Partners' Capital Account

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A Partnership is a business association where two, or more people come together to start a business entity with the aim of making a profit. Partners usually come together to achieve their object, and this is seen through individuals partners commitment. Under the partnership, there is always capital contribution by each partner to the business. There are still different kind of partners, where we have we have limited partner, and general partner and this dictates their contribution to the partnership. Partners come into business to invest their capital or finances into the entity, and this kind investment needs an account to record the amount of capital investment. Partnership capital account is an ownership /equity account representing, partner's contribution into the business and it contains the following elements; partner's contribution, profit and losses according to the provision of the partnership agreement, and distribution to partners (Partners Capital Account 2014).

Partnership capital accounts is also a record of contribution by partner's, drawing, interest on capital, profit and losses according to documented ratio, and even upon revaluation of assets of a business entity. This type of account also record the returns that belong to business after taxation of the business entity by tax authorities. In this relation, every partnership must keep proper accounting records in the capital accounts since this will be useful in even calculating purchased goodwill of the business. In partnership business, there are two types of partners' capital accounts, and they include; fixed and fluctuating capital account where the first one having fixed balances and the latter having changing balances each year (Wood & Sangster 2005). A partnership account, either fixed or fluctuating depending on the existence or non-existence of a partnership agreement. The absence of partnership agreement warrants the use of fluctuating accounts plus current accounts in dealings with the partners and the business as a whole.

Partners make several contributions to the partners' capital account, and this is indicated in the partnership agreement. The accounts show the partner's equity in the partnership and partners usually contributes the following to the accounts. The first one is the contribution made by individual partners to the entity either in cash or the form of property the give to the partnership. In support of this partners can opt to contribute their money, or their property like trucks, land, etc. Partners also contribute payments given to them inform of incomes to establish the account. Now partners can earn some income from the business, and this will be credited to the capital account whenever they submit it to increase their capital accounts. In addition to these, profits and losses contribute to the capital accounts too. Once profit and loses have been shared according to the provision of the partnership agreement, profits are credited to the partners' capital account while losses are debited based on the rule of double entry. There are constituents of the capital account, and some increases the balances of the account and some reduces the scales of the same account.

Whenever partners make drawings from the partnership, the account balances are reduced, interest on capital also reduces the balances. Besides, losses also minimize the account balances, and all these are always a debit balance on the partner's capital account. Partner's contribution, interest on drawing and admission of new partners increase the partners' account balance and are credited to the partners' capital account. Majorly capital contribution and interest contribution are the main things that partners contribute to the partnership.

Profit and losses in the partnership are shared according to the profit and loss sharing ratio. The gain of a business has always arrived after the business has paid corporate tax and if possible the partner's salaries paid to them (Wood & Sangster 2005). The ratio is in a document called partnership agreement which can be either written or not, however, it has to be certified accountant or a lawyer as this will ease the work between partners and also minimize confusion and conflict amongst partners. The agreement is in writing has the following content; capital contribution, profit and loss sharing ratio, interest on capital and drawing, salaries to be given to a partner, and final rules to be followed when admitting a new partner or upon dissolution of the existing partnership among others (Wood & Sangster 2005).

The profit and loss are distributed in strict compliance with the agreement for, example, Smith and Ethen are partners in Sunshine, and firm they agreed to share profits and losses in ratio 3:2 and their capital contribution is $10000 and $ 9000 respectively, and the net business profit is $36000. Then the profit will be $ 21600 and $14400 accordingly. Where the agreement does not exist, the gains are shared equally, and both Smith and Ethen would both get $18000 each, neither salaries to partners nor interest on capital and drawing are allowed (Wood and Sangster 2005).

There are various kinds of income ratios when it comes to partnership business. To start there is liquidity ratio which deals how quick business can convert its current assets mostly to cash, under this, we have the current ratio, quick ration amongst others (Financial Analysis 2011). There is also solvency ratio which is an indicator of how fast a business can pay its debt, here there is debt ratio, debt to equity ratio, etc. Finally, there is profitability and activity ratio with the first one dealing with how the business is earning returns to the company, and the latter indicating the number of activities that a business does transaction faster, and it is always shown in times (Financial Analysis 2011). These income ratios differ because they have different users for example profitability ratio is used by potential investors and shareholders in the making of investment decision, suppliers of business strictly watch solvency ratio.

In conclusion, keeping accounting records in any partnership business is significant since this will help the industry know the amount in its books and also help in legitimizing partnership business. Keeping both current accounts and capital accounts assist both partnership business and individual partners in examining the progress of the firms concerning returns. The partnership also needs to have a written down partnership agreement which will give it the necessary guidelines. Finally, the income ratios like debt ratios are of good use to suppliers and also good reputation of the business before the suppliers. The other ratios for example profitability ratios show the earning of a company.

References

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