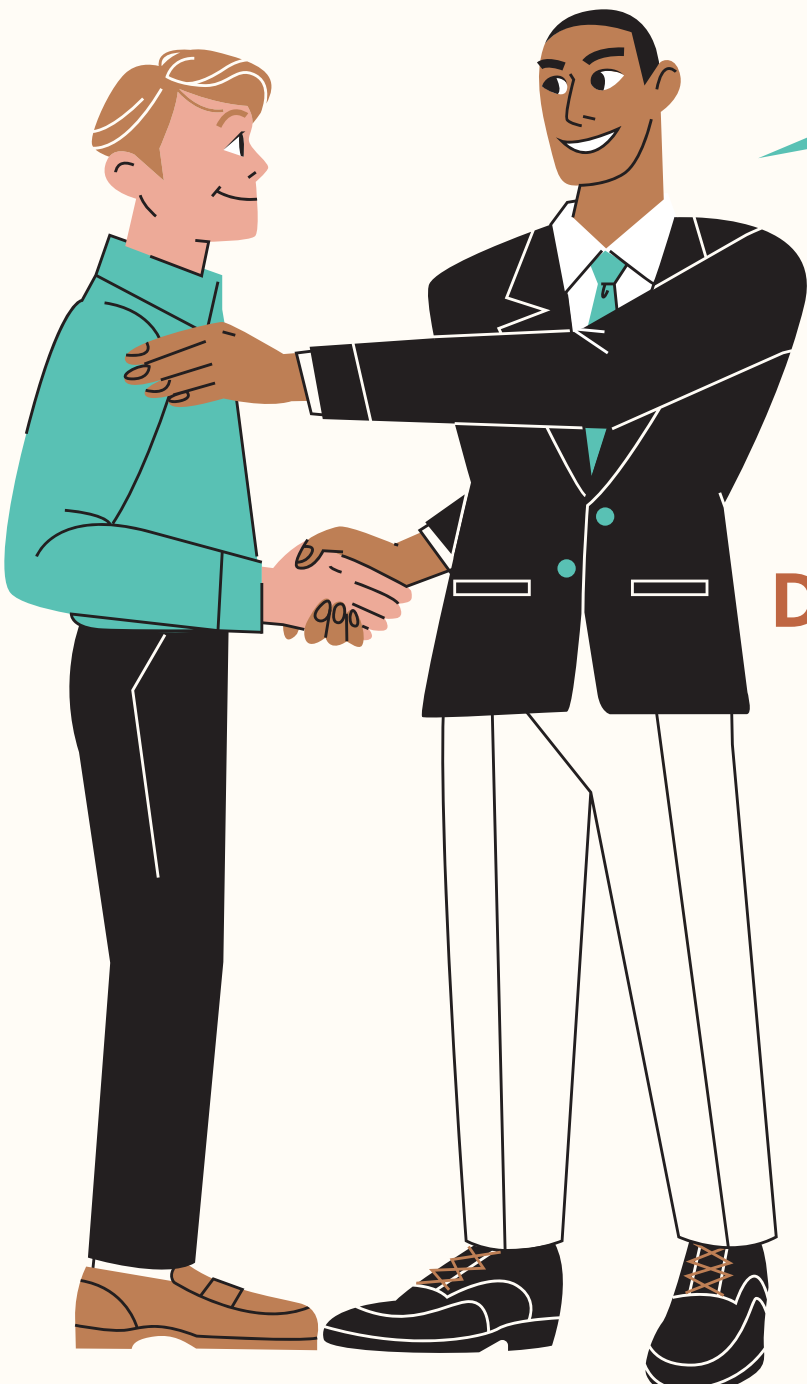
Drawings

The amount withdrawn by partners in cash or in kind from the firm out of their capital or against profit to meet their personal expenses is called drawing.

1. Drawing may be made by partners either in cash or in the form of goods.
2. Drawings may be out of capital or against profit.



01



Drawings

1. Drawings against Capital- withdrawal of capital-

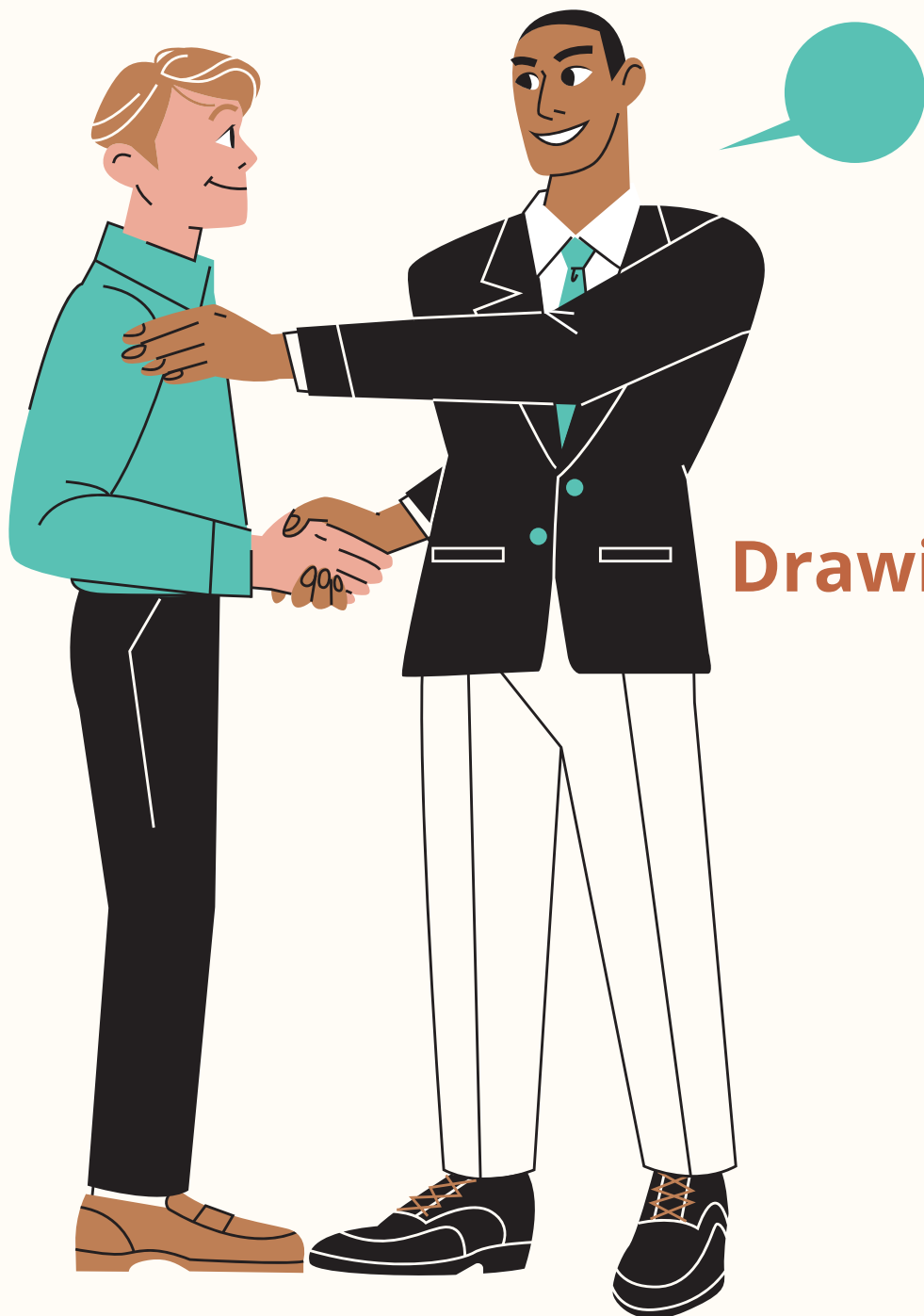
- a. Drawings against capital is the withdrawal of the amount out of his or her capital in the firm.
- b. Drawings against capital is debited to his or her Capital Account. It means that the capital is reduced by the amount withdrawn.
- c. Interest on capital is allowed on capital for the period it is used in business. As a result of drawings against capital, interest on capital is not allowed to a partner on the withdrawn amount.





Interest on Partners' Drawings

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Drawings



01

Anmol (partner) has capital of ₹5,00,000 on 1st April, 2019. He withdraws ₹1,00,000 on 1st October, 2019 out of his capital. If the Partnership Deed allows interest on capital @ 10% p.a., Anmol will get interest of ₹45,000 on capital for the year ended 31st M 2020, calculated as follows:

On 5,00,000 @ 10 p.a. for 6 months (1st April, 2019 to 30th September, 2019) = ₹25,000

On 4,00,000 (i.e., 5,00,000 — 1,00,000) @ 10% p.a. for 6 months (1st October, 2019 to 31st March, 2020) = ₹20,000

Total Interest = ₹45,000

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02

2. Drawings against Profit- Withdrawal in anticipation of profit

a. The amount withdrawn by partners from the firm in anticipation of their profit share to meet their personal expenses is called drawing.

b. Drawings against profit is debited to Drawings Account and not to the Capital account of the partner.

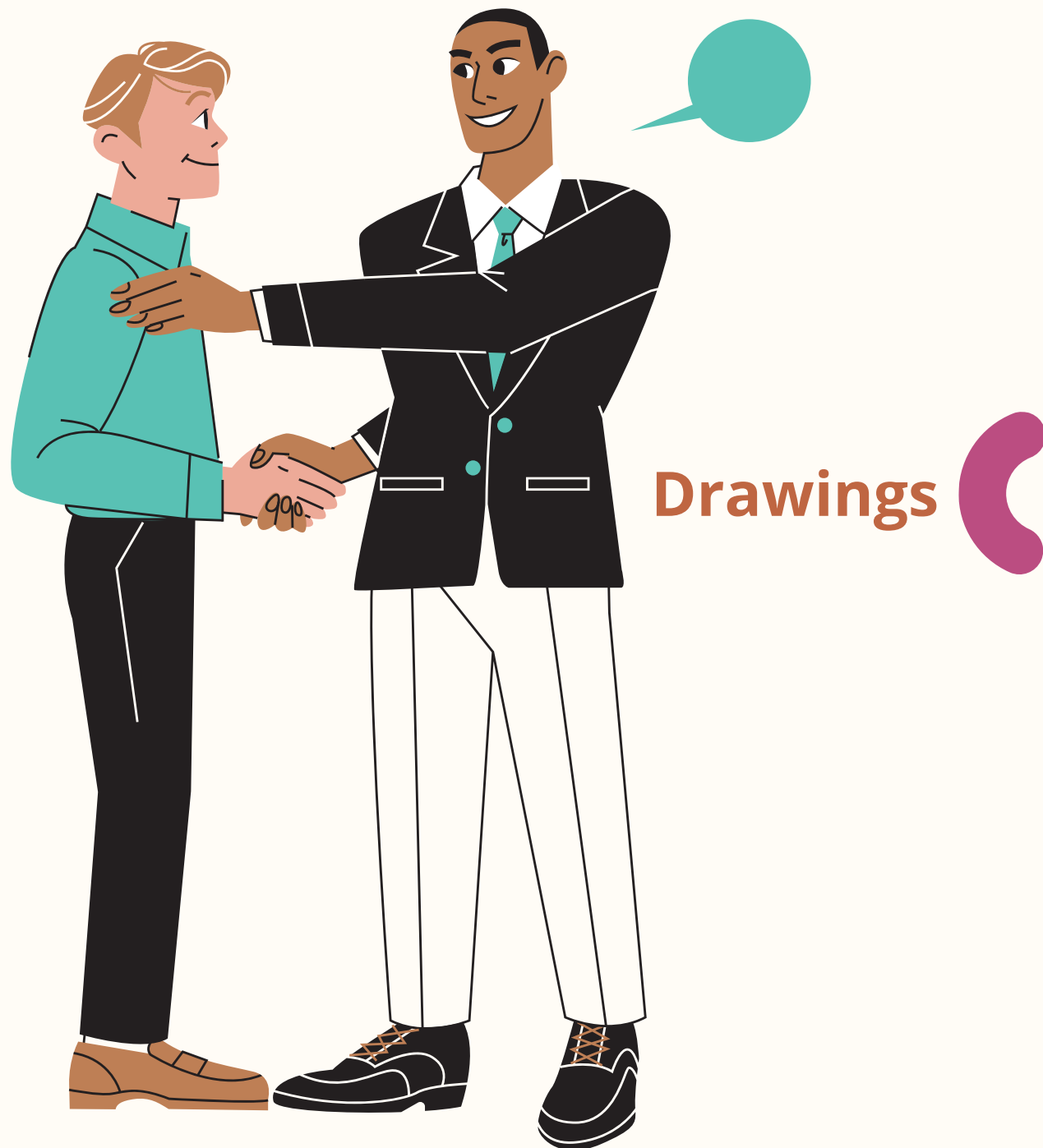
c. Actual share of profit of a partner is known at the end of the year and the date when it becomes due to the partner. Since withdrawal is earlier than it is due, the firm charges interest for the period amount is withdrawn by the partner

Drawings





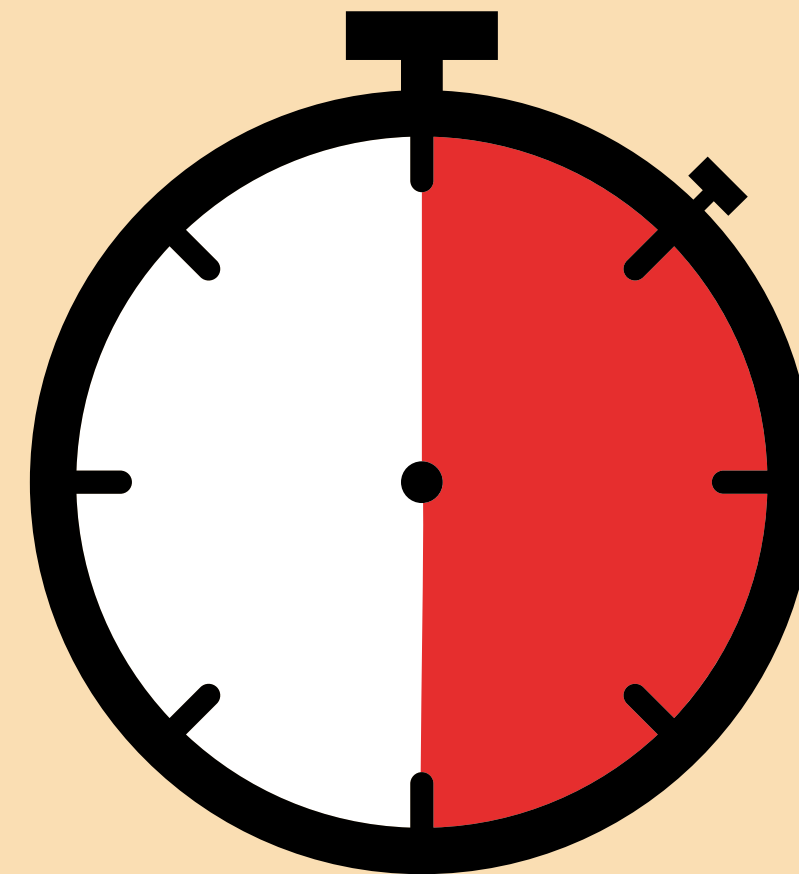
Interest on Partners' Drawings



Drawings

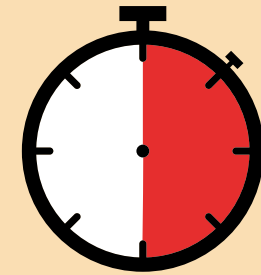
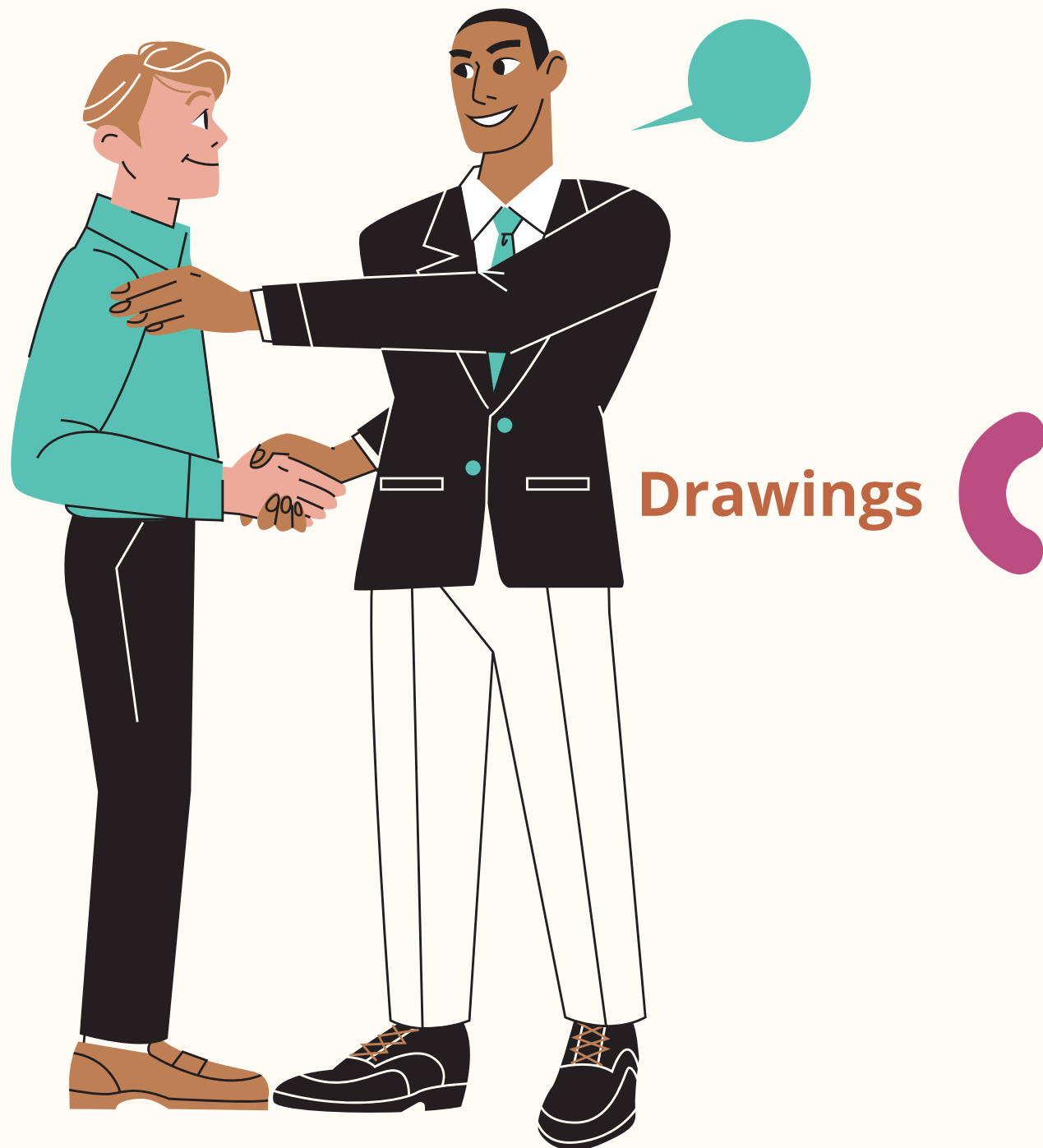
1. Drawings against Capital- withdrawal of capital-

Quick Revision



2. Drawings against Profit- Withdrawal in anticipation of profit





Quick Revision

Distinction between Drawing against Capital and Drawing against Profit

Basis	Drawing against Capital	Drawing against Profit
Where debited	Partners' Capital Account is debited.	Drawing of Partners' account is debited.
Part	It constitutes part of partners' capital.	It is part of expected profit of the firm.
Effect on Capital	Partners' capital is reduced.	It is recorded in partners' current account so capital of partners is not reduced.
Interest on Capital	Interest on capital is affected.	Interest on drawing is affected but there is no effect on interest on capital.
Interest on drawings	It is not considered for calculating Interest on drawings	It is considered for calculating Interest on drawings



Interest on partners' Drawings





Interest on Partners' Drawings

It is charged on drawings against expected profit by the firm, if the Partnership Deed provides for charging interest on drawings.

Interest charged on drawings is transferred to Profit and Loss Appropriation Account and debited to Partners' Capital Accounts (in case of Fluctuating Capital is Method) or Partners' Current Accounts (in case of Fixed Capital Accounts Method).



Journal entries passed for interest on drawings are:





Interest on Partners' Drawings

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Journal entries passed for interest on drawings are:

Partner's Capital/Current A/c ...Dr.
To Interest on Drawings A/c
(Interest charged on drawings)

Interest on Drawings A/c ...Dr.
To Profit and Loss Appropriation A/c
(Interest on Drawings transferred)



Calculation of Interest on Drawings





Calculation of Interest on Drawings

Interest on drawings is always calculated with reference to the time period for which money is withdrawn.

Interest on the drawing is calculated depending upon the availability of information




Interest on Partners' Drawings



Drawings by a partner may be broadly divided into:

(i) Irregular Drawings



(ii) Regular Drawings



Calculation of Interest on Drawings

(i) Irregular Drawings





Interest on Partners' Drawings

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Drawings by a partner may be broadly divided into:



(i) Irregular Drawings

It means drawings of same amount or different amounts at irregular intervals;

Simple and Product Method of calculating interest is followed.



Calculation of Interest on Drawings

(i) Irregular Drawings

Simple Method





Interest on Partners' Drawings

01

Simple Method

(i) Irregular Drawings

In a partnership, partners are charged interest on drawings @ 15% p.a. During the year ended 31st March, 2020, a partner withdrew as follows:

Date	Amount (₹)
1st May, 2019	2,000
1st August, 2019	5,000
30th September, 2019	2,000
31st January, 2020	6,000
31st March, 2020	2,000

What is the interest chargeable from the partner?

Sol 1

(i) Simple Method

Date	Amount (₹)	No. of Months up to 31st March, 2020	Interest @ 15%
1st May, 2019	2,000	11	275
1st August, 2019	5,000	8	500
30th September, 2019	2,000	6	150
31st January, 2020	6,000	2	150
31st March, 2020	2,000	0	0
	17,000		1,075

*Interest = ₹2,000 x 15/100 x 11/12 = ₹ 275.





Calculation of Interest on Drawings

(i) Irregular Drawings

Product Method





Interest on Partners' Drawings

01

Product Method

(iii) Irregular Drawings

In a partnership, partners are charged interest on drawings @ 15% p.a. During the year ended 31st March, 2020, a partner withdrew as follows:

Date	Amount (₹)
1st May, 2019	2,000
1st August, 2019	5,000
30th September, 2019	2,000
31st January, 2020	6,000
31st March, 2020	2,000

What is the interest chargeable from the partner?

Sol 2

(ii) Product Method

A Date	B Amount (₹)	C No. of Months up to 31st March, 2020	D= B X C Product (₹)
1st May, 2019	2,000	11	22,000
1st August, 2019	5,000	8	40,000
30th September, 2019	2,000	6	12,000
31st January, 2020	6,000	2	12,000
31st March, 2020	2,000	0	0
	17,000		86,000

Interest on ₹ 86,000 @ 15% p.a. for one month is $86,000 \times 15/100/1/12 = ₹ 1,075.$





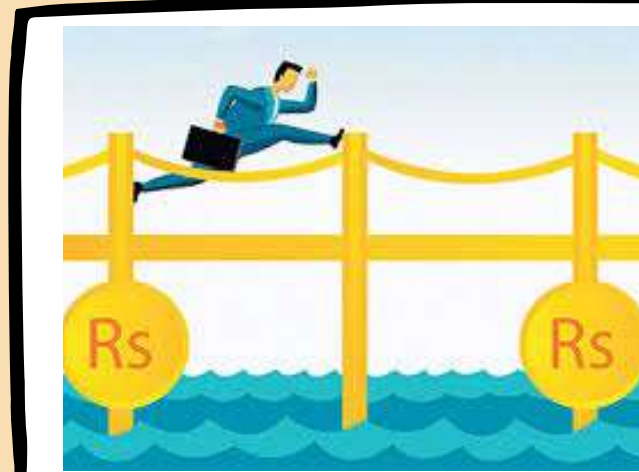
Calculation of Interest on Drawings

(ii) Regular Drawings





Drawings by a partner may be broadly divided into:



(ii) Regular Drawings

It means drawings of the same amount at regular intervals.

Interest on drawings is calculated using the Average Period Method.



Calculation of Interest on Drawings

(ii) Regular Drawings

Formula





Interest on Partners' Drawings

Formula

(ii) Regular Drawings



$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$

Average Period Method: The formula for calculating interest on drawings under this method is:
$$\text{Average Period} = \frac{\text{Months Left after First Drawing} + \text{Months Left after Last Drawing}}{2}$$

Let us take Different situations for calculating interest on drawings under this method.





Calculation of Interest on Drawings

(ii) Regular Drawings

✦ Situation 1. Every Month

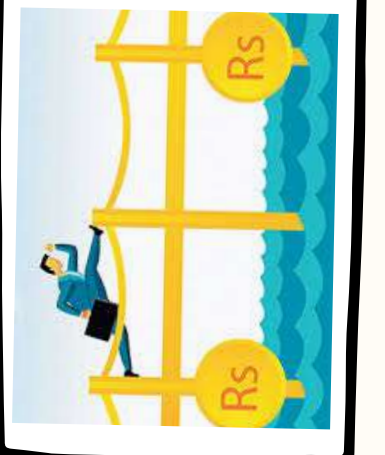




Interest on Partners' Drawings

Case 1a

(ii) Regular Drawings



✦ Situation 1. Every Month

Nikunj a partner draws ₹ 1,600 per month. According to the partnership deed interest will be charged at 15% per annum.

Case 1a.

If a partner withdraws fixed amount in the beginning of every month,

$$\text{Average Period} = \frac{12\text{Months} + 1\text{ Months}}{2}$$

$$= 6\frac{1}{2}\text{ months}$$

$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$

$$\text{Interest on Drawings} = 1600 \times 12 \times \frac{15}{100} \times \frac{13}{2 \times 12}$$

$$= ₹1,560$$

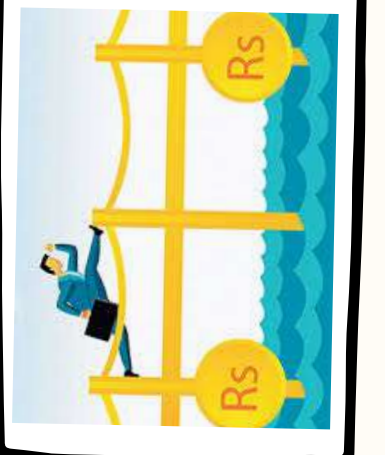




Interest on Partners' Drawings

Case 1b

(iii) Regular Drawings



✦ Situation 1. Every Month

Nikunj a partner draws ₹ 1,600 per month. According to the partnership deed interest will be charged at 15% per annum.

Case 1b.
 If a partner withdraws **fixed amount** at the **end of every month**,

$$\text{Average Period} = \frac{11 \text{ Months} + 0 \text{ Month}}{2}$$

$$= 5\frac{1}{2} \text{ months}$$

$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$

$$\text{Interest on Drawings} = 1600 \times 12 \times \frac{15}{100} \times \frac{11}{2 \times 12}$$

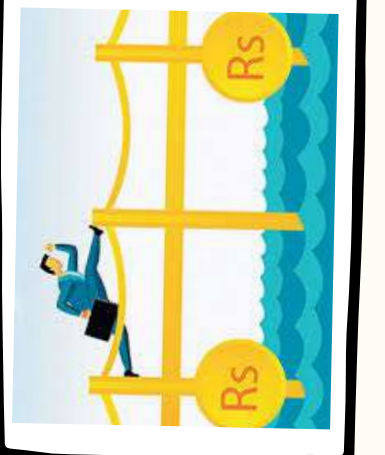
$$= ₹ 1,320$$




Interest on Partners' Drawings

Case 1c

(iii) Regular Drawings



Situation 1. Every Month

Nikunj a partner draws ₹ 1,600 per month. According to the partnership deed interest will be charged at 15% per annum.

Case 1c.
 If a partner withdraws **fixed amount** in the middle of every month,
Average Period = $\frac{11\frac{1}{2} \text{ Months} + \frac{1}{2} \text{ Month}}{2}$
 = 6 months
Interest on Drawings = Total Drawings x $\frac{\text{Rate of Interest}}{100}$ x $\frac{\text{Average Period}}{12}$
Interest on Drawings = $1600 \times 12 \times \frac{15}{100} \times \frac{6}{12}$
 = ₹ 1,440





Calculation of Interest on Drawings

(ii) Regular Drawings

✦ Situation 2. Every Quarter

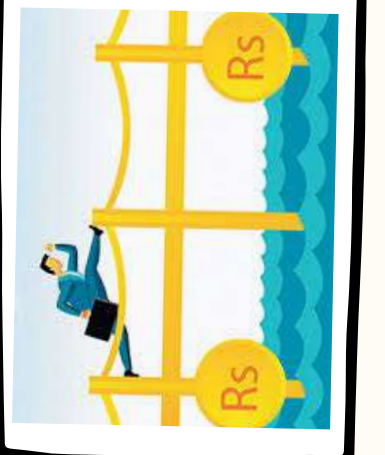




Interest on Partners' Drawings

Case 2a

(ii) Regular Drawings



Situation 2. Every Quarter

Nitin a partner draws ₹ 3,750 quarterly. According to partnership deed interest will be charged at 10% per annum.

Case 2a.
 If a partner withdraws **fixed amount** in the **beginning** of each quarter,
Average Period = $\frac{12\text{Months} + 3\text{ Months}}{2}$
 = $7\frac{1}{2}$ months
Interest on Drawings = $\text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$
Interest on Drawings = $3,750 \times 4 \times \frac{10}{100} \times \frac{15}{2 \times 12}$
 = ₹937.50

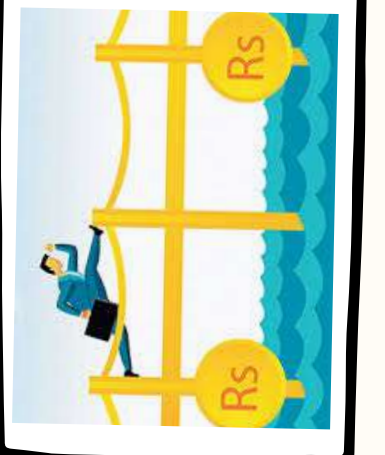




Interest on Partners' Drawings

Case 2 b

(ii) Regular Drawings



Situation 2. Every Quarter

Nitin a partner draws ₹ 3,750 quarterly. According to partnership deed interest will be charged at 10% per annum.

Case 2b.
If a partner withdraws **fixed amount** at the **end of each quarter**,

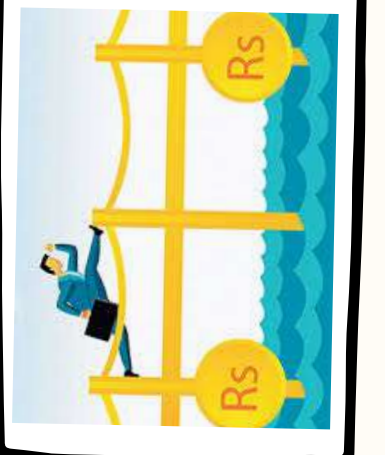
$$\text{Average Period} = \frac{9 \text{ Months} + 0 \text{ Month}}{2}$$
$$= 4\frac{1}{2} \text{ months}$$
$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$
$$\text{Interest on Drawings} = 3,750 \times 4 \times \frac{10}{100} \times \frac{9}{2 \times 12}$$
$$= ₹562.50$$




Interest on Partners' Drawings

Case 2 c

(ii) Regular Drawings



Situation 2. Every Quarter

Nitin a partner draws ₹ 3,750 quarterly. According to partnership deed interest will be charged at 10% per annum.

Case 2c.
If a partner withdraws **fixed amount** in the middle of **each quarter**

$$\text{Average Period} = \frac{10.5 \text{ Months} + 1.5 \text{ Month}}{2}$$
$$= 6 \text{ months}$$
$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}}{12}$$
$$\text{Interest on Drawings} = 3,750 \times 4 \times \frac{10}{100} \times \frac{6}{12}$$
$$= ₹ 750$$




Calculation of Interest on Drawings

(ii) Regular Drawings

✦ Situation 3. during 6 months

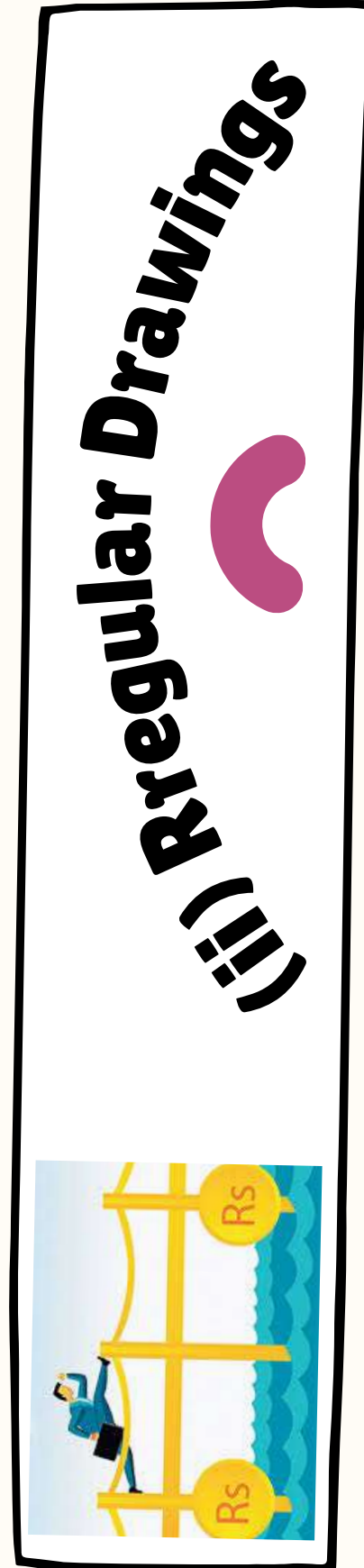




Interest on Partners' Drawings

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Case 3 a



✦ Situation 3. during 6 months

P, Q and R are partner in a firm. They draw ₹ 6,000 during 6 months. According to partnership deed interest will be charged at 8% p.a. Calculate interest on drawings

Case 3a.

P drew ₹6,000 in the beginning of every month for 6 months ending 31st March, 2018.

$$\text{Average Period} = \frac{6 \text{ Months} + 1 \text{ Month}}{2}$$
$$= 3.5 \text{ months}$$

$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$

$$\text{Interest on Drawings} = 6,000 \times 6 \times \frac{8}{100} \times \frac{3.5}{12}$$
$$= ₹840$$

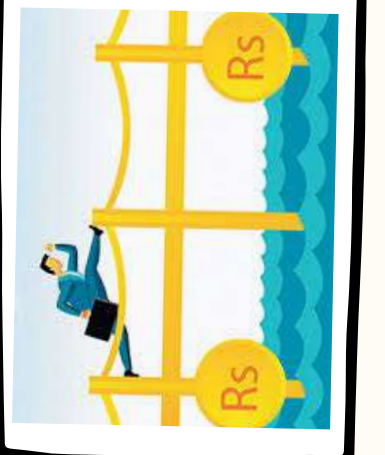




Interest on Partners' Drawings

Case 3 b

(ii) Regular Drawings



✦ Situation 3. during 6 months

P, Q and R are partner in a firm. They draw ₹ 6,000 during 6 months. According to partnership deed interest will be charged at 8% p.a. Calculate interest on drawings

Case 3b.
Q drew ₹6,000 at the end of every month for 6 months ending 31st March, 2018.

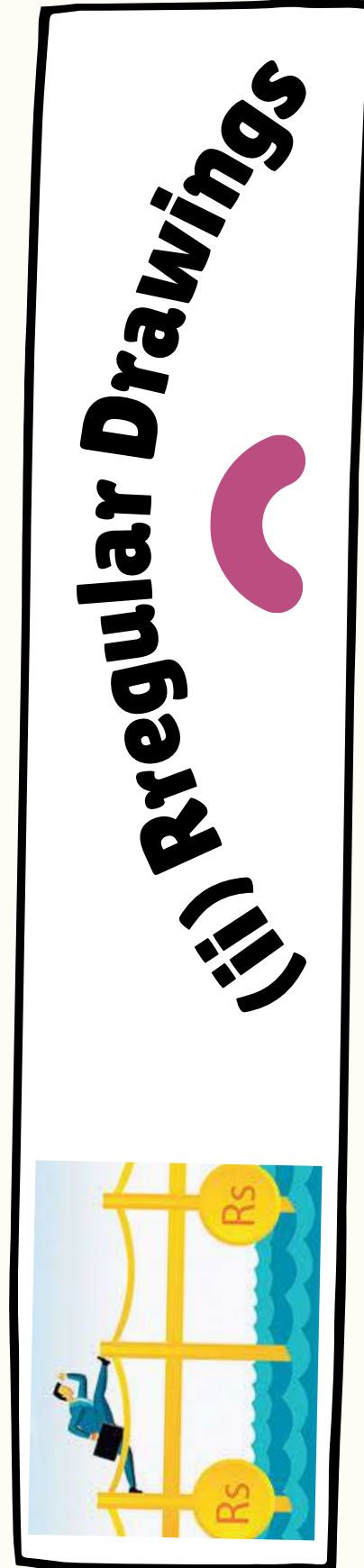
$$\text{Average Period} = \frac{5 \text{ Months} + 0 \text{ Month}}{2}$$
$$= 2.5 \text{ months}$$
$$\text{Interest on Drawings} = \frac{\text{Total Drawings} \times \text{Rate of Interest} \times \text{Average Period}^*}{100 \times 12}$$
$$\text{Interest on Drawings} = 6,000 \times 6 \times \frac{8}{100} \times \frac{2.5}{12}$$
$$= ₹600$$




Interest on Partners' Drawings

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Case 3 c



✦ Situation 3. during 6 months

P, Q and R are partner in a firm. They draw ₹ 6,000 during 6 months. According to partnership deed interest will be charged at 8% p.a. Calculate interest on drawings

Case 3c.

R drew ₹6,000 in the middle of every month for 6 months ending 31st March, 2018.

$$\text{Average Period} = \frac{5.5 \text{ Months} + 0.5 \text{ Month}}{2}$$

$$= 3 \text{ months}$$

$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$

$$\text{Interest on Drawings} = 6,000 \times 6 \times \frac{8}{100} \times \frac{3}{12}$$
$$= ₹720$$





Calculation of Interest on Drawings

(ii) Regular Drawings

✦ Situation 4. during 9 months



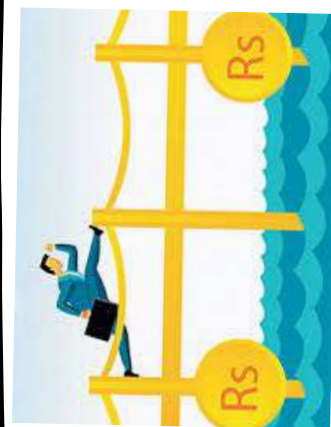


Interest on Partners' Drawings

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Case 4 a

(ii) Regular Drawings



✦ Situation 4. during 9 months

A, B and C started business on 1st July, 2015. When drawings of ₹8,000 are made during 9 months. Calculate interest on drawings @ 10% p.a.

Case 4a

A drew ₹ 8,000 in the beginning of every month for 9 months ending 31st March, 2016.

$$\text{Average Period} = \frac{9 \text{ Months} + 1 \text{ Month}}{2}$$

$$= 5 \text{ months}$$

$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}^*}{12}$$

$$\text{Interest on Drawings} = 8,000 \times 9 \times \frac{10}{100} \times \frac{5}{12}$$
$$= ₹3,000$$

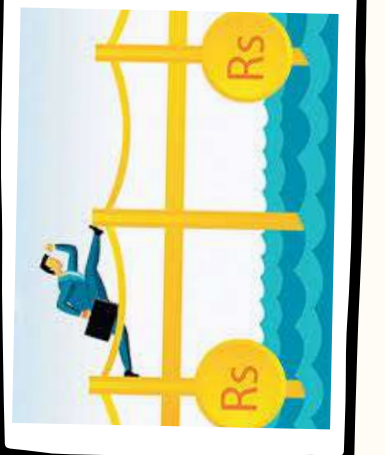




Interest on Partners' Drawings

Case 4 b

(ii) Regular Drawings



✦ Situation 4. during 9 months

A, B and C started business on 1st July, 2015. When drawings of ₹8,000 are made during 9 months. Calculate interest on drawings @ 10% p.a.

Case 4b
B drew ₹ 8,000 at the end of every month for 9 months ending 31st March, 2016.

Average Period = $\frac{8 \text{ Months} + 0 \text{ Month}}{2}$
= 4 months

Interest on Drawings = Total Drawings x $\frac{\text{Rate of Interest}}{100}$ x $\frac{\text{Average Period}}{12}$ *

Interest on Drawings = $8,000 \times 9 \times \frac{10}{100} \times \frac{4}{12}$
= ₹2,400

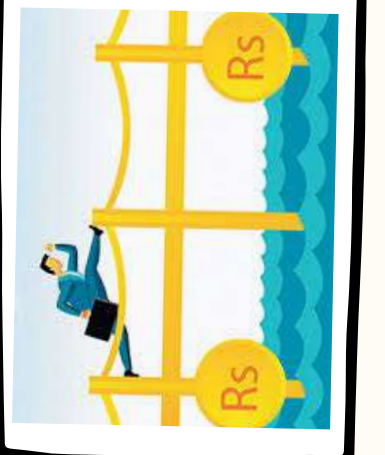




Interest on Partners' Drawings

Case 4 c

(ii) Regular Drawings



✦ Situation 4. during 9 months

A, B and C started business on 1st July, 2015. When drawings of ₹8,000 are made during 9 months. Calculate interest on drawings @ 10% p.a.

Case 4c
 C drew ₹8,000 middle of every month for 9 months ending 31st March, 2016.

$$\text{Average Period} = \frac{8.5 \text{ Months} + 0.5 \text{ Month}}{2}$$

$$= 4.5 \text{ months}$$

$$\text{Interest on Drawings} = \text{Total Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Average Period}}{12}$$

$$\text{Interest on Drawings} = 8,000 \times 9 \times \frac{10}{100} \times \frac{4.5}{12}$$

$$= ₹2,700$$




Calculation of Interest on Drawings

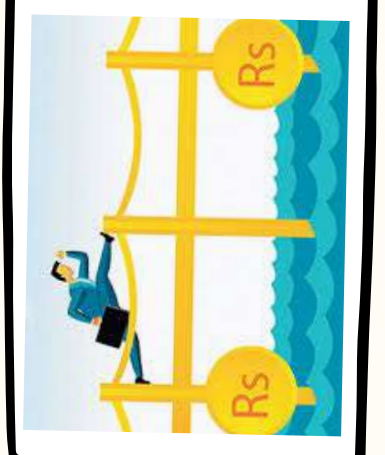
(ii) Regular Drawings

Situation 5. When date of withdrawal is not given





(ii) Regular Drawings



✦ Situation 5. When date of withdrawal is not given

Notes

- ✦ When date of withdrawal is not given, the interest will be calculated on total drawings for the year for six months on average basis.

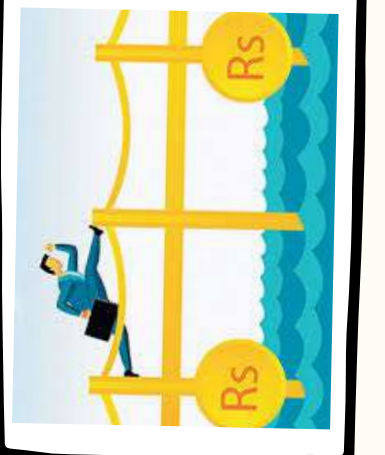




Interest on Partners' Drawings

Case 5 a

(ii) Regular Drawings



✦ Situation 5. When date of withdrawal is not given

Compute the interest on drawings at the rate of 5% per annum for the year ended 31st December 2007 in each of the following case:

Case 5a.

if partner's drawings during the year was ₹50,000.

Interest on Drawings = Total Drawings x $\frac{\text{Rate of Interest}}{100}$ x $\frac{\text{Average Period}}{12}$ *

$$\text{Interest on Drawings} = 50,000 \times \frac{5}{100} \times \frac{6}{12}$$

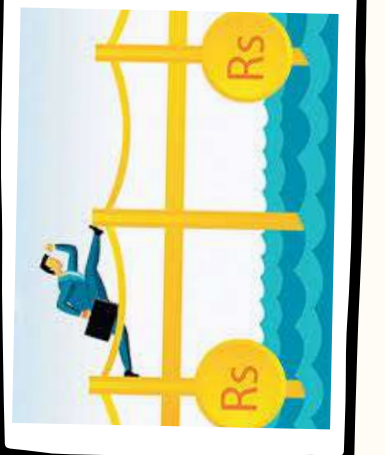
$$= ₹1,250$$





Case 5 b

(ii) Regular Drawings



✦ Situation 5. When date of withdrawal is not given

Compute the interest on drawings at the rate of 5% per annum for the year ended 31st December 2007 in each of the following case:

Case 5b

if partner withdraws ₹ 3,000 per month during the year

Interest on Drawings = Total Drawings x Rate of Interest x Average Period*

$$\text{Interest on Drawings} = 3,000 \times 12 \times \frac{5}{100} \times \frac{6}{12} = ₹900$$





Calculation of Interest on Drawings

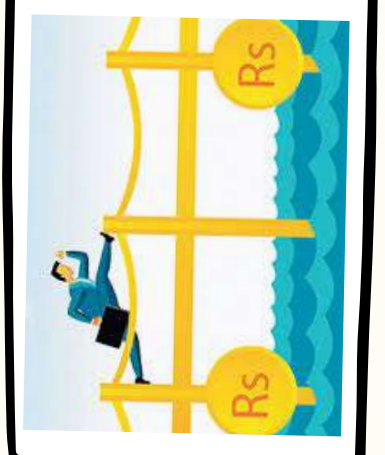
(ii) Regular Drawings

★ Situation 6. When the rate of interest is given without the word 'per annum (p.a.)'





(ii) Regular Drawings



✦ Situation 6. When the rate of interest is given without the word 'per annum (p.a.)'

Notes

- ✦ 'per annum (p.a.)' word is not written or with the rate, at an average rate is written. The interest will be calculated with given rate without considering the time factor means interest will be charged for 1 year.



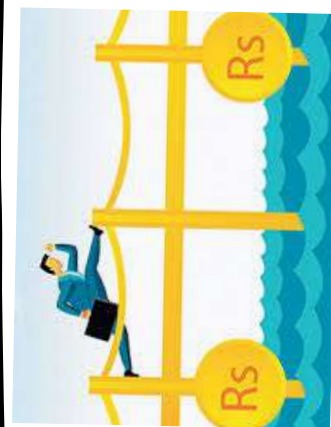


Interest on Partners' Drawings

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Case 6 a

(ii) Regular Drawings



Situation 6. When the rate of interest is given without the word 'per annum (p.a.)'

Calculate interest on X's drawings @12%

Case 6a.

If he withdraws ₹4,80,000 during the year.

Interest on Drawings = Total Drawings x $\frac{\text{Rate of Interest}}{100}$

$$= ₹4,80,000 \times \frac{12}{100}$$

$$= ₹57,600$$

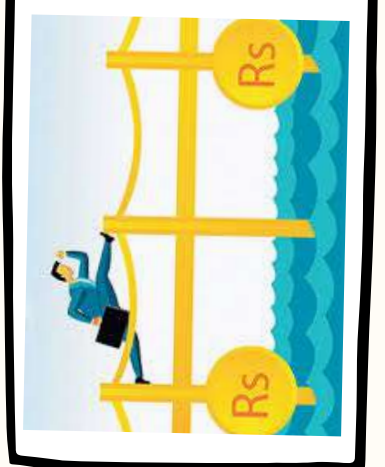




Interest on Partners' Drawings

Case 6 b

(ii) Regular Drawings



✦ Situation 6. When the rate of interest is given without the word 'per annum (p.a.)'

Calculate interest on X's drawings @12%

Case 6b.
If he withdraws ₹2,000 per month during the year.
Interest on Drawings = $\frac{\text{Total Drawings} \times \text{Rate of Interest}}{100}$
 $= (\text{₹ } 2,000 \times 12) \times 12/100$
 $= \text{₹ } 2,880$





Note

While calculating interest, rate as % with the word 'per annum' and the rate '%' without the word per annum must be read very carefully.



Excercise



1

Money withdrawn against the anticipated profits, by a partner for personal use on 1st July 2019 ₹10,000 and interest on drawings is 6% p.a. (Books are closed on 31st March)
The amount of interest will be rupees:

(A) ₹ 600

(C) ₹ 350

(B) ₹ 450

(d) No interest will be charged



Excercise



2

What will be the Interest on drawing of Mr. Z from the following information as on 31.03.2021 Mr. Z withdrew ₹1200 per month in the middle of each month? The partnership deed is silent on interest on drawings.
Interest on drawings will be:

(A) ₹ 864

(C) ₹ 720

(B) ₹ 432

(d) No interest will be charged



Excercise



3

1.If a fixed amount is withdrawn by a partner on the last day of each quarter, interest on the total amount is charged for months

(A) 6

(C) 7.5

(B) 4.5

(d) 3



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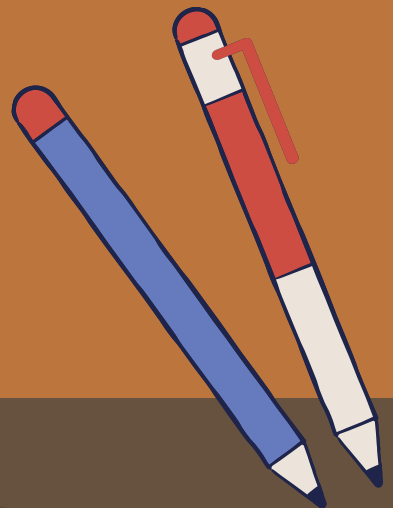
Feel free to approach us
if you have any questions.

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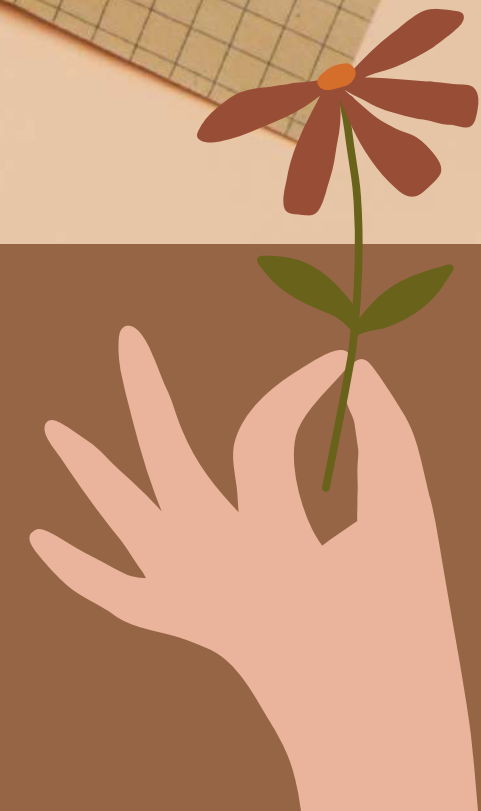
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THANK YOU



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