OPEN STUDENT FOUNDATION

Date : 20-02-2024 **STD 12 Commerce Elements of Account** **Total Marks : 30**

12th Account Practice Sheet Day 3 (Part 1 - Ch.3)

Section A

*** Choose The Right Answer From The Given Options.** **[5]**

1. When profit amount of the last years constantly increases, which methods of valuation of goodwill is to be adopted?

(A) Simple average profit method (B) Weighted average profit method (C) Capitalization of average profit method (D) None of the given

Ans. : (B) Weighted average profit method

2. Value of goodwill is .... for business which depends on skill and proficiency of an individual.

(A) Less (B) More (C) Negative (D) Zero

Ans. : (A) Less

3. What is the formula for super profit?

(A) Average profit Expected profit (B) Expected profit Average profit (C) Average profit + Expected profit (D) Average profit + Expected profit

Ans. : (A) Average profit Expected profit

4. Super profit means.......

(A) Capital employed Expected profit

(B) Expected profit Capital employed

(C) Average profit Expected profit

(D) Expected profit Average profit

Ans. : (C) Average profit Expected profit

5. Following factors are affecting the valuation of goodwill except-

(A) Business location (B) Nature of business (C) Competitiveness of business (D) Customer's frequency

Ans. : (D) Customer's frequency

Section B

*** Answer The Following Questions In One Sentence.** **[5]**

6. Which type of asset is goodwill?

Ans. : Goodwill is an intangible asset which cannot be seen but it has a value in the market.

7. Under which head goodwill is shown in the balance sheet?

Ans. : Goodwill is shown in the balance sheet on the assets Side under the head of non-current assets as intangible asset.

8. What is the base for the valuation of goodwill?

Ans. : Profit earning capacity of the business is the main base for the valuation of goodwill.

9. When valuation of goodwill Is necessary?

Ans. : In case of purchase or sales of the business or when status of the business changes, valuation of goodwill is necessary.

10. State the methods for the valuation of goodwill.

Ans. : Following are the methods for the valuation of goodwill:

(1) Simple average profit method;

(2) Weighted average profit method;

(3) Capitalization of average profit method;

(4) Super profit method

Section D

*** Answer The Following Questions With Necessary Calculations. [20]**

11. Rajesh and Harish are partners of a partnership firm. On the basis of their partnership firm's profit and other information, determine the value of goodwill on the basis of two years purchase of super profit. .

(1) Capital employed: Rs.8,00,000

(2) Expected rate of return: 12 %

(3) Previous year's profit:

Year	2014-15	2015-16	2016-17
Profit (Rs.)	1,20,000	90,000	1,50,000

Ans. :

Statement showing computation of Goodwill

Step No.	Particulars	Amount (Rs.)
(1)	Capital employed	8,00,000
(2)	Expected rate of return	12%
(3)	Expected profit = Capital employed x Expected rate of return = Rs.8,00,000 x 2% = Rs.96,000	96,000
(4)	**Average profit:**	

Year	**Profit (Rs.)**
2014-15	1,20,000
2015-16	90,000

Step No.	Particulars	Amount (Rs.)
	<table><tr><td>2016-17</td><td>1,50,000</td></tr><tr><td>**Total**</td><td>**7,00,00**</td></tr></table>	
	Average profit $= \frac{Total\ Profit}{No.\ of\ years}$ $= \frac{3{,}60{,}000}{3}$ = Rs.1,20,000	1,20,000
(5)	Super profit = Average profit - Expected profit = Rs.1,20,000 – Rs.96,000 = Rs.24,000	24,000
(6)	Goodwill = Super profit x No. of purchase = Rs.24,000 x 2 = Rs.48,000	**48,000**

12. Pushpa, Pratibha and Bhavna are partners of the partnership firm. They decided to change date profit-loss sharing ratio from 3:2:1 to 1:1:1. Therefore I decided to make the valuation of goodwill. On the basis of partnership firm's profit and other information, determine the value of goodwill on the basis of 3 year purchase of super profit.

Assets: Rs.6,00,000; liabilities: Rs.2,50,000; expected rate of return: 10%

Actual Profit:

Year	Profit(Rs.)
2014-15	80,000
2015-16	70,000
2016-17	90,000

Ans. :

Statement showing computation of Goodwill

Step No.	Particulars		Amount (Rs.)
(1)	Capital employed:		
	Total Assets	6,00,000	
	- Total Liabilities	2,50,000	3,50,000
(2)	Expected rate of return		10%
(3)	Expected profit=Capital employed X Expected rate of return = Rs. 3,50,000 X 10%		35,000
(4)	**Average profit:** <table><tr><td>**Year**</td><td>**Profit(Rs.)**</td></tr><tr><td>2014-15</td><td>80,000</td></tr><tr><td>2015-16</td><td>70,000</td></tr><tr><td>2016-17</td><td>90,000</td></tr><tr><td></td><td>**2,40,000**</td></tr></table>		

	Average profit = $\frac{Total\ profit}{No.of\ years}$ = $\frac{2,40,000}{3}$ = Rs. 80,000	80,000
(5)	Super profit = Average profit – Expected profit = Rs.80,000 - 35,000 = Rs.45,000	45,00080,00 0
(6)	Goodwill = Super profit X No. of purchase = Rs.45,000 X 3 = Rs.1,35,000	**1,35,000**

13. Explain the nature of the goodwill.

Ans. :

At the time of reconstructions of partnership firm business assets and liabilities are revaluated with this, the value of goodwill is also to be decided.

- (i) For business goodwill is an intangible assets included in the group of non-current assets.
- (ii) Intangible assets cannot be seen but it has its value in the market over a period of time, a well-established business develops an advantage of good name, reputation and wide business connections which benefits the business.
- Monetary value of such advantage is the main reason for the goodwill
- (iii) Goodwill does not exists in those business which earn normal profit or incur loss.

(iv) Goodwill is shown in the balance sheet on the assets side under the head of non-current assets as intangible asset.

14. Explain the simple average method for the valuation of goodwill.

Ans. :

In the simple average method for the valuation of goodwill the average profit of the past certain years are taken into consideration.

- Then, this average profit is to be multiplied by the certain number of years for the valuation of goodwill. Here it is assumed that a new business will take certain number of years to earn the same profit. Therefore, the business purchaser is ready to pay the value of goodwill equal to the number of years of average profit.
- Generally, the multiplication of average profit and the number of years during which the anticipated profit are expected is known as goodwill.

Average = $\frac{\text{Total Profit of given years}}{\text{Number of years}}$

Goodwill = Average profit x No. of years of purchase

15. Mahendra and Pravin are partners of a firm sharing profit and loss in the ratio of 3 : 2. They want to change their profit-loss sharing ratio to 1:1. Therefore, they decided to make valuation of goodwill. As per partnership agreement, value of goodwill to be determine on the basis of 5 years Purchase of last 4 years average profit.

Year	2013-14	2014-15	2015-16	2016-17
Profit (Rs.)	60,000	80,000	(20,000)	30,000

Ans. :

Statement showing computation of average profit:

Year	Profit (Rs.)
2013-14	60,000
2014-15	80,000
2015-16	(20,000)
2016-17	30,000
Total	1,50,000

Average profit $= \frac{Total\ profit}{No.\ of\ years}$

$= \frac{1,50,000}{4}$

= Rs.37,500

Goodwill = Average profit × No. of purchasing year

= Rs.37,500 X 5

= Rs.1,87,500

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