Treatment of Goodwill & Revaluation of Assets & Re-assessment of liabilities

1 Mark Questions

1. P, Q and R were partners in a firm sharing profits in the ratio of 5 : 4 : 3 respectively. Their capitals were Rs. 50,000, Rs. 40,000 and Rs. 30,000 respectively. State the ratio in which the goodwill of the firm, amounting to Rs. 6,00,000, will be adjusted in the capital accounts of the remaining partners on the retirement of Q. (Compartment 2014)

Ans. The goodwill will be adjusted in the gaining ratio of the continuing partners.

2. Give the journal entry to distribute 'workmen compensation reserve' of Rs. 60,000 at the time of retirement of Sajjan, when there is no claim against it. The firm has three partners Rajat, Sajjan and Kavita. (Delhi 2013)

Ans. **JOURNAL**

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	Workmen Compensation Reserve A/c	Dr		60,000	
	To Rajat's Capital A/c				20,000
	To Sajjan's Capital A/c				20,000
	To Kavita's Capital A/c				20,000
	(Being workmen compensation reserve distributed to old partners in old ratio)				

NOTE Since, the profit sharing ratio is not given, it is distributed equally.

3. Give the journal entry to distribute workmen compensation reserve of Rs. 70,000 at the time of retirement of Neeti when there is a claim of Rs. 25,000 against it. The firm has three partners Raveena, Neeti and Rajat. (All India 2013)

Ans. **JOURNAL**

Date	Particulars		LF	Amt (Dr)	Amt (Dr)
	Workmen Compensation Reserve A/c	Dr		70,000	
	To Liability for Workmen Compensation A/c				25,000
	To Raveena's Capital A/c				15,000
	To Neeti's Capital A/c				15,000
	To Rajat's Capital A/c				15,000
	(Being workmen compensation reserve distributed to old partners in old ratio)				

NOTE Since, the profit sharing ratio is not given, it is distributed equally.

4. For which share of goodwill a partner is entitled at the time of his retirement? (Delhi 2012)

Ans. At the time of retirement, a partner is entitled to get an amount equal to his share out of firm's goodwill.

5. P, Q and R were partners in a firm sharing profits in the ratio of 5 : 4 :3. Their capitals were Rs. 40,000, Rs. 50,000 and Rs.1,00,000 respectively. State the ratio in which the goodwill of the firm amounting to Rs.1,20,000 will be adjusted on the retirement Of R. (All India 2010,2008C)

Ans. R's share of goodwill, i.e. Rs. 30,000 (1,20,000 x 3/12) will be contributed by P and Q in their gaining ratio, i.e. 5 : 4.

6. A, B and C are partners sharing profits in the ratio of 4 : 3 : 2. B retires and the goodwill of the firm is valued at Rs.18,000. Pass journal entry for the treatment of goodwill on B's retirement. (Delhi 2008C)

Ans. JOURNAL

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	A's Capital A/c	Dr		4,000	
	C's Capital A/c	Dr		2,000	
	To B's Capital A/c				6,000
	(Being retiring partner's amount of goodwill adjusted)				

Working Note

Firm's goodwill = ₹ 18,000

B's share of goodwill = $18,000 \times \frac{3}{9}$ = ₹ 6,000, to be contributed by A and C in their gaining ratio, i.e. 4 : 2 or 2 : 1.

4 Marks Questions

7. Arjun, Bheem and Nakul are partners sharing profits and losses in the ratio of 14 : 5: 6 respectively. Bheem retires and surrenders his 5/25th share in favour of Arjun. The goodwill of the firm is valued at 2 years' purchase of super profits based on average profits of last 3 years. The profits of the last three years are Rs. 50,000, Rs.55,000 and Rs. 60,000 respectively. The normal profits of the similar firms are Rs. 30,000. Goodwill already appears in the books of the firm at Rs. 75,000. The profit for the first year after the Bheem's retirement was Rs.1,00,000.
Give necessary journal entries to adjust goodwill and distribute profits showing your workings. (Delhi 2012)

Ans. **JOURNAL**

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	Arjun's Capital A/c	Dr		42,000	
	Bheem's Capital A/c	Dr		15,000	
	Nakul's Capital A/c	Dr		18,000	
	To Goodwill A/c				75,000
	(Being amount of goodwill written-off in old ratio)				
	Arjun's Capital A/c	Dr		10,000	
	To Bheem's Capital A/c				10,000
	(Being amount of goodwill adjusted in gaining ratio)				

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	Profit and Loss Appropriation A/c	Dr		1,00,000	
	To Arjun's Capital A/c				76,000
	To Nakul's Capital A/c				24,000
	(Being profit distributed among partners)				

Working Note

(*i*) **Calculation of New Profit Sharing Ratio**

Old ratio of Arjun, Bheem and Nakul = 14 : 5 : 6

Bheem surrenders in favour of Arjun = $\frac{5}{25}$th share, Arjun's new share = $\frac{14}{25} + \frac{5}{25} = \frac{19}{25}$

New ratio of Arjun and Nakul = 19 : 6

(*ii*) **Calculation of Bheem's Share of Goodwill**

$$\text{Actual average profit} = \frac{50,000 + 55,000 + 60,000}{3} = ₹\ 55,000$$

Normal profit = ₹ 30,000

Super Profit = Average Profit − Normal Profit

= 55,000 − 30,000 = ₹ 25,000

Firm's goodwill = 25,000 × 2 = ₹ 50,000

Bheem's share of goodwill = $50,000 \times \frac{5}{25}$ = ₹ 10,000 (to be contributed by Arjun alone).

8. A, B, C and D are partners sharing profits in the ratio of 3 : 3 : 2 : 2 respectively. D retires and A, B and C decide to share the future profits in the ratio of 3 : 2 : 1. Goodwill of the firm is valued at Rs. 6,00,000. Goodwill already appears in the books at Rs. 4,50,000. The profit for the 1st year after D's retirement amount to Rs. 1,20,000. Give the necessary journal entries to record goodwill and to distribute the profits. Show your calculations clearly. (All India 2012)

Ans. JOURNAL

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	A's Capital A/c	Dr		1,35,000	
	B's Capital A/c	Dr		1,35,000	
	C's Capital A/c	Dr		90,000	
	D's Capital A/c	Dr		90,000	
	To Goodwill A/c				4,50,000
	(Being amount of goodwill in books written-off in old ratio)				
	A's Capital A/c	Dr		1,20,000	
	B's Capital A/c	Dr		20,000	
	To C's Capital A/c				20,000
	To D's Capital A/c				1,20,000
	(Being amount of goodwill adjusted)				
	Profit and Loss Appropriation A/c	Dr		12,00,000	
	To A's Capital A/c				6,00,000
	To B's Capital A/c				4,00,000
	To C's Capital A/c				2,00,000
	(Being profit distributed among partners in new ratio)				

Working Note

(*i*) **Calculation of Sacrificing or Gaining Ratio**

Old ratio = 3 : 3 : 2 : 2 New ratio = 3 : 2 : 1

Gaining Ratio = New Ratio – Old Ratio

$$A = \frac{3}{6} - \frac{3}{10} = \frac{15-9}{30} = \frac{6}{30} \text{ gain,}$$

$$B = \frac{2}{6} - \frac{3}{10} = \frac{10-9}{30} = \frac{1}{30} \text{ gain}$$

$$C = \frac{1}{6} - \frac{2}{10} = \frac{5-6}{30} = \left(\frac{1}{30}\right) \text{ sacrifice}$$

$$\text{A's share in goodwill} = 6,00,000 \times \frac{6}{30} = ₹\,1,20,000$$

$$\text{B's share in goodwill} = 6,00,000 \times \frac{1}{30} = ₹\,20,000$$

$$\text{C's share in goodwill} = 6,00,000 \times \frac{1}{30} = ₹\,20,000$$

$$\text{D's share in goodwill} = 6,00,000 \times \frac{2}{10} = ₹\,1,20,000$$

9. A, B and C were partners sharing profits in the ratio of 6: 4: 5. Their capitals were A Rs. 1, 00,000, B Rs. 80,000 and C Rs. 60,000. On 1st April, 2009 B retired from the firm and the new profit sharing ratio between A and C was decided as 11: 4. On B's retirement, the goodwill of the firm was valued at Rs. 1, 80,000. Showing your calculations clearly, pass necessary journal entry for the treatment of goodwill on B's retirement. (Delhi 2010)

Ans. JOURNAL

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	A's Capital A/c	Dr		60,000	
	To B's Capital A/c				48,000
	To C's Capital A/c				12,000
	(Being amount of goodwill adjusted)				

Working Note

Old ratio among A, B and C = 6 : 4 : 5

New ratio between A and C = 11 : 4

Gaining Ratio = New Ratio − Old Ratio

$$A = \frac{11}{15} - \frac{6}{15} = \frac{5}{15} \text{ gain ;} \qquad C = \frac{4}{15} - \frac{5}{15} = \left(\frac{1}{15}\right) \text{ sacrifice}$$

Here, only A is the gaining partner so, he will compensate both B and C.

$$\text{A's share in goodwill} = 1{,}80{,}000 \times \frac{5}{15} = ₹\,60{,}000$$

$$\text{B's share in goodwill} = 1{,}80{,}000 \times \frac{4}{15} = ₹\,48{,}000$$

$$\text{C's share in goodwill} = 1{,}80{,}000 \times \frac{1}{15} = ₹\,12{,}000$$

10. A, B and C were partners in a firm sharing profits in the ratio of 6 : 5 : 4. Their capitals were A, Rs. 1,00,000, B Rs. 80,000 and C Rs. 60,000 respectively. On 1st April, 2009, C retired from the firm and the new profit sharing ratio between A and B was decided as 11: 4. On C's retirement the goodwill of the firm was valued at Rs. 90,000. Showing your calculations clearly, pass necessary journal entry for

the treatment of goodwill on C's retirement. **(All India 2010)**

Ans.

JOURNAL

Date	Particulars		LF	Amt (Dr)	Amt (Cr)
	A's Capital A/c	Dr		30,000	
	To B's Capital A/c				6,000
	To C's Capital A/c				24,000
	(Being amount of goodwill adjusted)				

Working Note

Calculation of Sacrificing or Gaining Ratio

Old ratio among A, B and C = 6 : 5 : 4 ;

New ratio between A and B = 11 : 4

Gaining Ratio = New Ratio – Old Ratio

$$A = \frac{11}{15} - \frac{6}{15} = \frac{5}{15} \text{ gain;}$$

$$B = \frac{4}{15} - \frac{5}{15} = \left(\frac{1}{15}\right) \text{ sacrifice}$$

Here, only A is the gaining partner so he will compensate both B and C.

$$\text{A gains} = 90{,}000 \times \frac{5}{15} = ₹\ 30{,}000\ ;$$

$$\text{B sacrifices} = 90{,}000 \times \frac{1}{15} = ₹\ 6{,}000\ ;$$

$$\text{C sacrifices} = 90{,}000 \times \frac{4}{15} = ₹\ 24{,}000$$