Student 1: Low Excellence

NZQA Intended for teacher use only

The following aspects of evidence have been omitted from this exemplar:

- *formation entries for both partners* 1
- *profit distribution statement*
- *capital account for Sam*
- *capital and current accounts for Alex*

Current: Sam					
Date		Dr	Cr	Bal	Dr/Cr
1/1/14	Balance			9,000	Dr
31/12/14	Salary		8,000	1,000	Dr
	Interest on capital		4,000	3,000	Cr
	Interest on drawings	1800		1200	Cr
	Interest on current	360		840	Cr
	Profit distribution		36,360	37,200	Cr
	Drawings	3,800		33,400	Cr

Mighty Mini Golf Statement of Financial Position (extract) as at 31 December 2014		
Equity	4	
Capital contribution		

Notes to the Statement of Financial Position

4 Equity

	Capital	Current	Total
Alex	50,000	15,300	65,300	2
Sam	90,000	33,400	123,400
	$140,000	$48,700	$188,700

Goodwill represents the future economic benefits from those assets with no physical presence, e.g. customer base, location and quality of service. The goodwill from Sam's existing business will be immediately profitable for Mighty Mini Golf as the existing customers are likely to support the new entity, bringing in sales revenue from the start. 3

In the absence of a partnership agreement, profits would be equally distributed between Sam and Alex in accordance with the Partnership Act 1908. This Act does not allow any other profit distributions like interest on capital, interest on drawings and interest on current accounts. The 3:2 profit share ratio in their partnership agreement is fairer than sharing profits equally.

Mighty Mini Golf needs to keep sufficient money in its bank account to be able to pay expenses and debts as they fall due. If partners' drawings are really high the bank balance might fall so low that an overdraft has to be taken out. The interest on the overdraft would decrease MMG's profit. So that this doesn't happen, Sam and Alex are charged 10% interest on drawings over $20,000 to discourage them from taking out excessive drawings. 3

Sam and Alex earn 5% per annum on the balance of their capital accounts. This encourages them to keep lump sum investments in the partnership which is good for the business. It is also good for the partners as they are getting rewarded with an interest rate that is about the same as they would earn from a bank.

Sam and Alex earn 4% interest on credit current account balances, to encourage them to keep their funds in the business. If they have negative (debit) current account balances they are charged 4% interest as negative balances usually mean they have taken more drawings than they have earned in profit share. Cash drawings would decrease the bank balance which can affect the ability to pay expenses and could jeopardise the ongoing viability of the partnership. 4