

Chapter 3- Goodwill- Nature and Valuation

Question 1

Define Goodwill.

Answer: Goodwill is an intangible asset which places an enterprise at an advantageous position due to which an enterprise is able to earn higher profits without putting extra effort.

Question 2

Give two features of goodwill.

Answer: The two features of goodwill are

- It is an intangible asset. It does not have any physical existence
- It helps in earning higher profits

Question 3

What is the need for valuation of goodwill?

Answer: The need for valuation of goodwill arises.

- When there is a change in the profit-sharing ratio
- When a new partner is admitted
- When a partner retires or dies
- When a partnership firm is sold as a going concern
- When two or more companies amalgamate
- When a partnership firm is converted into a company

Question 4

What are the methods to evaluate goodwill

Answer: The two methods of evaluating goodwill are.

- **Average Profit Method** – (a) Simple average profit method (b) Weighted average profit method
- **Super Profit Method**
- **Capitalization Method** – (a) Capitalisation of average profit method (b) Capitalization of super profit.

Question 5

What is purchased goodwill?

Answer: Purchased goodwill is that goodwill which is acquired by a firm for a consideration, whether paid in cash or kind.

Question 6

What is self-generated goodwill?

Answer: Self-generated goodwill is the goodwill which is not purchased for consideration but is earned by the efforts of the management or partners.

Question 7

What is a super profit method?

Answer: When a buyer's advantage lies in the excess of the normal return capital employed. The excess of actual/average profit over normal profit is known as super profit method.

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Question 9

What are the factors that affect the value of goodwill?

Answer: The factors that affect the value of goodwill are.

- Efficient Management
- Favorable Location
- Favorable Contracts
- Advantage of Patent
- Market Situation
- Nature of Business

Question 10

State two features of purchased goodwill.

Answer: The two features of purchased goodwill are.

- It arises on the purchase of a business

- It is shown in the Balance Sheet as an asset

Question 11

State two features of self-generated goodwill.

Answer: The two features of self-generated goodwill are.

- It is generated internally, generally over the years
- Its valuation is subjected assessment of the valuer, is not based on an evidence

Question 12

Give the formula for super profit method.

Answer: The formula for super profit method are

Super Profit= Average Profit – Normal Profit

Question 13

Give the formula for value for goodwill.

Answer: The formula for super profit method are

Goodwill = Weighted Average Profit x Number of years' purchase