

# 1. Introduction to Partnership and Partnership Final Accounts

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## EXERCISE - 1

### Q.1 Objective Questions :

A Select the most appropriate alternatives from the following & rewrite the sentences :

1) When there is no partnership agreement between partners, the division of Profits take

place in ..... ratio.

a) Equal

b) capital ratio

c) initial contribution

d) experience and tenure of partners.

2) To find out Net Profit or Net Loss of the business ..... account is prepared.

a) Trading

b) Capital

c) Current

d) Profit & Loss

3) A ..... is an Intangible Asset.

a) Goodwill

b) Stock

c) Cash

d) Furniture

4) In the absence of an agreement, interest on loan advanced by the partner to the firm is

allowed at the rate of .....

a) 5%

b) 6%

c) 10%

d) 9%

5) Liability of partners in a partnership business is .....

a) Limited

b) Unlimited

- c) Limited and Unlimited
- d) None of the above

**6) The Indian Partnership act is in force since .....**

- a) 1932**
- b) 1881
- c) 1956
- d) 1984

**7) Maximum number of Partners in a firm are ..... according to Companies Act 2013.**

- a) 10
- b) 25
- c) 20
- d) 50**

**B Write the word/phrase/term, which can substitute each of the following sentences.**

**1) Persons who form the partnership firm.**

**Ans:** Partneres

**2) Amount of cash or goods withdrawn by partners from the business from time to time.**

**Ans:** Drawings

**3) An association of two or more persons according to Indian partnership Act 1932.**

**Ans:** Partnership firm

**4) Act under which partnership firms are regulated.**

**Ans:** Indian Partnership Act.

**5) Process of entering the name of partnership firm in the register of Registrar.**

**Ans:** Registration

**6) Partnership agreement in written form.**

**Ans:** Partnership Deed

**7) Under this method capital balances of partners remains constant.**

**Ans:** Fixed Capital Method

**8) Proportion in which partners share profits.**

**Ans:** Profit Sharing Ratio

**9) Such capital method in which only capital account is maintained for each partner.**

**Ans:** Fluctuating Capital Method

**10) The account to which all adjustment are made when capital is fixed.**

**Ans:** Current Account

**11) Expenses which are paid before they are due.**

**Ans:** Prepaid Expensess

**12) The accounts that are prepared at the end of each accounting year.**

**Ans:** Final Accounts

**13) An asset which can be converted into cash easily.**

**Ans:** Current Assets or Liquid Assets

**14) Order in which fixed assets are recorded first in Balance sheet.**

**Ans:** Order of liquidation

**15) The account in which selling expenses of business are recorded.**

**Ans:** Profit & Loss Account

**16) Debit balance of Trading Account.**

**Ans:** Gross loss

**17) Credit balance of profit & loss account.**

**Ans:** Net Profit

**(C) (1) State whether the following statements are True or False with reasons :**

**(1) Partnership firm is a Non-Trading concern.**

**Ans. This statement is False**

Main aim of partnership firm is to earn maximum profit. Partnership Is a trading concern. It undertakes either manufacturing or distributive activities with sole aim of earning profit and distribute that profit among the partners in specife mdo. It is never formed for charitable purpose.

**(2) Profit and Loss Account is a Real Account.**

**Ans. This statement is False**

Account of expenses, losses, gains and incomes is called Nominal account. Profit and Loss Account contains all indirect expenses and Indirect incomes of the firm. Therefore, Profit and Loss Account Is a Nominal Account and not real account.

**(3) Carriage inward is carriage on purchase.**

**Ans. This statement is True**

Total transport expenses incurred on bringing the goods from market to the place of business is called carriage. When goods are purchased, carriage is supposed to be borne by the firm, It is known as carriage inward. It means carriage paid on purchase.

**(4) Adjustments are recorded in Partners Current Account in Fixed Capital Method.**

**Ans. This statement is True**

In Fixed Capital Method, as name suggest capital balances (opening and closing are generally remain fixed. Under this method, adjustments are not to be recorded in Capital Account. All adjustments are recorded in a separate account called Partners Current Accounts.

**(5) Prepaid expenses are treated as liabilities.**

**Ans. This statement is False.**

Prepaid expenses are expenses which are paid before they are due. Therefore, they are considered an asset of the business organisation.

**(6) If partnership deed is silent, partners share profits and losses in proportion to their capital.**

**Ans. This statement is False.**

As per the provisions made under Indian Partnership Act 1932. when partnership deed is silent about profit and loss sharing ratio, partners are supposed to share profits and losses in equal proportion, and not in their capital ratio.

**(7) Balance Sheet is an Account.**

**Ans. This statement is False.**

Financial statement showing all assets and liabilities is called Balance sheet. It is not an account. It is a position statement which shows various assets owned by the firm and various liabilities owned by it. On the left hand side all liabilities are listed and on the right hand side all assets are recorded.

**(8) Wages paid for installation of machinery is a Revenue expenditure.**

**Ans. This statement is False**

Wages paid for Installation of machinery is a capital expenditure and therefore it is added to the cost of machinery. It is generally paid once in a life of an asset. It is a long term and capital expenditure.

**(9) Income received in advance is a liability.**

**Ans. This statement is True.**

When income in respect to next year, it received in the current year, it is known as income received in advance. So, in next year firm will not be able to receive that amount and therefore it is considered as a liability for current year.

**(10) R.D.D. is created on Creditors.**

**Ans. This statement is False.**

R.D.D. stands for Reserve for Doubtful Debts. It is created on the value of debtors. Such provision is made against profit and loss account. In future if loss is incurred on account of bad debts, such amount is used to run the business.

**(11) Depreciation is not calculated on Current Assets.**

**Ans. This statement is True.**

Current Assets means liquid assets having no fixed tenure therefore depreciation cannot be calculated on it. Depreciation is calculated and charged on fixed assets for their use, wear and tear etc.

**(12) Goodwill is an intangible asset.**

**Ans. This statement is True.**

Goodwill is a reputation of business computed in terms of money. Reputation can be experienced but can't be seen or felt. Therefore, Goodwill is an intangible asset.

**(13) Indirect expenses are debited to Trading Account.**

**Ans. This statement is False.**

Indirect expenses means expenses which are not directly related with production of goods and services. Therefore, indirect expenses cannot be debited to Trading Account. All indirect expenses are debited to profit and Loss Account.

**(14) Bank loan is a current liability.**

**Ans. This statement is False.**

Loan usually taken for the period more than 1 year say 5 years from the bank is

called Bank Loan. It is long term loan. It is not repaid within 1 year but paid in installments over number of years. It might be paid in lumpsum at the expiry of term.

**(16) Net profit is debit balance of Profit and Loss Account.**

**Ans. This statement is False.**

In a Profit and Loss Account, when credit side total i.e., total of incomes is more than the debit side total i.e., expenses it is known as credit balance. When incomes exceed expenses there is profit. Therefore credit balance of Profit and Loss Account indicates net profit.

**D Find odd one**

**1. Wages, Salary, Royalty, Import Duty. .**

**Ans: Salary**

**2. Postage, Stationery Advertising, Purchases.**

**Ans: Purchases**

**3. Capital, Bills Receivable, Reserve Fund, Bank overdraft**

**Ans: Bills Receivable**

**4. Building, Machinery, Furniture, Bills payable.**

**Ans: Bills payable**

**5. Discount received, Dividend received, Interest received, Depreciation.**

**Ans: Depreciation**

**E Complete the Sentences**

1) Partners share profit & losses in **equal** ratio in the absence of partnership deed.

2) Registration of Partnership is **optional** in India.

3) Partnership business must be **lawful**

4) Liabilities of Partners in Partnership firm is **unlimited**

5) The balance of Drawings Account of a partner is transferred to his **current** account under the Fixed Capital Method.

- 6) The interest on capital of a partner is debited to **profit and loss** account.
- 7) Partners are **joint & several** liable for the debts of the firm.
- 8) Partnership Deed is an **Article** of Partnership.
- 9) The withdrawal by partner for personal use from the firm is **debited** to his account.
- 10) Commission payable to partner is **liability/outstanding expense** to the firm.
- 11) When partners adopt Fixed Capital Method then they have to operate **Partner's Current Account** Account.
- 12) If partners Current Account shows **credit** balance it is shown to the liability side of Balance sheet.
- 13) The expenses paid for trading purpose are known as **trade** expenses.
- 14) Cash receipts which are recurring in nature are called as **revenue** Receipts.
- 15) Return outward are deducted from **purchase**
- 16) Expenses which are paid before due date are called as **prepaid expenses**
- 17) Assets which are held in the business for a long period are called **Fixed Assets**
- 18) Trading Account is prepared on the basis of is **direct** expenses.
- 19) When commission is allowed to any partner, it is **expenditure** of the business.
- 20) When goods are distributed as free samples, it is treated as **advertisement expenses** of the business.

**(D) Answer in one sentence only:**

**(1) What is Fluctuating Capital ?**

**Ans.** When capital balances of the partners go on changing every year due to transactions of partners with the firm, it is known as Fluctuating Capital.

**(2) Why is Partnership Deed necessary ?**

**Ans.** Partnership Deed is necessary to prevent disputes or misunderstandings among the partners in future.

**(3) If the Partnership Deed is silent, in which ratio, the partners will share the profit or loss?**

**Ans.** If the Partnership Deed is silent, partners will share profits and losses in equal ratio.

**(4) What is the Fixed Capital Method ?**

**Ans.** Fixed Capital Method is one in which capital balances of the partners remains same at the end of every financial year unless any amount of additional capital is introduced or part of the capital is withdrawn by the partner from the business.

**(5) How many partners are required to form a partnership firm ?**

**Ans.** Minimum two persons are required to form a partnership firm.

**[6) What is Partnership Deed ?**

**Ans.** A partnership deed is a written agreement duly stamped and signed document containing the terms and condition of the partnership.

**[7) What are the objectives of the Partnership Firm ?**

**Ans.** To earn maximum profit is the main objective of the partnership firm.

**(8) What rate of interest is allowed on partner's loan in the absence of an agreement ?**

**Ans.** 6% is the rate of interest to be allowed on partner's loan in the absence of an agreement.

**(9) What is the minimum number of partners in a partnership firm according to Indian Partnership Act 1932 ?**

**Ans.** Minimum two persons are required number of partners in a partnership firm according to Indian Partnership Act 1932.

**(10) What is liability of a partner ?**

**Ans.** Liability of a partner (except minor partner) is unlimited.

**(11) In the absence of Partnership Deed, what is the rate of interest on loan advanced by partner to the firm is allowed ?**

**Ans.** In the absence of Partnership Deed, 6 % is the rate of interest on loan advanced by partner to the firm.

**(12) What do you mean by pre received income ?**

**Ans.** Income which is received by the partnership firm before it is due is called pre received income.

**(13) What is the effect of the adjustment of provision for discount on debtors in the final accounts of partnership ?**

**Ans.** The effects of the adjustment of provision for discount on debtors in the final accounts of partnership are as follows: Debit Profit and Loss A/c and deduct the amount of provision for discount on debtors from the amount of debtors.

**(14) When is Partners Current Account is opened ?**

**Ans.** When Fixed Capital Method is adopted by the firm. Partners Current Account is opened.

**(15) As per which principle of accounting, closing stock is valued at cost price or at market price whichever is less?**

**Ans.** As per Conservatism principle of accounting, closing stock is valued at cost price or at market price whichever is less.

**(16) What is the provision of Indian Partnership Act with regard to Interest on Capital ?**

**Ans.** As per provision of Indian Partnership Act. Interest on Capital is not to be allowed.

**(17) Why is Balance Sheet prepared ?**

**Ans.** Balance Sheet is prepared to know the financial position of the business in the form of its assets and liabilities on a particular date.

**(18) Why wages paid for installation of machinery are not shown in Trading Account ?**

**Ans.** Wages paid for installation of machinery is a capital expenditure and it is not to be recorded in Trading Account

**(19) What do you mean by indirect incomes?**

**Ans.** All Incomes other than direct incomes are called indirect incomes. [e.g. Interest received on investment, Incomes like discount, commission, dividend, rent etc. received].

**(20) Why partners capital is treated as long-term liability of business ?**

**Ans.** Partner's Capital is not refunded during the existence of partnership firm unless partner is retired or expired.

**G Do you agree/disagree with the following statements.**

**1) When Partnership Deed is silent, Partners share profits of the firm according to capital ratio.**

**Ans:** Disagree

**2) Current account always shows a debit balance.**

**Ans:** Disagree

**3) It is compulsory to have a partnership agreement in writing.**

**Ans:** Disagree

**4) Partnership Firm is a trading concern.**

**Ans:** Agree

**5) An interest on capital is an expenditure for the partnership firm.**

**Ans:** Agree

6) Partnership is an association of two or more persons.

Ans: Agree

7) Partners are entitled to get Salary or Commission.

Ans: Disagree

8) The balance of Capital Account remains constant under Fixed Capital Method.

Ans: Agree

9) The Indian Partnership Act, came into existence in the year 1945.

Ans: Disagree

10) Profit and Loss Account reflects the true Financial position.

Ans: Disagree

11) Amount borrowed by partner from his business will be debited to Current Account.

Ans: Agree

12) Sold but undispached goods must be part of valuation of closing stock.

Ans: Disagree

13) Carriage Inward is a selling and distribution overhead

Ans: Disagree

14) Gross profit is an operation profit

Ans: Disagree

15) All financial expenditures are debited to profit and loss account.

Ans: Agree

16) Free distribution of goods is debited to trading account.

Ans: Disagree

H. Calculate the following:

1. Undervaluation of Closing Stock by 10%. Closing Stock was ₹30,000 find out the value of Closing Stock

**Solution:** Undervaluation of closing stock by 10%

$$\text{Revise value} = \frac{\text{Book value}}{100 - \% \text{ of undervaluation}} \times 100$$

$$= \frac{30,000}{100 - 10} \times 100$$

$$= ₹ 33,333$$

∴ valuation of closing stock = ₹33,333.

2. Calculate 12.5% P. A.depreciation on Furniture -

a) on ₹ 220,000 for 1 year

b) on ₹10,000 for 6 months

**Solution:**

Depreciation = Amount of Asset X Period X %

(a) Depr. On furniture =

$$2,20,000 \times 1 \times \frac{12.5}{100}$$

$$= ₹27,500$$

∴ Depreciation on furniture for 1 year = ₹27,500

(b) Depr. On furniture =

$$10,000 \times \frac{6}{12} \times \frac{12.5}{100}$$

$$= ₹625$$

∴ Depreciation on furniture for 6 months = ₹625

3. Insurance Premium is paid for the year ending 1st September 2019 Amounted to ₹1,500. Calculate prepaid insurance assuming that the year ending is 31st March 2019.

**Solution:** From 31st March to 1st September, 5 months period prepaid insurance amount we have to find. Insurance premium paid for 12 months is = 1500

∴ for 5 months period it is

$$1500 \times \frac{5}{12} = ₹625$$

Thus, prepaid insurance premium amount = ₹625

4. Find out Gross profit / Gross Loss Purchases ₹ 30,000, Sales ₹ 15,000, Carriage Inward ` 2,400, Opening Stock ₹ 10,000, Purchase Returns ₹1,000, Closing Stock ₹ 36,000.

Solution:

Dr.		Trading Account (Partial)		Cr.	
Particulars	Amount (₹)	Amount (₹)	Particulars	Amount (₹)	Amount (₹)
To Opening Stock		10,000	By Sales		15,000
To Purchase	30,000		By Closing Stock		36,000
Less : Purchase Return	1,000	29,000			
To Carriage Inward		2,400			
To Gross Profit		9,600			
		51,000			51,000

5. Borrowed Loan from Bank of Maharashtra ₹ 2,00,000 on 1st October 2019 at rate of 15% p.a. Calculate Interest on Bank Loan for the year 2019-20 assuming that the financial year ends on 31st March, every year.

Solution:

From 1st October to 31st March, 6 months period interest on loan is to be calculated.

Interest

$$\text{Interest} \times I \times \frac{\text{PNR}}{100}$$

∴ Interest on loan =

$$2,00,000 \times \frac{15}{100} \times \frac{6}{100}$$

$$= ₹15,000$$

∴ Interest on loan ₹2,00,000 for 6 months = ₹15, 000