

Chapter-1
Accounting for Partnership firms

Ques 1 (Manager's commission)

A & B are partners sharing profits in the ratio of 3:2, with capitals of ₹5,00,000 and ₹3,00,000 resp. Interest on capital is agreed @ 6% p.a. B is to be allowed as annual salary of ₹60,000. During the year 2016-17, the profits prior to the calculation of interest on capital but after charging B's salary amounted to ₹1,80,000. A perm of ₹5% of the profit is to be made in respect of commission to the manager. Prepare P/L Approp. account showing the distribution of profit & the partner's cap A/c for the year ending march 31, 2017.

Solution: Profit and Loss A/c
for the year ended March 31, 2017.

Dr.		Cr	
Particular	₹	Particular	₹
To manager's commin (5% of 2,40,000)	12,000	By profit for the year (1,80,000 + 60,000)	2,40,000
To Net profit.	2,28,000		
	2,40,000		2,40,000

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Profit and loss Appropriation A/c
for the year ended March 31, 2017.

Particulars	₹	Particulars	₹
To B's salary	60,000	By profit & loss A/c	3,28,000
To int. on cap.			
A 30,000			
B 18,000	48,000		
To profit transferred			
A 72,000			
B 48,000	1,20,000		
	2,28,000		3,28,000

Partner's Capital A/c

Date	Particulars	A	B	Date	Particulars	A	B
2017	To Bal. c/d	60,200	4,26,000	2016	By Bal. b/f	5,00,000	3,00,000
Mar 31				2017	By salary	-	60,000
				Mar 31	By int. on cap	30,000	18,000
					By P/L App.	72,000	48,000
					OK		
		60,200	4,26,000			60,200	4,26,000

Ques 142 A & B are partners with capitals of ₹5,00,000 and ₹3,00,000 resp. The profit for the year ended 31st Mar. 2016 was ₹3,46,000 before allowing interest on partner's loan. Show the distribution of profit after taking the following into consideration —

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- Ques i) Int. on A's loan of ₹ 1,50,000 to the firm provided on 1st apr., 2015
- ii) Int. on capital to be allowed @ 5% p.a.
- iii) Int. on drawing @ 6% p.a. Drawings were A ₹ 60,000 & B ₹ 40,000
- iv) B is to be allowed a comm. of 2% on sales. Sales for the year were ₹ 30,00,000.
- v) 10% of the divisible profits is to be kept in a Reserve A/c.

Soln

P/L A/c		P/L A/c	
Parti.	₹	Parti.	₹
To int. on A's loan	9000	By profit before int.	3,46,000
To profit	3,37,000		
	3,46,000		3,46,000

P/L Appropriation A/c			
Parti.	₹	Parti.	₹
To int. on cap.		By profit & loss A/c	3,37,000
A 25000		By int. on draw.	
B 15000	40,000	A 1800	
To comm. to B	60,000	B 1200	3000
To Reserve A/c	24,000		
To profit trans. to			
A 108000			
B 108000	216000		
	3,40,000		3,40,000

Soln.	Product
A : ₹50,000 for the whole 12 months	<u>6,00,000</u>
B : 40,000 for 4 months	160 000
46,000 for 5 months	230 000
30,000 for 3 months	<u>90 000</u>
C ₹80,000 for 5 months	<u>4,80,000</u>
	400 000
₹ 60,000 for 7 months	<u>420 000</u>
	<u>820,000</u>

[illegible]

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Ques 4 X, Y & Z were partners in a firm. on 1st April, 2016 their capitals stood at ₹6,00,000, ₹4,00,000 & ₹2,00,000 resp. As per provision of the partnership deed:

- i) Y was entitled for commission of ₹12,000 p.a.
 - ii) X was entitled for a salary of ₹1200 per month
 - iii) Partners were entitled to interest on cap. @ 8% p.a.
 - iv) Profits were to be shared in the ratio of capitals
- Net profit for the year ended 31 March, 2017 was ₹4,22,400 which was distributed equally without taking into consideration the above provisions. Showing your working clearly pass necessary adjustment entry for the above.

Solu

	X	Y	Z	Total
Commission of Y (Cr.)		12,000		12,000
Salary to X (Cr.)	14,400			14,400
Int. on cap. (Cr.)	48,000	32,000	16,000	96,000
	1,50,000	1,00,000	50,000	3,00,000
Net amount which should have been received (Cr.)	2,12,400	1,44,000	66,000	4,22,400
Less: Profit already dist. equal (Dr.)	1,40,800	1,40,800	1,40,800	4,22,400
	71,600	32,000	74,800	-
	(Dr.)	(Dr.)	(Dr.)	

Ques 5 Anil, Sunil and Ravinder entered into a partnership on 1st April, 2016 to share profits in the ratio of 2:1:1. It was provided in the deed that Ravinder's share of profit will not be less than



₹10,000 per annum. The losses for the year ended 31 March, 2016 were ₹2,00,000 before allowing interest ₹8,000 on Amil's loan which is due for the current year. You are required to show necessary account for division of loss and also pass the necessary journal entries -

Soln.

P/L Account

Particulars	₹	Particulars	₹
To Loss before int.	2,00,000	By Net loss	
To Int. on Amil's loan	8,000	Amil	1,04,000
		Sumil	52,000
		Ravinder	52,000
	2,08,000		2,08,000
			2,08,000

Journals

Date	Particulars	Dr.	Cr.
2016	Int. on Amil's loan A/c	8,000	
Mar. 31	To Amil's loan A/c		8,000
	Profit & loss A/c	8,000	
	To int. on Amil's loan A/c		8,000
	Amil's cap. A/c	1,04,000	
	Sumil's cap. A/c	52,000	
	Ravinder's cap. A/c	52,000	
	To P/L A/c		2,08,000
	Amil's Cap. A/c	81,333	
	Sumil's cap. A/c	40,667	
	To Ravinder's cap. A/c		1,22,000

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Average profit method.

Goodwill of a firm is valued at three year's purchase of the average profits of the last five years. The profits of each year ending 31st March are as under:-

	£		£
2011	50,000 Profit	2014	60,000 Profit
2012	20,000 Loss	2015	80,000 Profit
2013	10,000 Profit		

Calculate the value of goodwill

Solution:

Total Profit of last five years:

$$= ₹ 50,000 - ₹ 20,000 + ₹ 10,000 + 60,000 + 80,000$$

$$= ₹ 1,80,000$$

$$\text{Average Profits} = \frac{₹ 1,80,000}{5} = ₹ 36,000$$

$$\text{Goodwill} = \text{Average profit} \times \text{Number of years's purchased}$$

$$= ₹ 36,000 \times 3 = ₹ 1,08,000$$

Weighted Average Profit method:

The profits of a firm for the last five years were as follows:

Year ended 31st March	Profits (₹)
2011	43,000
2012	50,000
2013	52,000
2014	65,000
2015	85,000

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you are required to calculate the value of goodwill on the basis of two two year's purchase of weighted average profits. The weights to be used are: 2011 — 1 ; 2012 — 2 ; 2013 — 3 ; 2014 — 4 ; 2015 — 5.

Solution.

31st March year ended	Profits (£)	weight	Products
2011	43000	1	43,000
2012	50000	2	1,00,000
2013	52000	3	1,56,000
2014	65000	4	2,60,000
2015	85000	5	4,25,000
		<u>15</u>	<u>9,84,000</u>

$$\text{weighted Average Profits} = \frac{9,84,000}{15} = \text{£} 65,600$$

$$\text{Goodwill} = \text{£} 65,600 \times 2 = \text{£} 1,31,200$$

Super profit method

A firm's average profits are £ 70,000. It includes an abnormal profit of £ 5,000. Capital invested in the business is £ 5,50,000 and the normal rate of return is 10%. Calculate goodwill at four times the super profit.



Solutions:

(1) Calculation of Actual Average profit:

Average Profit	70,000
less: Abnormal profit	5,000
Actual Average Profit	65,000

$$(2) \text{ Normal profits} = \text{Capital Invested} \times \frac{\text{Normal Rate of Return}}{100}$$
$$= 5,50,000 \times \frac{10}{100} = ₹ 55,000$$

$$(3) \text{ Super profit} = \text{Actual Average profit} - \text{Normal profit}$$
$$= 65,000 - 55,000 = ₹ 10,000$$

$$(4) \text{ Goodwill} = \text{Super profit} \times \text{Number of years purchased}$$
$$= ₹ 10,000 \times 4 = 40,000$$

Capitalisation method (1) capitalisation of Average profit

From the figure given below, calculate goodwill according to the capitalisation of Average profit method.

(i) Actual Average profit	72,000
(ii) Normal Rate of Return	10%
(iii) Assets	9,70,000
(iv) Liabilities	4,00,000



Solutions:

$$\begin{aligned} \text{Capitalised value of Average profits} &= \text{Average profit} \times \frac{100}{\text{Normal Rate of Return}} \\ &= 72000 \times \frac{100}{10} = \text{£ } 7,20,000 \end{aligned}$$

$$\begin{aligned} \text{Capital employed} &= \text{Asset} - \text{Liabilities} \\ \text{(i.e. Net Assets as on the date of valuation of goodwill)} &= 970,000 - 400,000 = \text{£ } 570,000 \end{aligned}$$

$$\begin{aligned} \text{Goodwill} &= \text{Capitalised value of Average profit} - \text{Net Assets} \\ &= 720,000 - 570,000 \\ &= \text{£ } 1,50,000 \end{aligned}$$

Capitalisation of Super profit method

From the figures given in Illustration 14, we calculated goodwill according to the capitalisation of super profit method.

Solution:

$$\begin{aligned} \text{Capital Employed} &= \text{Assets} - \text{Liabilities} \\ &= 970,000 - 400,000 = \text{£ } 570,000 \end{aligned}$$

$$\text{Super Profit} = \text{Average Profit} - \text{Normal Profit}$$

$$= 72000 - 57000 (10\% \text{ of } 570,000) \\ = 15,000$$

$$\text{Goodwill} = \frac{\text{Super Profit} \times 100}{\text{Normal Rate of Return}} \\ = \frac{15000 \times 100}{10} = \text{₹ } 1,50,000$$

P, Q and R are partners sharing profits equally. they decided that in future R will get $\frac{1}{5}$ th share in profits. On the day of change, firm's goodwill is valued at 3,00,000. Make the necessary journal entry.

Solution: Old Ratio of P, Q and R, = $\frac{1}{3} : \frac{1}{3} : \frac{1}{3}$

New Ratio of P, Q and R, = $\frac{2}{3} : \frac{2}{5} : \frac{1}{5}$

Sacrifice or Gain:

$$P = \frac{1}{3} - \frac{2}{5} = \frac{5-6}{15} = \frac{1}{15} \text{ (Gain)}$$

$$Q = \frac{1}{3} - \frac{2}{5} = \frac{5-6}{15} = \frac{1}{15} \text{ (Gain)}$$

$$R = \frac{1}{3} - \frac{1}{5} = \frac{5-3}{15} = \frac{2}{15} \text{ (Sacrifice)}$$



Particular

DATE: / /

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20/5

P's capital A/c (1/5 of 3,00,000) 20,000

Q's capital A/c (1/5 of 3,00,000) 20,000

To R's capital A/c (2/5 of 3,00,000) 40,000

(R compensated by P and Q for the sacrifice made by him)