

GOODWILL

- Q.1.** Negotiation is going on for transfer of X Ltd. on the basis of the Balance sheet and the additional information as given below :

Balance Sheet of X Ltd. as on 31st March, 1988

Liabilities	Rs.	Assets	Rs.
Share Capital (Rs.10 fully paid-up shares)	10,00,000	Goodwill	1,00,000
Reserve and Surplus	4,00,000	Land and Building	3,00,000
Sundry Creditors	3,00,000	Plant and Machinery	8,00,000
		Investments	1,00,000
		Stock	2,00,000
		Debtors	1,50,000
		Cash and Bank	50,000
	17,00,000		17,00,000

Profit before tax for 1987-88 amounted to Rs.6,00,000 including Rs.10,000 as interest on investment. However, an additional amount of Rs.50,000 p.a. shall be required to be spent for smooth running of the business.

Market values of Land and Buildings and Plant and Machinery are estimated at Rs.9,00,000 and Rs.10,00,000 respectively. In order to match the above figures further depreciation to the extent of Rs.40,000 should be taken into consideration. Income tax rate may be taken at 50%. Return on capital at the rate of 20% before tax be considered normal for this business at the present stage.

For the purpose of determining the rate of return, profit for this year after the aforesaid adjustments may be taken as expected average profit. Similarly, average trading capital employed is also to be considered on the basis of the position in this year. It has been agreed that four years' purchase of super profit shall be taken as the value of goodwill for the purpose of the deal. You are required to calculate the value of goodwill of the company.

- Q.2.** The net profit of a company after providing for taxation for the past five years are :

Rs.40,000; Rs.50,000; Rs.30,000; Rs.70,000 and Rs.80,000.

The net tangible assets in the business is Rs.4,00,000 on which the normal rate of return is expected to be 10%. It is also expected that the company will be able to maintain its super profits for next five years.

Calculate the value of goodwill of the business on the basis of an annuity of super profits, taking the present value of an annuity of one rupee for five years at 10% interest is Rs.3.78.