3RD SEMESTER.CCI.CH &CG

PARTNERSHIP NACCOUNTING

CHAPTER-2……TREATMENT OF LIFE POLICY

Introduction: Sometimes , partners agree to take life policy either in the name of individually or jointly to overcome the financial stringency for the payment of dues in the event of death of any partner. Such policies are taken by the firm and pays insurance premium there for. The Insurance policy matures on the death /expiry of partner or on the expiry of the policy which occurs earlier.

This insurance policy is a property of the firm on which all the partners have their proportionate stake. Hence it should be adequately accounted for in the case of change in constitution of a firm (admission , Retirement, etc.) and in the event of death also.

It is important to mention the term Surrender Value and Maturity value of the policy. **Maturity value** is an amount receivable by the insured , here firm, from the insurance company in the event of the death of a partner or on the expiry of the period. **Surrender value** arise when an insured here firm, terminate or surrender an insurance policy before the date of maturity. In that case insurance company pays an amount to insured for such surrendering . That is, the amount which is receivable by the insured from the insurance company on surrendering all the rights of the insurance policy is known as surrender value. It is not affixed amount rather it changes over the year.

Example: 1 (If policy taken for individual partner) Mr. X , Y and Z ,are partners sharing profit and losses in the ratio 2:2:1. Maturity value (mv) and Surrender value (sv) of the insurance policy , they have taken , are for X –mv-200000 (sv 50000), Y-mv-400000 (sv-100000) and for Z-mv-100000 (sv-20000).

The treatment of these two value depends on the situation arise in a firm such as:- 1. In the case of ADMISSION, RETIREMENT ETC. ------Only surrender value is to be considered and here it is of no significance of maturity value.

2. In the event of DEATH OF PARTNER:- a. Maturity value of deceased partner only is to be considered while Surrender Value of remaining surviving partners are to be taken into account.

Example 2: (If Joint life policy is taken) A,B and C are partners sharing profits & losses in the ratio 2:2:1.The firm has taken a joint life policy of 10,00,000 covering the lives of all partners. The surrender values (S.V) of the policies as on 31st March of last 3 years were as under: 2018—400000 2019—300000 2020—100000.

1. On change in constitution of firm (admission , retirement etc.) : Surrender value of the joint life policy as on that date of change is to be considered.
2. In the event of death Maturity value is to be considered.

ACCOUNTING TREATMENT:-

1. **In case of ILP (Individual Life Policy)** :- a. for payment of premium (say A& B) A' premium a/c ..Dr. B' premium a/c Dr. To Cash/ Bank a/c..

b. At the end of year……..Profit and Loss A/c Dr. To A & B' premium…

c. /1/ In case of any constitutional change (when premium is borne by firm and desire to reflect in the books)

Individual life policy a/c Dr…. To Existing partners capital a/c (surrender value in existing profit sharing ratio)

When it is not reflected in the books…..ILP may raised and written off or capital adjustment may be made (like goodwill treatment).

c./2/ In case of the event of death:- a. On maturity of ILP -----

ILP Receivable (deceased partner) A/c Dr….. To All partners' capital a/c (in old profit ratio)……

b. On receipt of maturity value------ Bank a/c Dr….. To ILP Receivable A/c….

c. For the surrender value of existing partner ----- ILP A/c (of all surviving partners)..Dr…To Existing partners capital A/c (in old profit ratio)

Alternatively, it may be raised among all partners and written off between existing partners in new ratio.

2. IN CASE OF JOINT LIFE POLICY (JLP) A/ When JLP is treated as an expenses of the firm and not as an asset.

a. On payment of prmium**………..** JLP premium a/c Dr. .. To Bank a/c and P/L a/c Dr… To JLP premium a/c… (here, premium is considered as revenue expenditure and is not appeared in Balance sheet as it not treated as asset . Hence , surrender value of the JLP is not reflected in the books.

b. On the constitutional change of the firm i. JLP a/c ..Dr. (Raised)

To Existing partners capital a/c (in old p.s.r)

If raised it must be written off in this way….Continuing partners a/c Dr. (written off) To JLP a/c (in p.s.r)

Alternatively Gaining partners Capital A/c Dr. To sacrificing partner Capital A/c

c. On the event of death of partner…for maturity of the JLP…
JLP receivable a/c Dr… To existing partners capital a/c (p.s.r)
For receipt of M.V…Bank A/c Dr. To JLP Receivable a/c

B/ **WHEN JLP IS TREATED AS ASSET OF THE FIRM**……..In that case premium paid on JLP is treated as investment in an asset and considered as capital expenditure and is also reflected in Balance sheet at its surrender value.

First method …Surrender value method…

a/for premium….JLP A/c DR.. To Bank….

b/ For the excess of premium paid over the increase in surrender value------ P/L..A/c ..Dr... To JLP A/c…

Alternatively JLP Reserve method a/ JLP A/c Dr. To Bank A/c…

b/ for creation of Reserve P/L appropriation A/c Dr. To JLP Reserve

c/ JLP Reserve A/c Dr.. To JLP A/c (for excess of surrender value)

EXAMPLE-1 A.B and C three partners of a firm sharing profit and losses equally took ILP of Rs.50000,40000 and 60000 and for which annual premium paid for Rs. 5000, 4000 and 6000 respectively. Mr. C died and firm received sum assured of C .Surrender value of A & B were Rs. 4000 and 2000 . Journalize the transactions.

SOL.

Date	Particulars	Amount….Dr	Amount..Cr
	Individual Life Insurance premium A/c ……Dr To Bank A/c (5000+4000+6000) (for paid premium)	15000	 15000
	C' Life policy Receivable A/c………………..Dr To A' Capital …………………………………….. To B' Capital ……………………………………… To C' Capital…………………………………….. (Transfer of policy amount receivable on C's expiry in the profit sharing ratio 1;1:1)	60000	 20000 20000 20000
	Bank A/c A/c …………………………………. Dr. To C's LP Receivable ………………………… (for Policy value received.)	60000	 60000
	ILP A/c………..(4000+2000)…………………Dr. To A' Capital A/c……………………………. To B' Capital A/c…………………………… To C' Capital A/c…………………………… (surrender value of LP raised & credited to all)	6000	 2000 2000 2000

	A' Capital A/c ....Dr B' Capital A/c......................................Dr To ILP A/c .... (for written off the ILP)	3000 3000	6000
	Profit & Loss A/c ....Dr. To Individual life policy A/c.............. (premium transferred)	15000	15000
	<u>ALTERNATIVELY, by passing capital adjustment without raising or raising and written off method as per working below.</u> A' Capital A/c ....Dr. B' Capital A/c.................................. Dr. To C' Capital A/c.............................. (S.V adjusted through capital account)	1000 1000	2000

Working:-

Particulars	Surrender value	A	B	C
Right to S.V before death of C 1:1:1)	6000	2000	2000	2000
Right to S.V after death (ratio,1:1)	6000	3000	3000	-
(+)gain /(-) Loss		+1000	+1000	-2000

EXAMPLE-2 Mr. A, B & C sharing profit & losses in the ratio 3:2:1 took a JLP of Rs.300000 on 1/1/17 and annual premium paid Rs. 20000 .The surrender value of the policy at the end of accounting year on Dec. each year were as under: 2017-nil,2018-16000, C died on April.1,2019 and Insurance co. accepted the claim of the business.

Show journal entries if 1) JLP premium is treated as revenue expenditure 2) Premium is treated as capital expenses 3)If JLP Reserve is maintained.

SOL

Date	Particulars	Dr. Amount	Cr, Amount
Case-1 2017	JLP premium A/c ....Dr. To Bank...	20000	20000
	P/L A/c ....Dr. To JLP premium	20000	20000
2018	Same entry		
2019	1st Two entries same and then the follwing		
2019	JLP Receivable A/c.................................Dr To A' Capital A/c................................. To B' Capital A/c.................................. To C' capital A/c .... (Claim Due on death of C transferred)	300000	150000 100000 50000
	Bank A/c..Dr. To JLP Receivable .... (Dues of claim received)	300000	300000

Case-2 2017	JLP A/c ……………………………………………Dr To Bank (annual premium paid)	20000	 20000
	P/L A/c ……………………………………………Dr To JLP A/c…………… (written off in full being S.V nil)	20000	 20000
2018	JLP A/c ……………………………………………Dr To Bank A/c ……………………………………	20000	 20000
	P/L A/c ….(O/balance +20000-16000) To JLP A/c …………………………………… (excess of premium paid over S.V written off)	4000	 4000
2019	JLP A/c ………………………………………………Dr. To Bank A/c…………………………………	20000	 20000
	JLP Receivable A/c………………………Dr To JLP ……………………………………….	300000	 300000
	JLP A/c …………300000-20000 (premium)-16000 (SV) To A' Capital A/c…………………………………….3/6 To B' Capital A/c,,,2/6, To C' Capital A/c……………………………………1/6 (Balance transferred)	264000	 132000 88000 44000
	Bank A/c ……………………………………Dr. To JLP Receivable………………………	300000	 300000
Case-3 2017	JLP A/c ……………………………………Dr. To Bank…………………………………………	20000	 20000
	P/L Appropriation A/c ……………….Dr. To JLP Reserve A/c…………………………………..	20000	 20000
	JLP Reserve A/c……………………………Dr. To JLP A/c……………… Premium (20000)minus S.V(nil)	20000	 20000
2018	JLP a/c …………………………Dr. To Bank……………………………………	20000	 20000
	P/L Appropriation A/c ………………Dr To JLP Reserve A/c	20000	 20000
	JLP Reserve A/c ……(opening balance +20000-SV) DR To JLP A/c ……………….	4000	 4000
2019	JLP A/c ……………………………………………Dr To Bank A/c……………………………………	20000	 20000
	JLP Reserve A/c ……………………(balance) To JLP A/c…………………………………	16000	 16000
	JLP Receivable A/c ……………………Dr. To JLP A/c……………………………………	300000	 300000
	JLP A/c ……….(300000-premium)………… To A' Capital A/c…………………………………3/6 To B' Capital A/c…………………………………2/6 To C' Capital A/c ……………………………….1/6	280000	 140000 93333 46667
	Bank A/c ……………………………………Dr To JLP Receivable A/c………………………	300000	 300000

CASE-2 **LEDGER** JOINT LIFE POLICY A/C

1/1/17	To Bank (premium)	20000	31/12	By Profit & loss A/c (written off)	20000
1/1/18	To Bank A/c (premium)	20000	31/12	By profit & loss By Balance c/d (surrender value)	4000 16000
1/1/19 1/1/19 1/4/19	To balance b/d To Bank (premium) To partners' capital A/c A' Capital 3/6x264000 B' capital 2/6x264000 C' capital 1/6x264000	16000 20000 132000 88000 44000	1/4/19	By Joint life policy Receivable	300000