

GOODWILL AND ITS TREATMENT IN ACCOUNTS

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Goodwill and its treatment in accounts by Lawrence R. Dicksee & Frank Tillyard

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LAWRENCE R. DICKSEE & FRANK TILLYARD

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BY

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ERRATUM.

Pages 141 and 142 should appear after the Balance Sheet on page 133, thus making page 140 the last page of Chapter XII.

PREFACE TO THIRD EDITION.

THE First Edition of this work, which was published in 1897, was founded upon a lecture delivered by the author at a meeting of the Birmingham Chartered Accountant Students' Society in the autumn of the previous year. Numerous *pro forma* examples were, however, appended to still further explain the principles laid down in the body of the work, and a valuable "introductory chapter" on the law relating to Goodwill was supplied by the late Mr. T. M. Stevens, D.C.L., Barrister-at-Law.

The Second Edition, which was issued in 1900, was but little more than a reprint of the first, save that the leading decisions which had been given between 1897 and 1900 were duly noted. It is, however, of interest to note that in the meantime the idea which was, I believe, first enunciated in this work—namely, that interest on capital and the value of a proprietor's time while engaged in the management of a business were both factors to be taken into account before arriving at the marketable value of Goodwill—began to find acceptance, and had been specially referred to in a lecture delivered by the late Mr. Edwin Guthrie, F.C.A., at a meeting of the Chartered Accountant Students' Society of London in 1898. Even then, however, the principle that the Goodwill of a business acquired by a joint-stock company should be paid for out of premiums derived from the issue of its share capital had by no means been generally recognised and, so far as the author has been able to ascertain, "Answers," Lim., was the only new company

whose shares had been issued at a premium in order to enable this question of Goodwill to be dealt with upon a scientific basis.

During the last few years events have occurred which can hardly have failed to bring home to the minds of the thoughtful student the inherent soundness of the principles laid down by the author nearly ten years since. Whatever other causes may have been at work, it will probably now be very generally admitted that the effect of further issues of capital by an established company, either at par or at a premium less than the price commanded in the market by the existing shares, is to "water" the capital of the undertaking as a whole—and therefore to cause a fall in the market value of its shares. Without going into particulars, and without seeking to cast any reflection upon existing undertakings, it is thought that it must at the present time be admitted that the fall that has taken place in the shares of the British South Africa Co., of the Aerated Bread Company, Lim., and of most British Railways (all of which for a number of years past have been systematically issuing new capital *pro rata* to their existing shareholders at a price lower than the current market rate) has directly contributed towards reducing the market values of these several securities. A principle that holds good with regard to an established undertaking must, of course, be equally sound when applied to a new company taking over an established business; and for these reasons I see no ground for modifying the views which I expressed in the first edition of this work. At that time there was, it is true, a practical objection to the singling out of the item "Goodwill" for such special treatment, in that it drew prominent attention to the amount that it was proposed to pay for this somewhat elusive asset: but inasmuch as the provisions of the Companies Act, 1900*, now require the price to be paid for the "Goodwill" to be separately stated in every prospectus,

* Now incorporated in Section 81, Sub-section 1 (g), of the Companies (Consolidation) Act, 1908.

there can be no possible reason for persistence in old and unscientific methods, inasmuch as they have been at last (and very properly) shorn of all practical advantages.

In the present edition the legal introduction, which is comprised in the first seven chapters, has been entirely re-written by my colleague, Mr. Frank Tillyard, and greatly amplified. Indeed this portion of the subject has been so fully dealt with that I venture to think that the work is now entitled to take its place as a legal text-book. It should be added, however, that it has been written, not from the point of view of lawyers and law students, but of practical business men, and that nothing has been taken for granted with which it would be unreasonable to assume that they were acquainted. The remaining five chapters, enunciating general business principles and explaining their practical application, are elucidated with the aid of numerous *pro formâ* examples which, it is hoped, will be found intelligible even to those who are not skilled accountants. The full text of the Trade Marks Act, 1905, is appended, as that useful measure would appear to be far less known to business men than its importance renders desirable; while the second appendix, dealing with the more customary forms of clauses in deeds of partnership, &c., relating to the treatment of Goodwill, will, it is thought, be found suggestive, no less on account of what it may be found expedient to avoid in them, than by reason of the merits which they undoubtedly possess. The Index to Cases will be found of considerable value to students, and others, desirous of readily ascertaining the exact practical effect of such decisions as have been given from time to time; while the General Index, which concludes the volume, will doubtless render it more serviceable as a book of reference, both to the practising accountant and to the man of business.

LAWRENCE R. DICKSEE.

48 Cophall Avenue,

7th June 1906.