

### 3. Reconstitution of Partnership (Admission of Partner)

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#### Q.1 Objective type questions.

(A) Select appropriate alternatives from those given below and rewrite the sentences.

1. Anuj and Eeshan are two partners sharing profits and losses in the ratio of 3:2. They decided to admit Aaroh for 1/5th share, the new profit sharing ratio will be .....

- (a) 12:8:5
- (b) 4:3:1
- (c) 12:8:1
- (d) 12:3:1

**Ans: (a) 12:8:5**

2. Excess of proportionate capital over actual capital represents.....

- (a) Equal capital
- (b) Surplus Capital
- (c) Deficit Capital
- (d) Gain

**Ans: (c) Deficit Capital**

3. ....is credited when unrecorded asset is brought into business.

- (a) Revaluation Account
- (b) Balance Sheet
- (c) Trading Account
- (d) Partners capital Account.

**Ans: (a) Revaluation Account**

4. When goodwill is withdrawn by the partner .....account is credited.

- (a) Revaluation
- (b) Cash / Bank
- (c) Current
- (d) Profit and Loss Adjustment

**Ans: (b) Cash / Bank**

5. If asset is taken over by the partner .....account is debited.

- (a) Revaluation
- (b) Capital

- (c) Asset
  - (d) Balance Sheet
- Ans: (b) Capital**

**(B) Write a word/ phrase / term which can substitute each of the following statements.**

**1. Method under which calculation of goodwill is done on the basis of extra profit earned above the normal profit.**

**Ans: Super Profit Method**

**2. An account opened to adjust the value of assets and liabilities at the time of admission of a partner.**

**Ans: Revaluation A/c or Profit and Loss A/c**

**3 Reputation of business measured in terms of money.**

**Ans: Goodwill**

**4 The ratio in which general reserve is distributed to the old partners.**

**Ans: Old Ratio**

**5 Name the method of the treatment of goodwill where new partner will bring his share of goodwill in cash.**

**Ans: Premium Method**

**6 The proportion in which old partners make a sacrifice.**

**Ans: Sacrifice Ratio**

**7  $\text{Capital employed} \times \text{NRR} / 100 =$**

**Ans: Normal Profit**

**8 An Account which is debited when the partner takes over the asset.**

**Ans: Partner's Capital A**

**9 Profit and Loss account balance appearing on liability side of Balance Sheet.**

**Ans: C**

**10 Old ratio - New ratio =**

**Ans: Sacrifice Ratio**

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

**(1) New partner can bring capital in cash or kind.**

**Ans. This statement is True.**

As per provision of partnership deed, when any person is admitted in the firm. he has to bring some amount as capital which can be in cash or in kind of assets to get rights in the assets and definite share in the future profit of the firm.

**(2) When goodwill is paid privately to the partners, it is not recorded in the books.**

**Ans. This statement is True.**

When goodwill is paid privately to the partners, by newly admitted person. Then in such case no transaction takes place in the business and firm as such is not all benefited. Hence it is not recorded in the books of accounts.

**(3) Gain ratio is calculated at the time of admission of partner.**

**Ans. This statement is False.**

At the time of admission of a person, in the business, sacrifices are made by the old partners in favour of new partner. It means there is no question of any gain to the partners, so we can say that Gain ratio is not calculated at the time of admission of partner.

**(4) Revaluation profit is distributed among all partners including new partner.**

**Ans. This statement is False.**

Revaluation profit arises due to efforts and hard working of the old partners in the past and hence profit earned on revaluation of assets and liabilities at the time of admission of a person as a partner in the business belongs to old partners. So, such profit is not distributed among all partners including new partner. It distributed only among old partners.

**(5) Change in relationship between the partners is called as Reconstitution of Partnership.**

**Ans. This statement is True.**

When any person joins business as a partner, change in relationship takes place. The old agreement is terminated and new agreement is prepared. There is change in profit or loss sharing ratio and relationship of the partners which is known as Reconstitution of Partnership.

**(6) New partner always bring his share of goodwill in cash. When new person is admitted in the partnership firm, the old partners surrender certain share in cash.**

**Ans. This statement is False.**

Profit and give it to new partner. In exchange of that new partner is required to bring goodwill in cash or in kind. If he is unable to bring cash for goodwill, then Goodwill is raised and adjusted to new partner's capital A/c.

**(7) When the goodwill is written off, goodwill account is debited.**

**Ans. This statement is False.**

To write off goodwill means to decrease or wipe out the value of goodwill. When goodwill as an asset of business is raised, Goodwill A/C is debited in the books of Account. Conversely, when Goodwill is written off from the business, the Goodwill A/c is credited in the books of business.

**(8) New ratio minus old ratio is equal to sacrifice ratio.**

**Ans. This statement is False.**

When new partner is admitted, old partners have to sacrifice their profit share in favour of new partner and their old ratio gets reduced and whatever ratio left becomes new ratio. Hence, as per equation :  $\text{New Ratio} = \text{Old Ratio} - \text{Sacrifice Ratio}$ . By interchanging the terms,  $\text{Sacrifice Ratio} = \text{Old Ratio} - \text{New Ratio}$ .

**(9) Usually when a new partner is admitted in the firm, there will be an increase in the capital of the firm.**

**Ans. This statement is True.**

When a new partner is admitted in the firm, he brings his share of capital and goodwill, in cash or in kind, to enjoy the right of sharing the future profit and hence there will be an increase in the capital of the firm.

**(10) Cash / Bank Account is credited when goodwill is withdrawn by the old partners. When a new partner bring his share of goodwill, old partners have right to withdraw it in cash.**

**Ans. This statement is True.**

Therefore, when old partners withdraw the amount of goodwill, cash goes out from the firm and not goodwill. Hence Cash/Bank A/c is credited.

**(D) Find odd one :**

(1) General reserve, Creditors, Machinery, Capital

Ans: Machinery

(2) Decrease in Furniture, Patents written off, Increase in Bills payable, R.D.D. written off

Ans: R.D.D. written off

(3) Super profit method. Valuation method, Average profit method. Fluctuating capital method

Ans. Fluctuating capital method

(E) Calculate the following

1. A and B are partners in a firm sharing profits and losses in the ratio of 1:1. C is admitted. A surrenders 1/4th share and B surrenders 1/5th of his share in favour of C. Calculate the new profit sharing ratio.

**Solution:** Old ratio of A and B = 1 : 1

$$\text{or } \frac{1}{2} : \frac{1}{2}$$

$$\text{A's sacrifice} = \frac{1}{4} : \frac{1}{2} = \frac{1}{8}$$

$$\text{B's sacrifice} = \frac{1}{5} : \frac{1}{2} = \frac{1}{10}$$

Sacrificing ratio of A and B

$$= \frac{1}{8} : \frac{1}{10} = 5 : 4$$

C's share = A's share + B's share

$$= \frac{1}{8} : \frac{1}{10} = \frac{5+4}{10} = \frac{9}{40}$$

A's new share = Old ratio - Sacrifice ratio

$$= \frac{1}{2} : \frac{1}{8} = \frac{4-1}{8} = \frac{3}{8}$$

B's new share = Old ratio - Sacrifice ratio

$$= \frac{1}{2} : \frac{1}{10} = \frac{5-1}{10} = \frac{4}{10}$$

Therefore, New ratio of A, B and C =

$$= \frac{3}{8} : \frac{4}{10} = \frac{9}{40}$$

$$=15:16:9$$

(Making denominator equal)

**2. Anika and Radhika are partners sharing profits in the ratio of 5:1. They decide to admit Sanika in the firm for 1/5th share. calculate the sacrifice ratio of Anika and Radhika**

**Solution:** Balance - 1 = 1-share of new partner

$$= 1 - \frac{1}{5}$$

$$= 1 - \frac{4}{5} \text{ (Remaining share)}$$

New Ratio = Old ratio  $\times$  Balance of 1

Anika's New ratio

$$= \frac{5}{6} \times \frac{4}{5} = \frac{20}{30}$$

Radhika's New ratio

$$= \frac{1}{6} \times \frac{4}{5} = \frac{4}{30}$$

Sanika's New ratio

$$= \frac{1}{5} \times \frac{6}{6} = \frac{6}{30}$$

(Making denominator equal)

$\therefore$  New profit & loss ratio

$$= \frac{20}{30} \times \frac{4}{30} = \frac{6}{30}$$

$$=20:4:6 \text{ i.e. } 10: 2:3$$

Sacrifice ratio = old ratio - New ratio

Anika's Sacrifice ratio =

$$= \frac{5}{6} - \frac{20}{30} = \frac{25 - 20}{30} = \frac{5}{30}$$

Radhika's Sacrifice ratio =

$$= \frac{1}{6} - \frac{4}{30} = \frac{5 - 4}{30} = \frac{1}{30}$$

$\therefore$  Sacrifice ratio

$$= \frac{5}{30} \times \frac{1}{30} = 5:1$$

**3. Pramod and Vinod are partners sharing profits and losses in the ratio 3:2. After admission of Ramesh the new ratio of Pramod, Vinod and Ramesh is 4:3:2. Find out the sacrifice ratio.**

**Solution:** Sacrifice ratio = old ratio – New ratio

Pramod's Sacrifice ratio

$$= \frac{3}{5} \times \frac{4}{9} = \frac{27 - 20}{45} = \frac{7}{45}$$

Vinod's Sacrifice ratio

$$= \frac{2}{5} \times \frac{3}{9} = \frac{18 - 15}{45} = \frac{3}{45}$$

∴ Sacrifice ratio

$$= \frac{7}{45} \times \frac{3}{45} = 7:3$$

**(F) (1) Answer in one sentence only:**

**(1) What is Revaluation Account ?**

**Ans.** An account opened and operated by any partnership firm for recording changes in the value of assets and liabilities and to ascertain profit or loss made on revaluation of assets and liabilities is called Revaluation Account.

**(2) What is meant by Reconstitution of Partnership?**

**Ans.** Reconstitution of partnership means change in the relationship between /among partners and in the form of partnership.

**(3) Why is new partner admitted?**

**Ans.** A new partner is admitted to the existing partnership firm to increase the capital resources of the firm and to secure advantages of a new entrant's skill and business connections, i.e. goodwill.

**(4) What is sacrifice ratio?**

**Ans.** A ratio which is surrendered or given up by the old partners in favour of a newly admitted partner Is called sacrifice ratio.

**(5) What do you mean by raising the goodwill at the time of admission of a new partner?**

**Ans.** Raising the Goodwill at the time of admission of a new partner means debiting Goodwill Account upto the value it is raised and crediting Old partners' Capital Accounts in their old ratio in the books of the firm.

**(6) What is super profit method of calculation of goodwill?**

**Ans.** Super profit method of calculation of Goodwill is a method in which Goodwill is valued at certain number of years purchases of the super profit of the partnership firm. Ans. The ratio of sacrifice is calculated when the benefits of goodwill contributed by a new partner in

**(7) When is the ratio of sacrifice calculated for distribution of goodwill?**

**Ans:** The ratio of sacrifice is calculated when the benefits of goodwill contributed by a new partner in cash is to be transferred to existing partners' Capital / Current Account.

**(8) What is the treatment of accumulated profits at the time of admission of a partner?**

**Ans.** Accumulated profits at the time of admission of a partner are transferred to old partners' Capital/Current Accounts in their old profit sharing ratio.

**(9) State the ratio in which old partner's Capital A/C will be credited for goodwill when the new partner does not bring his share of goodwill in cash.**

**Ans.** When the new partner does not bring his share of goodwill in cash, Goodwill is raised upto certain value and credited to old partners' Capital/Current A/cs in their old profit sharing ratio.

**(10) What does the excess of debit over credits in Profit and Loss Adjustment Account indicate?**

**Ans.** The excess of debit over credits in Profit and Loss Adjustment Account indicates loss on revaluation of assets and liabilities.