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## Correspondence: Valuation of Goodwill

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## Correspondence

### Valuation of Goodwill

Editor, *The Journal of Accountancy*:

SIR: In the October, 1921, issue of THE JOURNAL OF ACCOUNTANCY, the author of *Valuation of Goodwill* says on page 263:

"In valuing the goodwill of Tiffany & Co. the court approved a multiple of ten years' purchase (*Matter of Moore*, 97 New York, 238). This case was decided as recently as 1916 and represents probably the maximum valuation which has been approved by the courts."

The citation, 97 N. Y., 238, indicates a case in the 97th volume of the New York court of appeals reports, the present number of which is 234. If the citation is correct, it is obvious that the case is not so recent as 1916; if incorrect, readers interested in the legal opinion may experience some difficulty in finding it. As a matter of fact, the citation should have read 97 Miscellaneous (N. Y.), 238, a set of volumes containing reports of cases tried in courts of record of New York other than the court of appeals and the appellate division. The case in question was tried in the surrogate's court of New York county before Surrogate Fowler, who wrote at page 240:

"If six years' purchase of the average annual net profits was considered not an unreasonable value of the goodwill in a case where the question of goodwill related to the name under which a number of candy stores are conducted (*Von Au v. Magenheimer*, 126 A. D., 257), it would seem that the goodwill of a company having the prominence, the permanency and the established reputation of Tiffany & Co. should be worth at least ten years' purchase of the annual net profits."

Within the month Surrogate Schulz of Bronx county wrote an interesting opinion in regard to the estate of James A. Bolton, copy of which, clipped from the *New York Law Journal*, is enclosed.

In closing, I would call to your attention a comment made by Cuthbert W. Pound, judge of the court of appeals of New York, in an address which is printed in *Cornell Law Quarterly*, February, 1923:

"Instruction in business administration, corporate finance, accounting and kindred subjects is almost as essential in connection with a law-school course as are the moot trials and practice courts."

Yours very truly,

W. B. WIEGAND.

New York, June 19, 1923.

[ENCLOSURE]

SURROGATE'S COURT—(BRONX COUNTY)—CHAMBERS

By SCHULZ, S.

Estate of James A. Bolton—The executors of the decedent's last will appeal from the order fixing the amount of tax upon the transfer of his property pursuant to the terms thereof. They contend that the appraiser erroneously failed to deduct the value of the widow's dower before making such appraisal. The decedent made certain provisions for his wife, and with respect to them stated that they "are made and are to be accepted by her in lieu of dower in my estate." Upon the argument it was agreed that for the purpose of this appeal it might be assumed that the widow has accepted the provisions thus made instead of insisting upon her dower. The appraiser was correct in not making an allowance for the widow's dower

under these circumstances (*Matter of Gould*, 156 A. D., 423; *Matter of Reimann*, 42 Misc., 648; In re *Barbey's Estate*, 114 N. Y. S., 725; *Matter of Stuyvesant*, 72 Misc., 295; *Matter of Taylor*, N. Y. L. J., May 26, 1923). The second ground of appeal is that the appraiser's valuation of 200 shares of the stock of a corporation which had been owned by the decedent is excessive. The stock was not listed, no sales appear to have been made, and the appraiser in fixing its value attempted to follow the method now generally adopted and sanctioned by the authorities when dealing with stock of this kind. This consists of adding to the value of the net assets of the corporation the value of the goodwill of its business and dividing the result by the number of shares of stock into which the capital is divided (*Matter of Jones*, 172 N. Y., 575; *Matter of Rees*, 208 N. Y., 590, affirming order of surrogate without opinion). In arriving at the value of the assets he has added the sum of \$408,728.77 surplus. This amount, however, had already been included in the calculation of assets and hence has been appraised twice. In ascertaining the value of the goodwill the approved method is to obtain the average yearly net profit extending over a period of years after deducting interest at 6 per cent. on the amount of capital invested each year (*Matter of Seaich*, 170 A. D., 686, aff'd 219 N. Y., 634; *Matter of Ball*, 161 A. D., 79; *Matter of Silkman*, 121 A. D., 202, aff'd 190 N. Y., 560; *Von Au v. Magenheimer*, 115 A. D., 84, 126 A. D., 257, aff'd 196 N. Y., 510), and then to take a number of years' purchase of the balance. There is no hard and fast rule as to the number of years of which an average shall be obtained, nor as to the number of years' purchase that shall be taken (see cases cited in *Matter of McMullen*, 92 Misc., 637). In each instance the particular circumstances must be considered. In the present matter the appraiser has taken the average net profits for the years 1915 to 1921, inclusive, deducted 6 per cent. interest on what he claims is capital invested and taken a three-year purchase of the balance then remaining, and thus reached his valuation of the goodwill. During the years 1916 to 1919, inclusive, the profits of the corporation were extraordinarily large due to the world war. Thus the average profits for the five years 1910-1914, inclusive, were \$35,674.68, while the average profits for the next five years, 1915-1919, exclusive, were \$149,210.66. In the affidavit of the president of the corporation the reason for these large profits is stated, and his explanation is not in any way controverted or impeached. To base the appraisal of the goodwill upon an average for a period of seven years where four of the seven years have been so unprecedentedly profitable does not appear to me to result in a fair valuation, which is the end sought to be attained (*Matter of Ball*, supra). A more equitable result would be obtained if the profits for the years 1910 to 1921, inclusive, were taken as a basis for the average per annum profit and a three years' purchase of that result obtained, and the appraiser is directed to so proceed. It also appears that the appraiser has deducted interest on only two items of capital. Interest on the whole capital which is invested in each of the years of which the average is taken should be deducted from the profits of that year. The decedent in his will nominated two executors and gave a legacy to each, providing, however, that such legacies were in lieu of the commissions of such executors. It is correctly urged by the appellants that the appraiser erred in failing to allow any deduction for executors' commissions. The statute provides that "the excess in value of the property so bequeathed \* \* \* above the amount of commissions \* \* \* prescribed by law in similar cases shall be taxable," and allowance should therefore have been made (Tax L., 1909, chap. 62; Cons. L., chap. 60, sec. 226; *Matter of Silliman*, 79 A. D., 98, aff'd 175 N. Y., 513). I am also of the opinion that the appraiser should have deducted the widow's exemption of \$150, as contended for by the appellants, before fixing the value of the estate for purposes of taxation (*Matter of Libolt*, 102 A. D., 29). For the reasons stated the order is reversed and the matter remitted to the appraiser to proceed as indicated.