

Accounting for Partnership Firm

Introduction to Partnership Accounting:

A sole trading concern often faces limitations due to the involvement of just one person in managing and operating the business. This includes limited capital, skill, and risk-taking capacity. To overcome these limitations, multiple individuals may come together to form a partnership, where they pool their resources, share risks, and jointly manage the business.

Partnerships are based on mutual trust and collaboration. Given this, it is crucial that partnership accounts are maintained honestly, accurately, and equitably to ensure transparency among partners. Proper maintenance of partnership accounts is essential to reflect a true and fair view of the partnership's financial position.

Characteristics of a Partnership:

1. Two or More Persons:

○ A partnership requires at least two people. While the Indian Partnership Act does not specify the maximum number of partners, the Companies Act, 2013, restricts the number of partners to 100.

2. Agreement:

○ A partnership is formed through an agreement, which can be either oral or written. This agreement is the foundation of the partnership. Unlike a Hindu Undivided Family (HUF), which is formed by law, a partnership is established through a mutual agreement.

3. Existence of Business and Profit Motive:

○ A partnership must be formed with the intention of conducting a legal business with the goal of earning profits. The mere joint ownership of property does not constitute a partnership unless it is associated with a business conducted for profit.

4. Sharing of Profits:

○ The agreement between partners must specify the sharing of profits from the business. A partnership exists only if there is an intention to share profits. If the activity is charitable and not profit-oriented, it does not constitute a partnership. Additionally, if a partner is excluded from sharing the profits, they are not considered a partner. It is important to note that while sharing profits is essential, sharing losses is not mandatory for all partners.

5. Relationship of Principal and Agent:

○ In a partnership, each partner acts both as a principal and an agent. As an agent, a partner can bind the other partners through their actions. As a principal, a partner is bound by the actions of other partners in relation to the business.

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Assignment

Ques 1: X and Y are partners in a firm sharing profits in the ratio of 3:2. The firm made a profit of ₹50,000. Calculate each partner's share of the profit. [Hint: Share of X = Rs 30,000 and Share of Y = Rs 20,000]

Ques 2: A and B are partners with capitals of ₹1,00,000 and ₹80,000, respectively. They have agreed to allow interest on capital at 10% per annum. Calculate the interest on capital for each partner at the end of the year. [Hint: Interest on Capital of A = Rs 10,000 and Interest on Capital of B = Rs 8,000]

Ques 3: A and B are partners sharing profits in the ratio of 4:3. They admit C as a new partner, and the new profit-sharing ratio is agreed upon as 3:2:1. If the total profit of the firm is ₹60,000, calculate the share of each partner. [Hint: Share of A = Rs 30,000, Share of B = Rs 20,000 and Share of C = Rs 10,000]

Ques 4: P, Q, and R are partners sharing profits and losses in the ratio of 5:3:2. The firm incurs a loss of ₹40,000. How much loss will each partner bear? [Hint: Share of loss of P = Rs 20,000, Share of loss of Q = Rs 12,000 and Share of loss of R = Rs 8,000]

Ques 5: X and Y are partners with initial capitals of ₹1,20,000 and ₹80,000, respectively. During the year, X withdraws ₹20,000 and Y withdraws ₹10,000 for personal use. If the partnership agreement does not allow for interest on withdrawals, what will be the adjusted capital for each partner at the end of the year? [Hint: Adjusted Capital of X = Rs 1,00,000 and Adjusted Capital of Y = Rs 70,000]

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