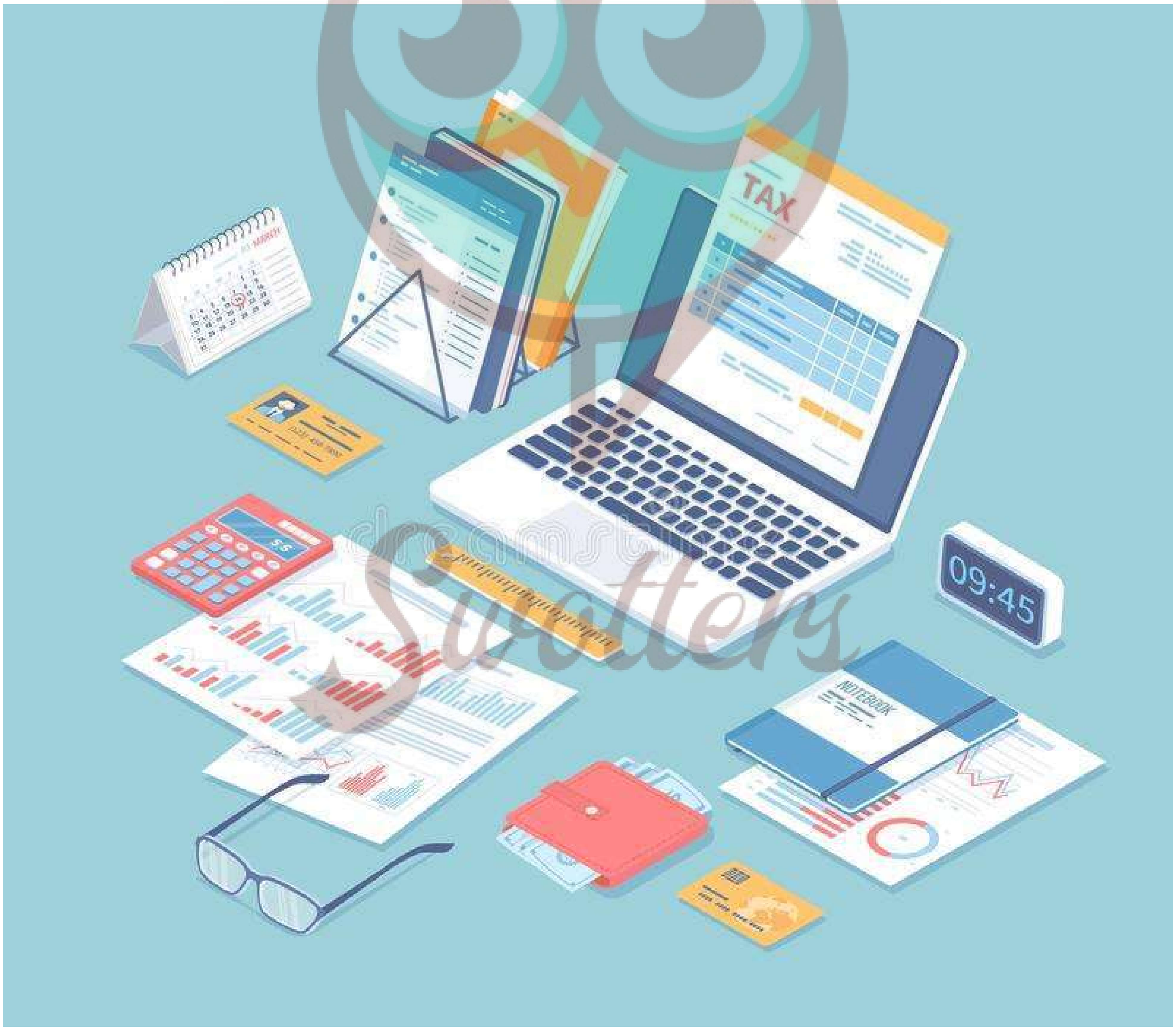
ACCOUNTANCY



Important Questions

Multiple Choice questions-

Question 1. A and B are partners in a firm having a capital of ₹ 54,000 and ₹ 36,000 respectively. They admitted C for 1/3rd share in the profits C brought proportionate amount of capital. The Capital brought in by C would be:
(a) ₹ 90,000
(b) ₹ 45,000
(c) ₹ 5,400
(d) ₹ 36,00
Question 2. Any change in the relationship of existing partners which results at an end of the existing agreement and enforces making of a new agreement is called
(a) Revaluation of partnership
(b) Reconstitution of partnership
(c) Realisation of partnership
(d) None of the above
Question 3. When the new partner brings cash for goodwill, the amount is credited to:
(a) Realisation Account
(b) Cash Account
(c) Premium for Goodwill Account
(d) Revaluation Account
Question 4. Goodwill is an _______ Assets.
(a) fixed
(b) intangible
(c) current
(d) fictitious
Question 5. Value of reputation of the firm is:
(a) Royalty
(b) Assets
(c) Goodwill
(d) Patents
Question 6. ________ profit is excess of actual profits over normal profits.
(a) Net
(b) Average
(c) Super
(d) Appropriated
Question 7. Sacrifice Ratio = _______
(a) New Ratio – Old Ratio
(b) Old Ratio – New Ratio
(c) New Ratio + Old Ratio
(d) Old Ratio + New Ratio

Question 8. Gaining Ratio = ________
(a) New Ratio – Old Ratio
(b) Old Ratio – New Ratio
(c) New Ratio + Old Ratio
(d) Old Ratio + New Ratio
Question 9. Share of old Partners will ________ if new partner admit in the firm.
(a) increase
(b) decrease
(c) remains same
(d) not changed
Question 10. Unrecorded liabilities will be ______ in Revaluation Account.
(a) debited
(b) credited
(c) not shown
(d) shown

Very Short Questions-

1. What is meant by 'Issued Capital'?
2. By which name the profit sharing ratio in which all partners, including the new partner, will share fixture profits?
3. At the time of admission of a partner, who decides the share of profit of the new partner out of the firm's profit?
4. X and Y are partners. Y wants to admit his son K into the business. Can K become the partner of the firm?
5. Name the accounting standard, issued by the Institute of Chartered Accountants of India, which deals with treatment goodwill.
6. Name any one factor responsible which affect the value of goodwill.
7. In which ratio is the profit or loss due to revaluation of assets and liabilities transferred to capital accounts?
8. What is the formula for calculating inferred goodwill?
9. When the new partner brings amount of premium for goodwill, by which ratio is this amount credited to old partners' Capital Accounts?
10. What is the formula of calculating sacrificing ratio?

Short Questions-

1. Identify various matters that need adjustments at the time of admission of a new partner.
2. Why is it necessary to ascertain new profit sharing ratio even for old partners when a new partner is admitted?
3. What is sacrificing ratio? Why is it calculated?
4. On what occasions sacrificing ratio is used?
5. Why is there need for the revaluation of Liabilities and Assets on the admission of a partner?
6. If some goodwill already exists in the books and the new partner brings in his share of goodwill in cash, how will you deal with existing amount of goodwill?

Long Questions-

1. What is goodwill? What are the factors that affect goodwill?
2. Explain how will you deal with goodwill when new partner is not in a position to bring his share of goodwill in cash?
3. Explain various methods for the treatment of goodwill on the admission of a new partner?
4. 7. How will you deal with the accumulated profit and losses and reserves on the admission of a new partner?

Assertion Reason Questions-

1. For two statements are given-one labelled Assertion and the other labelled Reason. Select the correct answer to these questions from the codes (a), (b), (c) and (d) as given below.
   a. Assertion and Reason both are correct and Reason is the correct explanation of assertion
   b. Assertion and Reason both are correct but Reason is not correct explanation of assertion
   c. Assertion is correct but Reason is not correct.
   d. Both Assertion and Reason are False.

Assertion: Anahat and Parminder are partners sharing profits in the ratio of 2:1. They admit Rubayat as partner w.e.f. 1st January 2021. On that date, Goodwill existed in the books at ₹1,00,000. Goodwill of ₹50,000 was written off by debiting capital accounts of

Anahat and Parminder in the ratio of 2:1. While balance goodwill was carried forward in the Balance Sheet.

Reason (R): Goodwill existing in the books is purchased goodwill and therefore, is not written off.

2. For two statements are given-one labelled Assertion and the other labelled Reason. Select the correct answer to these questions from the codes (a), (b), (c) and (d) as given below.

    a. Assertion and Reason both are correct and Reason is the correct explanation of assertion
    b. Assertion and Reason both are correct but Reason is not correct explanation of assertion
    c. Assertion is correct but Reason is not correct.
    d. Both Assertion and Reason are False.

Assertion: Undistributed profits or losses appearing in the balance sheet at the time of admission should be transferred to the old partner's capital/current account.

Reason (R): Undistributed profits or losses appearing in the balance sheet at the time of admission belong to the old partners as they are earned by them.

MCQ Answers-

1. Answer: (b) ₹ 45,000
2. Answer: (b) Reconstitution of partnership
3. Answer: (c) Premium for Goodwill Account
4. Answer: (b) intangible
5. Answer: (c) Goodwill
6. Answer: (c) Super
7. Answer: (b) Old Ratio – New Ratio
8. Answer: (a) New Ratio – Old Ratio
9. Answer: (b) decrease
10. Answer: (a) debited

Very Short Answers-

1. Answer: Issued capital means such capital as the company issues from time to time for subscription-section 2(50) of the companies Act 2013.

2. Answer: New profit sharing ratio

3. Answer: It is decided mutually between the old partners and the new partner.

4. Answer: Yes, if X agrees to it otherwise not

5. Answer: AS26

6. Answer: Location of a business

7. Answer: Old Ratio of existing partners

8. Answer: Net worth of business on the basis of new partner's capital minus net worth of business in new firm

9. Answer: Sacrificing ratio

10. Answer: Sacrificing Ratio = Old Ratio – New Ratio

Short Answers-

1. **Identify various matters that need adjustments at the time of admission of a new partner:**
   i. Capital Adjustment among partners.
   ii. Revised calculation of profit sharing ratio.
   iii. Evaluating and adjusting the goodwill of partners who are sacrificing their share.
   iv. Accumulated profits, reserves and losses should be distributed to old partners as per the old ratio that was agreed upon.
   v. Revaluation of the Liabilities and Assets to determine the current value and distribution of profit or loss as per the old ratio.

2. At the time of admission of a new partner, the existing partners sacrifice their present profit sharing ratio to make way for a share in profit sharing to new partner which results in reducing their profit. Therefore it is essential to determine the new profit sharing ratio for old partners on the occasion of adding a new partner as it creates a more justified share of profit.

3. The portion of profit sharing ratio that is sacrificed by current partners when a new partner joins the firm is called as sacrificing ratio. It is calculated as the difference between old profit sharing ratio and new profit sharing ratio.

   Sacrificing ratio = Old profit sharing ratio – New profit sharing ratio

It is compulsory to determine this ratio as the new partner has to reimburse the existing partner for making the sacrifice of profit. It is paid to them as goodwill.

4. **Sacrificing ratio needs to be used in these occasions:**

   i. When it is mutually decided by partners of the firm to change profit sharing ratio among the partners.

   ii. A new partner is introduced in the firm and accordingly the sum contributed by the new partner is distributed as goodwill based on the sacrificing ratio of existing partners.

5. When a new partner gets admitted in the firm, there is a need to revalue the Liabilities and Assets of the firm for determining the true value on that day. Revaluation is helpful as the value of Liabilities and Assets may increase or decrease and as such their values in old balance sheet may be not justified, also some assets or liabilities may not be recorded at all. Hence, for recording the changes in market value for the Liabilities and Assets, a revaluation account is needed to be prepared and the associated profits or losses needs to be distributed between the existing partners of firm.

6. Goodwill that exists in the firms before arrival of a new partner must be written off between the existing partners in the ratio of their profit sharing as previously decided. The following journal entry needs to be passed.

   Old Partner's Capital A/c Dr.

   To Goodwill A/c

   (Being goodwill written off in the old ratio between existing partners)

Long Answers-

1. Goodwill refers to the intangible asset that represents the firms value and reputation and the brand name that it carries in the market. Goodwill is earned by a firm from the work it does which helps earn people trust by meeting all customer demands both in quality and quantity. Having a positive goodwill is very much helpful for a firm to earn extraordinary profits in comparison to its competitors. It also ensures profits that keep coming in the future and helps in retaining old customers.

   Factors affecting firms' goodwill are:

   i. **Product Quality:** A firm which is constantly delivering the best product for its customers will have a greater goodwill.

   ii. **Location:** A central location makes it easy to reach and attracts more footfalls which leads to higher sales and more goodwill.

iii. **Management:** Cost efficiency and higher productivity can be achieved by having an efficient management in place, also it ensures quality products at less price which increases goodwill.

iv. **Market Structure:** A firm will enjoy more benefits of goodwill if the market is monopolistic in nature and there are no substitutes, it will add more goodwill to the firm.

v. **Other Advantages:** A firm that is getting benefits such as continuous supply of fuel, power and raw materials and uses it to produce quality goods enjoys a higher goodwill.

2. The situation in which a new partner is unable to bring his share of goodwill in cash, the goodwill account gets adjusted through Old Partners account. New partners' capital account is debited with the share of goodwill and the same gets credited to Old Partner's account.

New Partner's Capital A/c		Dr.
	To Old Partners' Capital A/c	
(New Partner account debited)		

Note: According to Para 16 of Accounting Standard 10, Goodwill is recorded only when it is any transaction equivalent to money or money's worth. It is a mandatory practice that is followed.

3. Goodwill is treated in the following ways on introduction of a new partner:

1. Premium Method

2. Revaluation Method

When a new partner pays the share of goodwill in the form of cash, it is called as premium method.

There can be two scenarios:

1. New partners pays directly to old partners.

2. Partner brings goodwill in form of cash and it is retained in the business.

The corresponding entries are:

(i) When goodwill brought in cash by new partner

Cash/Bank A/c Dr.

To Premium for Goodwill A/c

(Amount of goodwill brought in by new partner)

(ii) When goodwill is retained by business:

Premium for Goodwill A/c Dr

To Sacrificing Partners' Capital A/c

(Goodwill brought by new partner distributed among old partners as per the sharing ratio)

Revaluation Method: Situations when new partner is unable to bring goodwill in form of cash

New Partner's Capital A/c Dr. (Goodwill amount not brought by new partner)

To Old Partners' Capital A/c

(Goodwill of new partner distributed to old partners as per their sharing ratio)

Note: According to Para 16 of Accounting Standard 10, Goodwill is recorded only when it is any transaction equivalent to money or money's worth. It is a mandatory practice that is followed.

4. A new partner is not entitled to bear the losses or enjoy the profits of a previous business. Hence, when a new partner is added to the firm, the accumulated profits or losses, reserves needs to be distributed to current partners (partners of old firm) in their profit sharing ratio.

Treatment of accumulated losses, profits and reserve

Profit and Loss A/C Dr.

General Reserve A/C Dr.

Contingency Reserve A/C Dr.

When losses accumulate over a period.

For Profits and losses

Deferred Advertising expense Dr.

(Losses accumulated shared to old partners as per sharing ratio)

Assertion Reason Questions-

1. (d) Both Assertion and Reason are False.
2. (a) Assertion and Reason both are correct and Reason is the correct explanation of assertion.