

Chapter 1: Introduction to Partnership

Question: 1

Answer in one sentence only.
What is Partnership?

Solution

A partnership is an agreement between two or more persons to share profits and losses of the firm. According to Section 4 of the Indian Partnership Act, 1932, "Partnership is the relation between persons who have agreed to share profits of a business carried on by all or any one of them acting for all.

Question: 2

Which act is applicable to partnership business?

Solution

Indian Partnership Act, 1932 is applicable to partnership firms.

Question: 3

Answer in one sentence only.
What is partnership deed?

Solution

An agreement that contains the details of every aspect and terms that the partners agree upon before starting a partnership firm is termed as partnership deed.

Question: 4

Answer in one sentence only.
How many persons are required to form partnership business?

Solution

At least two persons are required to form a partnership business. However, according to the Companies Act, 1956, a firm cannot have more than 10 partners in case of banking business and not more than 20 persons in case of any other business.

Question: 5

Answer in one sentence only.
Who is called a nominal partner?

Solution

A nominal partner is a partner who is paid a certain amount of fee for lending his name to the firm, which is important for building recognition of the firm. He's also called a limited partner, as he neither invests in the business nor actively participates in its affairs.

Question: 6

Answer in one sentence only.
Why is a partnership deed prepared?

Solution

A partnership deed defines the relationship among the partners. So, it acts as evidence in case of disputes among the partners of a firm. Therefore, it is advised to prepare a partnership deed.

Question: 7

Answer in one sentence only.
What do you mean by Fixed Capital Method?

Solution

When capital accounts of the partners are maintained under fixed capital method, then the capital of the partners remains unchanged or unaltered. It alters only in case of permanent change in capital (i.e. additional capital introduced or withdrawal of capital). In this method, two accounts, namely, Capital Account and Current Account are prepared.

Question: 8

Answer in one sentence only.
What is Fluctuating Capital Method?

Solution

Under fluctuating capital method, the capital of the partners does not remain fixed but changes with each and every transaction. In this method, only one account i.e. Capital Account is maintained for each partner.

Question: 9

Answer in one sentence only.
When is partner's current account opened?

Solution

A Current Account is opened when the capital of the partners is to be kept unaltered. In such cases, all transactions relating to (except introduction and withdrawal of capital) interest on capital, interest on drawings, salary to partners, etc. are recorded in this account itself.

Question: 10

Answer in one sentence only.
Who is called a Minor Partner?

Solution

A person who is under the age of 18 is regarded as a minor. Generally, a minor cannot be appointed as a partner. But with the consent of all the partners, a minor may be admitted for sharing profits of the firm. Such a partner, if admitted, is called a minor partner.

Question: 11

Answer in one sentence only.
What are the methods of maintaining partners' capital accounts?

Solution

There are two methods of maintaining partners' capital accounts:-

1. Fixed Capital Method
2. Fluctuating Capital Method

Question: 12

Answer in one sentence only.
What is the relation between the partners?

Solution

All the partners of a firm can jointly manage the business or any one of them can manage the business on behalf of the other partners. In other words, partners act as agent as well as principal.

Question: 13

Answer in one sentence only.
What is the liability of partners?

Solution

Generally, the liability of a partner is unlimited. But in case of Limited Liability Partnership, the liability of the partners is limited to the extent of their capital.

Question: 14

Give the word / term or phrase which can substitute the following statement.
Method of Capital account in which capital balances of partners changes every year?

Solution

Fluctuating Capital Method

Explanation: In this method, the capital balances of partners change every year. This is because under fluctuating capital method, only one account, i.e. Capital Account, is opened and every transaction is recorded in it.

Question: 15

Give the word / term or phrase which can substitute the following statement.
A partnership agreement between the partners in written form.

Solution

Partnership Deed

Explanation: An agreement between partners in written form, which contains the terms and conditions of the partnership agreement, is called partnership deed.

Question: 16

Give the word / term or phrase which can substitute the following statement.
A partner who provides only his name to the partnership firm.

Solution

Nominal partner

Explanation: A nominal partner is a person who provides only his name to the firm which is very important for the reputation and credibility of the firm.

Question: 17

Give the word / term or phrase which can substitute the following statement.
A partner who is engaged in day to day activities of the business.

Solution

Active partner

Explanation: A partner who is engaged in day to day activities of the business is regarded as an active partner. He works on behalf of all other partners of the firm and is also paid a salary, if mentioned in the deed.

Question: 18

Give the word / term or phrase which can substitute the following statement.
An amount contributed by the partners into the business.

Solution

Partner's Capital

Explanation: Partner's Capital is the amount which is brought in by the partners into the business for smooth functioning of their firm.

Question: 19

Give the word / term or phrase which can substitute the following statement.

An association of two or more persons to carry on business.

Solution

Partnership

Explanation: A Partnership is an association of two or more persons who have agreed to carry on a lawful business and share profits or losses in the agreed ratio.

Question: 19

Give the word / term or phrase which can substitute the following statement.

A partner who contributes only capital for the business but does not take any active part.

Solution

Sleeping partner

Explanation: A partner who contributes only capital for the business and does not take any active part in the day to day functioning of the business is regarded as a sleeping partner.

Question: 20

Give the word / term or phrase which can substitute the following statement.

A partner below the age of 18 years.

Solution

Minor partner

Explanation: A partner below the age of 18 years is known as a minor partner. He can be admitted to the benefits of the partnership firm only with the consent of all the partners.

Question: 21

Give the word / term or phrase which can substitute the following statement.

To close the business of partnership firm.

Solution

Dissolution of the firm

Explanation: Closure of partnership is termed as dissolution of the firm. A firm is closed with the consent of all the partners which terminates the firm's business.

Question: 22

Give the word / term or phrase which can substitute the following statement.

Capital method in which partner's current account is opened.

Solution

Fixed Capital Method

Explanation: Under Fixed Capital Account Method, a partner's Current Account is opened. In this method, the capital of the partners remains unaltered and all other transactions relating to interest on drawings, salary, etc. are recorded in the Current Account.

Question: 23

Give the word / term or phrase which can substitute the following statement.

An amount withdrawn by partner from business for his personal use.

Solution

Drawings

Explanation: Drawings refer to the amounts which are withdrawn (in cash or in kind) by the partners from the business for their personal use. It is recorded in the Current Account in case of Fixed Capital Method and in the Capital Account in case Fluctuating Capital Method is used.

Question: 23

Give the word / term or phrase which can substitute the following statement.

The partner who is entitled to share profits only.

Solution

Partner in profits only

Explanation: A partner who has the right to share the profits of the partnership firm without being liable to bear losses is regarded as a partner in profits only. Such a partner also does not take part in the management of the business.

Question: 24

Give the word / term or phrase which can substitute the following statement.

A partner who acts and behaves like a partner, but he is not a partner of the firm.

Solution

Partner by Estoppel or Holding out

Explanation: A partner who is actually not a partner of the firm but represents to the outside world that he is a partner in the firm is regarded as a partner by estoppel or holding out. Also, such persons are liable to outsiders as partners because on the faith of their representation, outsiders have granted credit to the firm.

Question: 25

Give the word / term or phrase which can substitute the following statement.
Under this method capital balances of partner remain constant.

Solution

Fixed Capital Method

Explanation: Under Fixed Capital Account Method, capital balances of partners remain constant. In this method, a separate account known as Current Account is opened and all transactions related to interest on capital, drawings, remuneration of partners etc are recorded in it.

Question: 26

Select the most appropriate alternative from those given below and rewrite the statement.

A debit balance of partner's current account will appear on the _____ side of the Balance Sheet.

Options

- asset
- liability
- debit
- Credit

Solution

A debit balance of partner's current account will appear on the **asset** side of the Balance Sheet.

Explanation: A debit balance in the Partners' Current Account represents that the partner has withdrawn more than his or her actual share of profits from the firm. Thus, this debit balance is the firm's asset and the firm has the right to recover this from the partner.

Question: 27

Select the most appropriate alternative from those given below and rewrite the statement.

The Indian Partnership Act is in force since _____

Options

- 1932
- 1956
- 1960
- 1984

Solution

The Indian Partnership Act is in force since **1932**.

Explanation: The Indian Partnership Act came into force on 1st October, 1932 which extends to the whole of India except the state of Jammu and Kashmir.

Question: 28

Select the most appropriate alternative from those given below and rewrite the statement.

A partner who provides only capital to the firm is called as _____.

Options

- active
- nominal
- sleeping
- minor

Solution

A partner who provides only capital to the firm is called as **sleeping partner**.

Explanation: A partner who just provides capital to the firm and does not take active part in day-to-day functioning of the business is a sleeping partner. But he is liable to the third parties for the dues of the firm.

Question: 29

Select the most appropriate alternative from those given below and rewrite the statement.

Under fixed capital method, capital account and _____ account is opened for each partner.

Options

- partner's drawings
- partner's salary
- partner's current
- partner's commission

Solution

Under fixed capital method, capital account and **partner's current** account are opened for each partner.

Explanation: Partner's Current Account is opened for each partner under fixed capital method because under this method, capital of the partners remains fixed, i.e. unaltered. All other transactions, except introduction and withdrawal of capital, such as those relating to interest on drawings and capital, partners' salary, share of profit etc, are recorded in the Partners' Current Accounts.

Question: 30

Select the most appropriate alternative from those given below and rewrite the statement.

The interest on capital of a partner is credited to _____ account.

Options

- trading
- Profit and loss
- partner's capital
- cash

Solution

The interest on capital of a partner is credited to **partner's capital** account.

Explanation: Interest on capital is an income for a partner. It is a kind of revenue that partners earn on the capital contributed by them in the partnership business. It leads to an increase in capital; so it is credited to Partners' Capital Account.

Question: 31

Select the most appropriate alternative from those given below and rewrite the statement.

Under fixed capital method, salary or commission to partner is credited to _____ account.

Options

- partner's capital
- partner's current
- partner's drawings
- partner's salary

Solution

Under fixed capital method, salary or commission to partner is credited to **partner's current** account.

Explanation: Under fixed capital method, any transaction that leads to a change in the capital balance of the partners is recorded in the Partners' Current Account. This is done so that the capital of the partners remains

unaltered. Accordingly, salary or commission to a partner is credited to the respective Partner's Current Account.

Question: 32

Select the most appropriate alternative from those given below and rewrite the statement.

A partner below 18 years of age is called as _____ partner.

Options

- active
- sleeping
- nominal
- minor

Solution

A partner below 18 years of age is called as **minor** partner.

Explanation: A minor partner is one who is below the age of 18 years. A minor can be admitted to partnership only with the consent of all the partners. Moreover, such partners are only entitled to profits and are not liable to bear the share in losses of the firm.

Question: 33

Select the most appropriate alternative from those given below and rewrite the statement.

A partner who lends only his name to the firm is called as _____ partner.

Options

- partner in profits only
- partner by estoppel
- nominal
- minor.

Solution

A partner who lends only his name to the firm is called as **nominal** partner.

Explanation: A partner who merely lends his name to the firm is regarded as a nominal partner. He neither invests in the business nor takes active part in it. But he is important for building up a good reputation for the firm.

Question: 34

Select the most appropriate alternative from those given below and rewrite the statement.

The interest on drawings is transferred to _____ side of partner's current account.

Options

- debit
- credit
- asset
- liability

Solution

The interest on drawings is transferred to **debit** side of partner's current account.

Explanation: Interest on drawings is an expense for a partner. It is the charge/fee that a partner needs to pay to the firm in lieu of the amount withdrawn by him/her for personal use. It leads to a decline in the capital balance of the partner. Thus, it is transferred to the debit side of Partner's Current Account.

Question: 35

Select the most appropriate alternative from those given below and rewrite the statement.

The liability of the partner in a firm is_____.

Options

- zero
- limited
- unlimited
- proportionate

Solution

The liability of the partner in a firm is **unlimited**.

Explanation: Partners in a firm have unlimited liability. From legal viewpoint, a partnership is not considered as a separate legal entity from its partners. So, all partners are personally liable to the outsiders for the acts of the firm.

Question: 36

Select the most appropriate alternative from those given below and rewrite the statement.

Partnership is an association of _____ or more persons.

Options

- two
- seven
- ten
- twenty

Solution

Partnership is an association of **two** or more persons.

Explanation: A partnership is an association of two or more persons as only one person cannot start a partnership firm. In fact, a single person in business is considered a sole proprietor. So, at least two persons are required to start a partnership firm.

Question: 37

Select the most appropriate alternative from those given below and rewrite the statement.

The drawings of partners are transferred to _____ account.

Options

- trading
- profit and loss
- partner's capital
- balance sheet

Solution

The drawings of partners are transferred to **partner's capital** account.

Explanation: Drawings are the amount withdrawn by the partners from the business for their personal use. Such withdrawals from the business cause a decline in partners' capital. Therefore, these are recorded on the debit side of Partner's Capital Account.

Question: 38

Select the most appropriate alternative from those given below and rewrite the statement.

If dates of drawings are not given, interest on drawings is charged for _____ months.

Options

- three
- six
- nine
- twelve

Solution

If dates of drawings are not given, interest on drawings is charged for **six** months.

Explanation: When the date of drawings is not given, interest on drawings is charged for an average period of six months. In such cases, it is assumed that a fixed amount is withdrawn as drawings in the middle of every month.

Question: 39

Select the most appropriate alternative from those given below and rewrite the statement.

Maximum _____ persons are required to form a partnership having trading business.

Options

- twenty
- fifty
- seven
- ten

Solution

Maximum **twenty** persons are required to form a partnership having trading business.

Explanation: As per the Companies Act of 1956, a maximum of twenty persons can form a partnership having trading business. The Act also prohibits a firm with more than 10 partners in case of banking business.

Question: 40

Select the most appropriate alternative from those given below and rewrite the statement.

Maximum _____ persons are required to form a partnership having Banking business.

Options

- two
- seven
- ten
- twenty

Solution

Maximum **ten** persons are required to form a partnership having Banking business.

Explanation: According to the Companies Act, 1956, a maximum of ten persons can form a partnership having Banking business.

Question: 41

State whether the following statement are True or False.

Partnership agreement must be in written form.

Options

- True
- False

Solution

False.

Explanation: According to the Indian Partnership Act, 1932, it is necessary to have an agreement between the partners but it is not compulsory to have it in

written form. An oral agreement is also valid although it is not advisable. Hence, the above statement is incorrect.

Question: 42

State whether the following statement are True or False.

Partnership firm is a trading concern.

Options

- True
- False

Solution

True.

Explanation: A partnership firm can be started as a trading concern which is involved in buying and selling of goods and services with a maximum limit of 10 partners. Hence, the above statement is true.

Question: 43

State whether the following statement are True or False.

Partners must share profits and losses equally.

Options

- True
- False

Solution

False.

Explanation: It is not mandatory for the partners to share profits and losses equally amongst themselves. They can share the benefits in any ratio as decided. The profits or losses will be distributed equally only when they agree or when the partnership deed is silent in this respect. Hence, the given statement is false.

Question: 44

State whether the following statement are True or False.

The interest on drawings is an income of the partnership firm.

Options

- True
- False

Solution

True .

Explanation: Interest on drawings is a kind of fee charged from the partner on the amount withdrawn by him/her from the firm's money for his/her personal use. So, it is an expense for the partner and accordingly, an income for the firm. Hence, the given statement is correct.

Question: 45

State whether the following statement are True or False.

Partner's current account is opened when fluctuating capital method is adopted.

Options

- True
- False

Solution

False.

Explanation: Partner's Current Account is opened when capital accounts are maintained under fixed capital method. This is because in this method, the capital of the partners remains unaltered. A separate account called current account is opened to record all other transactions (except introduction or withdrawal of capital), such as those relating to salary, commission, interest on capital, etc. Hence, the above statement is incorrect.

Question: 46

State whether the following statement are True or False.

A partner who provides only capital to the firm is called as nominal partner.

Options

- True
- False

Solution

False.

Explanation: A partner who only provides capital to the firm is known as a sleeping partner. On the other hand, a nominal partner is one who merely renders his/her name to the firm. Hence, the above given statement is false.

Question: 47

State whether the following statement are True or False.

An interest on capital is an expenditure of the partnership firm.

Options

- True
- False

Solution

True.

Explanation: Money invested by the partners in a business is regarded as partners' capital. Any interest paid on such capital will be an income for the partners and an expense for the firm. Hence, the above statement is true.

Question: 48

State whether the following statement are True or False.

There is no limit to maximum number of partners in a firm.

Options

- True
- False

Solution

False.

Explanation: The Companies Act of 1956 specifies the maximum limit of partners in a firm as 10 in case of banking business and 20 in case of any other business. Hence, the given statement is false.

Question: 48

State whether the following statement are True or False.

The balance of capital account remains constant under fixed capital method.

Options

- True
- False

Solution

True.

Explanation: Under fixed capital method, all transactions other than introduction of fresh capital or withdrawal of capital are recorded in Partners' Current Accounts. This is done so that the balance of Partners' Capital Accounts remains intact. Hence, the given statement is correct.

Question: 49

State whether the following statement are True or False.

If the partnership deed is silent, partners share profits and losses equally.

Options

- True
- False

Solution

True.

Explanation: Generally, partners can share profits and losses in any ratio as mentioned in the deed. But if the deed is silent, then according to the provisions of Indian Partnership Act, 1932, the profits and losses must be shared equally among the partners. Hence, the above statement is true.

Question: 50

State whether the following statement are True or False.

Partnership is an association of two or more persons.

Options

- True
- False

Solution

True.

Explanation: According to the Indian Partnership Act of 1932, partnership is defined as "the relation between two or more persons who have agreed to share the profits of a business carried on by all or any of them acting for all." This definition clearly implies that at least two persons are required to start a partnership firm. Hence, the above statement is true.

Question: 51

State whether the following statement are True or False.

Partners' current account always shows credit balance.

Options

- True
- False

Solution

False.

Explanation: It is not mandatory that the current account of a partner will always show a credit balance. It might show a debit balance when the partner has withdrawn more than his or her share of profits from the firm. Hence, the given statement is incorrect.

Question: 52

State whether the following statement are True or False.

The liability of minor partner is limited.

Options

- True
- False

Solution

True.

Explanation: With the consent of all the partners, a minor can be admitted to the benefits of partnership. That is, he can be admitted as a partner but only for sharing profits of the firm. His liability is limited to the extent of capital contributed by him. Hence, the above statement is true.

Question: 53

State whether the following statement are True or False.

Capital account always shows credit balance.

Options

- True
- False

Solution

False.

Explanation: It is not necessary that a partner's capital account will always show a positive balance (i.e. credit balance). The capital account of a partner might show a debit balance when a partner withdraws more than his or her share of profits from the firm. Hence, the given statement is incorrect.

Question: 54

State whether the following statement are True or False.

Partners are entitled to get salary or commission.

Options

- True
- False

Solution

False.

Explanation: A partner may be entitled to receive salary or commission if mentioned in the partnership deed. However, if the partnership deed is silent in this regard, then, remuneration is not provided to any of the partners. Hence, the above statement is false.