CBSE Test Paper 01

Ch-2 Fundamentals of partnership and Goodwill

1. Goodwill is capitalized valued of ____.
   a. Normal Profit
   b. Super Profit
   c. Capital employed
   d. Gross Profit
2. A, B, and C were partners in a firm having no partnership agreement. A, B and C contributed ₹2,00,000, ₹3,00,000 and ₹1,00,000 respectively. A and B desire that the profits should be divided in the ratio of capital contribution. C does not agree to this. How will the dispute be settled? Who is correct?
   a. C
   b. Both C and A
   c. B
   d. A
3. Which of the following is not a content of partnership deed?
   a. Interest on Bank Loan
   b. Interest on Drawings
   c. Interest on Partner's Loan
   d. Interest on Capital
4. Money withdrawn by a partner on 1st July Rs. 20,000 and interest on drawings is fixed @ 6% (Books are closed on 31st March.) The amount of interest will be Rupees:
   a. 900
   b. No interest will be charged.
   c. 1,200
   d. 600
5. In the absence of Partnership deed profit sharing ratio will be:
   a. Senior partner will get more profit
   b. Capital Ratio
   c. Equal ratio irrespective of partners capitals.
   d. Profits will not be distributed

6. Calculate interest on drawings of Mr. X @ 10% p.a. if he withdrawn Rs. 1000 per month (i) in the beginning of each Month (ii) In the middle each of month (iii) at end of each month.
   Total Amount withdrawn = Rs. 1000×12=12, 000.
7. When will you record Goodwill in the books, as per Accounting Standard-26 (AS-26)?
8. Where would you record interest on drawings when capitals are fluctuating?
9. Define Goodwill.
10. Distinguish Between Average Profit Method and Super Profit Method.
11. When and why rectifying entries are made in the partners' capital accounts?
12. Singh and Gupta decided to start a partnership firm to manufacture low cost jute bags as plastic bags were creating many environmental problems. They contributed capitals of Rs 1,00,000 and Rs 50,000 on 1st April, 2012 for this. Singh expressed his willingness to admit Shakti as a partner without capital, who is specially abled but a very creative and intelligent friend of his. Gupta agreed to this. The terms of partnership were as follows

    a. Singh, Gupta and Shakti will share profits in the ratio of 2: 2: 1.
    b. Interest on capital will be provided @ 6% per annum.

    Due to shortage of capital, Singh contributed Rs 25,000 on 30th September, 2012 and Gupta contributed Rs 10,000 on 1st January, 2013 as additional capital. The profit of the firm for the year ended 31st March, 2013 was Rs 1,68,900.

    i. Prepare profit and loss appropriation account for the year ending 31st March, 2013.
    ii. Identify any two values which the firm wants to communicate to society.
13. Azad and Benny are equal partners. Their capitals are Rs 40,000 and Rs 80,000, respectively. After the accounts for the year have been prepared it is discovered that interest at 5% p.a. as provided in the partnership agreement, has not been credited to the capital accounts before distribution of profits. It is decided to make an adjustment entry at the beginning of the next year. Record the necessary journal entry.

14. A, B and C sharing profits in the ratio 3:2:1 respectively. C wants that profits be shared equally and it should be applicable retrospectively from the last three years. Other partners have no objection to this. Profits for the last three years were Rs 1,20,000, Rs 94,000 and Rs 1,10,000 respectively. Record adjustment that means of a journal entry and show the working notes.

15. L, M, and N were partners in firm sharing profit in the ratio of 3 : 4 : 5. Their fixed capitals were L Rs 4,00,000 , M Rs 5,00,000 and N Rs 6,00,000 respectively. The partnership deed provided for the following:

    i. Interest on capital @ 6% p.a.
    ii. Salary of Rs 30,000 p.a. to N.
    iii. Interest on partner's drawings will be charged @ 12% p.a.

    During the year ended 31.3.2009, the firm earned a profit of Rs 2,70,000. L withdrew Rs 10,000 on 1.4.2008. M withdrew Rs 12,000 on 30.09.2008. and N withdrew Rs 15,000 on 31.12.2008. Prepare profit and loss appropriation account for the year ended 31.3.2009.

Answer

1. b. Super Profit, **Explanation:** Goodwill is the capitalized value of super profits. To find out the super profits, we deducted normal profits from the actual average profits (average profits – normal profits). To find out the value of goodwill, super profit should be capitalised i.e. super profits × 100/Normal Rate of Return.
2. a. C, **Explanation:** C is correct. Profit will be distributed in Equal ratio. When there is no partnership deed or partnership deed is prepared but it is silent on profit sharing ratio, in such a case rules of Partnership Act, 1932 will be applicable. According to which, profits or losses will be shared by the partners equally irrespective of their capitals.
3. a. Interest on Bank Loan, **Explanation:** Interest on bank loan will be fixed by the bank and not by the partners or partnership deed. A partnership deed can show only those contents which are concerned with partners or firm. Interest on bank loan is a charge against the profit. It means it will be paid in all conditions whether there is profit or loss in the business.
4. c. 1,200, **Explanation:** When rate of interest on drawings is fixed, interest will be calculated for the full year i.e. Interest on drawings = 20,000 × 6/100 = 1,200.
5. c. Equal ratio irrespective of partners capitals.
   Explanation: When there is no Partnership deed or Partnership deed is prepared but it is silent on profit sharing ratio, in such a case rules of Partnership Act, 1932 will be applicable. According to which, profits or losses will be shared by the partners equally irrespective of their capitals.
6. Calculation of Average period
   - In the begining of month = (12+1)/2=6.5
   - In the middle of month = (11.5+0.5)/2=6
   - In the end of month = (11+0)/2=5.5

   Calculation of Interest on drawings
   1. Interest on Drawing = amount ×rate/100 ×6.5/12 =Rs. 650
   2. Interest on drawing = amount × rate/100× 6/12 = Rs.600

iii. Interest on drawing = amount ×rate/100 ×5.5/12= Rs. 550

7. According to AS-26, Goodwill should be recorded in the books only when some consideration in money or money's worth has been paid for it. If no consideration is paid for it than no Goodwill Account is raised.
8. When capitals are fluctuating interest on drawings will be recorded on the debit side of partners' capital accounts. As in case of fluctuating capitals method only one capital account is made in which all entries related to appropriation of profit, introduction of capital and drawings etc. are passed.
9. Goodwill is the excess amount paid for purchasing a running business as a whole, over the book values or over the computed value of all tangible assets purchased from that business. Normally, goodwill thus acquired is only of one type (i.e. purchased), appearing in books of account and in financial statements.
10.

Basis	Average Profit Method	Super Profit Method
Meaning	It is average of the profits of past agreed years.	It is the excess of average profit over normal profits
Normal rate of return	Normal rate of return is not relevant in the calculation of average profit.	Normal rate of return is considered while calculating the super profit.

11. Sometimes after the final accounts of the firm have been closed, certain matters may have been omitted or wrongly done. In that case rectifying entry for such mistakes must be made in the partners' capital or current accounts in the beginning of financial year.

12. **Profit and Loss Appropriation Account**

for the year ended 31st March, 2013

Dr.

Particulars		Amount (Rs)	Particulars	Amount (Rs)
To Interest on Capital			By Net Profit as per Profit	1,68,900

A/c's:			and Loss A/c	
Singh	6,750			
Gupta	3,150	9,900		
To Profit Transferred to Capital A/cs:				
Singh	63,600			
Gupta	63,600			
Shakti	31,800	1,59,000		
		1,68,900 =======		1,68,900 ====

Working Note

Interest on Capital

Singh On 1,00,000 = 1,00,000$\times \frac{6}{100}$ = Rs 6,000 ; On 25,000 = 25,000 $\times \frac{6}{100} \times \frac{6}{12}$ = Rs 750

Total interest on Singh's capital = 6,000 + 750 = Rs 6,750; Gupta On 50,000 = 50,000 $\times \frac{6}{100}$ = Rs 3,000 ; On 10,000 = 10,000 $\times \frac{6}{100} \times \frac{3}{12}$ = Rs 150

Total interest on Gupta's capital = 3,000 + 150 = Rs 3,150 Interest on capital is allowable only if there is enough profits to cover it up otherwise not as well as it should be cleared to all that partners shall not be entitled any interest on capital, unless specifically given or written in the partnership agreement. Interest on capital introduced by the partners is calculated on the basis of time of contribution and it should also be considered the introduction of fresh capital by any partner as well as drawings made by the partners. It is important to note here that, the interest on capital provided to a partner is a compensation given to him for his/her investment in the firm foregoing the alternative risk free/risky investment available with even higher return. Interest on capital is necessary to partners because they always not share the profit on the basis of capital contribution ratio rather sometime equally even through the capital contribution is unequal. So, it equalizes the weight to maintain a parity the interest on capital plays a vital role among partners.The values which the firm wants to communicate to the society are:Environment Protection By manufacturing low cost jute bags instead of plastic bags they are protecting the environment from getting polluted.Empathy By admitting Shakti as a partner, who is specially abled, firm has shown empathy and concern towards specially abled people.

13. Interest on capital is always calculated on the basis of opening capital, and with respect to the period it has been used in the business. Simple formula used to be : Interest on capital=(Opening capital * rate*months)/1200 Interest on Capital Azad = 40,000 × $\frac{5}{100}$ =Rs 2,000 Benny = 80,000 × $\frac{5}{100}$ =Rs 4,000

Adjustment of Profit

	Azad	Benny		Total
Interest on Capital	2,000	4,000	=	6,000
Less: Wrong distribution of Profit Rs 6,000 (1: 1)	(3,000)	(3,000)	=	(6,000)
Adjusted Profit	(1,000)	(1,000)	=	NIL

Adjusting Journal Entry

Date	Particulars		L.F	Debit Amount Rs	Credit Amount Rs
	Azad's Capital A/c	Dr.		1,000	
	To Benny's Capital A/c				1,000
	(Adjustment of profit made)				

14. Adjustment entries are journal entries made at the end of an accounting cycle to update certain revenue and expense accounts and to make sure you comply with the matching principle. The matching principle states that expenses have to be matched to the accounting period in which the revenue paying for them is earned. **Books of A, B and C**

Journal

Date	Particulars		L.F	Dr(Rs)	Cr(Rs)
	A's Capital A/c	Dr.		54,000	
	To C's Capital A/c				

	(Being the excess profit already credited now written back from A’s capital and credited to C’s capital)				54,000

Working note: Statement Showing Adjustments

Particulars	A(Rs)	B(Rs)	C(Rs)
Profit already given in the ratio of 3 : 2 : 1 now to be debited	1,62,000(Dr.)	1,08,000(Dr.)	54,000
Profit to be given in the ratio 1 : 1 : 1 to be credited	1,08,000(Cr.)	1,08,000(Cr.)	1,08,000(Cr.)
Adjustments Required	**54,000(Dr.)**	**Nil**	**54,000(Cr.)**

15. The profit and loss appropriation account is an extension of the profit and loss account. The main intention of preparing a profit and loss appropriation account is to show the distribution of profits among the partners. So as per the particulars available in this question the Profit & Loss Appropriation A/c is prepared as follows:-

Profit and Loss Appropriation Account
for the year ended 31.3.2010

Dr.					**Cr.**
Particulars		**(Rs)**	**Particulars**		**(Rs)**
To Interest on Capital			By Net Profit		2,70,000
L's Current A/c	24,000		By Interest on Drawings:		
M's Current A/c	30,000		L's Current A/c	1,200	
N's Current A/c	36,000	90,000	M's Current A/c	720	
To Salary			N's Current A/c	460	2,370
N's Current A/c		30,000			
To Profit transferred to					

L's Current A/c	38,092.50				
M's Current A/c	50,790.00				
N's Current A/c	63,487.50	1,52,370			
		2,72,370			2,72,370

Working Notes:

i. As capitals are fixed, therefore interest, salary, and share of profit will be transferred to partners' current account.

ii. Calculation of interest on drawings

$L = 10{,}000 \times \frac{12}{100} \times 1$ = Rs 1,200

$M = 12{,}000 \times \frac{12}{100} \times \frac{6}{12}$ = Rs 720

$N = 15{,}000 \times \frac{12}{100} \times \frac{3}{12}$ = Rs 450

iii. Interest on capital

$L = 4{,}00{,}000 \times \frac{6}{100}$ = Rs 24,000

$M = 5{,}00{,}000 \times \frac{6}{100}$ = Rs 30,000

$N = 6{,}00{,}000 \times \frac{6}{100}$ = Rs 36,000