

**Illustration 8** (Weighted Average Profit when Past Adjustments are Made). Akhil and Nikhil are partners sharing profits equally. They admitted Dinesh into partnership. It was agreed to value goodwill at three years' purchase following Weighted Average Profit Method on the basis of past five years' profits. Weights assigned to each year would be—years ended 31st March, 2013–1, 2014–2, 2015–3, 2016–4 and 2017–5. The profits for these years were—₹ 90,000, ₹ 80,000, ₹ 1,25,000, ₹ 1,50,000 and ₹ 1,75,000 respectively.

Scrutiny of books of account revealed the following:

1. There was an abnormal loss of ₹ 15,000 during the year ended 31st March, 2013.
2. There was an abnormal gain of ₹ 10,000 during the year ended 31st March, 2015.
3. Closing Stock as on 31st March, 2016 was overvalued by ₹ 15,000.

Calculate value of goodwill.

**Solution:**

1. CALCULATION OF NORMAL PROFITS			
Year Ended	Profit (₹)	Adjustment (₹)	Normal Profit (₹)
31st March, 2013	90,000	15,000	1,05,000
31st March, 2014	80,000	...	80,000
31st March, 2015	1,25,000	(10,000)	1,15,000
31st March, 2016	1,50,000	(15,000)*	1,35,000
31st March, 2017	1,75,000	15,000*	1,90,000

\*Closing Stock being overvalued on 31st March, 2016 means that profit for the year is shown at higher amount. It has effect on the profit for the next year. Profit for next year is shown at lower amount as Closing Stock of previous year is carried forward as Opening Stock of next year.

2. CALCULATION OF WEIGHTED AVERAGE PROFIT			
Year Ended	Profit (₹)	Weight	Product (₹)
31st March, 2013	1,05,000	1	1,05,000
31st March, 2014	80,000	2	1,60,000
31st March, 2015	1,15,000	3	3,45,000
31st March, 2016	1,35,000	4	5,40,000
31st March, 2017	1,90,000	5	9,50,000
		15	21,00,000

$$\text{Weighted Average Profit} = \frac{\text{Total of Profit Product}}{\text{Total of Weights}} = \frac{\text{₹ } 21,00,000}{15} = \text{₹ } 1,40,000.$$

Number of Years' Purchase = 3

$$\begin{aligned} \text{Value of Goodwill} &= \text{Weighted Average Profit} \times \text{Number of Years' Purchase} \\ &= \text{₹ } 1,40,000 \times 3 = \text{₹ } 4,20,000. \end{aligned}$$

- revenue. The said sum is to be capitalised & depreciation of 10% on Reducing Balance Method.
- (ii) The Closing Stock for the years 2006 and 2007 were overvalued by ₹ 1,000 and ₹ 2,000 respectively. Depreciation of 10% on Reducing Balance Method.
- (iii) To cover management cost an annual charge of ₹ 5,000 should be made for the purpose of goodwill valuation.
14. X and Y are partners sharing profits and losses in the ratio of 3 : 2. They admit Z into partnership for 1/4th share in goodwill. Z brings in his share of goodwill in cash. Goodwill for this purpose shall be calculated at two years' purchase of the weighted average normal profit of past three years. Weights being assigned to each year 2013-1; 2014-2 and 2015-3. Profits of the last three years were:
- 2013—Profit ₹ 50,000 (including profits on sale of assets ₹ 5,000).  
 2014—Loss ₹ 20,000 (including loss by fire ₹ 35,000).  
 2015—Profit ₹ 70,000 (including insurance claim received ₹ 18,000 and interest on investments and dividend received ₹ 8,000).

Calculate the value of goodwill. Also, calculate the goodwill brought in by Z.

15. Manbir and Nimrat are partners and they admit Anahat into partnership. It was agreed to value goodwill at three years' purchase on Weighted Average Profit Method taking profits of last five years. Weights assigned to each year as 1, 2, 3, 4 and 5 respectively to profits for the year ended 31st March, 2013 to 2017. The profits for these years were: ₹ 70,000, ₹ 1,40,000, ₹ 1,00,000, ₹ 1,60,000 and ₹ 1,65,000 respectively.

Scrutiny of books of account revealed following information:

- (i) There was an abnormal loss of ₹ 20,000 in the year ended 31st March, 2013.
  - (ii) There was an abnormal gain (profit) of ₹ 30,000 in the year ended 31st March, 2014.
  - (iii) Closing Stock as on 31st March, 2016 was overvalued by ₹ 10,000.
- Calculate the value of goodwill.