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The Journal for CMAs

The Institute of Cost Accountants of India ● www.icwai.org

Accounting for Intellectual Capital

Glimpses of Pakistan India Management Summit held at Lahore on 20-21 September 2012

Group photograph. Seen CMA H.K. Goel, Council Member along with the participants & officials of Indian Railways

1st Technical Training program for the IRAS Officers of Indian Railways in progress during 24th Sept - 8th Oct 2012 at Delhi, London, Paris. Shri P.V. Vaidialingam, ED (Accounts), Indian Railways addressing the participants. Also seen CMA Rakesh Singh, President of the Institute, CMA H.K. Goel, Council Member and CMA D. Chandru (Director), CEP

CMA Rakesh Singh, President of the Institute, CMA T.C.A. Srinivasa Prasad, Council Member, CMA P. Bhattacharya, RCM and other officials at the Regional Seminar on 'CAS' & 'CARR' on 22.09.12 at Jamshedpur

CMA Manas Kumar Thakur, Council Member seen with Shri Khegendra Jamatia, Hon'ble Minister of Co-operation Fisheries, Govt. of Tripura at the office of the Hon'ble Minister at Agartala on 5.10.12

Inauguration of Programme on "Filing of Cost Audit and Compliance Report in XBRL" at Bangalore on 16.10.12 by CMA T.C.A. Srinivasa Prasad, Council Member. Also seen CMA A. Om Prakash, Council Member (extreme left), CMA G.N. Venkataraman, past President (2nd from right) & other officials

Seminar on XBRL Taxonomy in progress at Guwahati held on 7.10.12. Seen (L to R) CMA Rana Bose, Chairman, GCCA, CMA T.C.A Srinivasa Prasad, Council Member and CMA S. K. Saha, Vice-Chairman, GCCA

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The Management Accountant

Official Organ of the Institute of Cost Accountants of India established in year 1944 (Founder member of IFAC, SAFA and CAPA)

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IDEALS THE INSTITUTE STANDS FOR

❏ to develop the Cost and Management Accountancy profession ❏ to develop the body of members and properly equip them for functions ❏ to ensure sound professional ethics ❏ to keep abreast of new developments.

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MISSION STATEMENT

"The Institute of Cost Accountants of India Professionals would ethically drive enterprises globally by creating value to stakeholders in the socio-economic context through competencies drawn from the integration of strategy, management and accounting."

VISION STATEMENT

"The Institute of Cost Accountants of India would be the preferred source of resources and professionals for the financial leadership of enterprises globally."

DISCLAIMER

The views expressed by the authors are personal and do not necessarily represent the views and should not be attributed to the Institute.

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Editorial

Seasons' Greetings!

The advent of the festive season has been the harbinger for a spate of significant economic events and some bold policy decisions by the Government - hike in diesel prices, imposition of subsidized LPG cap, clearing of FDI in multi-brand retail & aviation, PSU restructuring proposals, announcing an SEB (State Electricity Boards) restructuring plan, approval of Companies Bill 2011; all aimed at bolstering the flagging economy. With the government going full throttle on the 'big-bang' reforms, bulls are having a party on Dalal Street as the 30-stock BSE Sensex reclaimed the 19000 mark after a gap of 18 months even amidst general perception that it is a sentiment driven rally while fundamentally the situation remains the same.

Now, let us turn our attention to the theme topic, 'Accounting for Intellectual Capital'. As a measurement-communication devise of economic events, the history of Accounting can be traced to the beginning of the recorded history. The clay tables found in some of the most ancient civilizations of the world suggest that accounting was an integral part of all socio-economic activities in an organised society. However, accounting apart from being a record-keeping device of a simple society, is also a highly adaptive social technology, always responding to the needs of the contemporary society.

In the history of the evolution of Accounting, Industrial Revolution and the emergence of corporate form of organisations are considered to be the major milestones. Accounting, in keeping with its reputation of being a flexible technology, has responded to support the emerging system of trade and commerce. But now in the wake of a technological revolution, the hallmark of the present time, the system of accounting appears to be inadequate. This accounting system was meant for an economy with preponderance of physical assets like land, building and plant and machinery. But these assets now constitute only a fraction of the market value of the most successful companies. Our accounting system starkly fails to capture what is considered to be the prime movers of economic values: the knowledge capitals or the intellectual capitals of the organisations. In this age, widely hailed as the new economy, companies are spending phenomenal sums on assets that go unrecorded in the books of accounts. In consequence, accounting provides at best an incomplete picture, and at worst a misleading picture to the stakeholders. It is imperative that the contribution of human capital needs to recognized and accounted for, for better and correct interpretation of the financial results of the company.

In the past a number of research in India and abroad have shown that our present accounting system portrays only a fraction of what the market is willing to pay for the company. The hiatus between the market value and the book value is generally ascribed to the intellectual capital. The scholars in the field feel that the present system of accounting needs to be overhauled to accommodate those values in the books of account.

The present issue of the Management Accountant is themed upon such an important issue. I am sure that our contributors will keep an indelible mark of scholarship and originality while delving on this issue.

Happy reading!

> **Change should result in progress in life. The metamorphosis from a cocoon to a butterfly, from a bud to the bloom and the flower to fruit should be the end result of the change.**
>
> **—Anonymous**

CMA Rakesh Singh, President

Dear Professional Colleagues,

All of us recognize the necessity for change, which results in progress. It gives way to new ideas and perspectives reflecting the current and emerging environment, which builds on the solid foundations of the past.

The change of guard at the helm of the Ministry of Corporate Affairs may be perceived in the same light, as the young new incumbent builds on the thrust given in the past with a new perspective. I on behalf of the Institute, the Council, its members and students congratulate **Honourable Shri Sachin Pilot** on assuming charge of the Ministry of Corporate Affairs as the new Minister (IC). I hope that under the able guidance and dynamic leadership of the new Minister, the Ministry will achieve newer heights and at the same time I also assure and extend committed professional support to the activities of the MCA.

As the activities of the Institute are increasing day by day, the need of fresh and dynamic professionals is being felt. The Institute will very soon be bolstered by the services of young and vibrant professionals as a result of the recruitment drive. I am happy to share with you that the work of face lifting of the New Delhi office building has also been started after an auspicious Puja on 25th October 2012.

To apprise all the members of the activities / initiatives undertaken by the Departments/ Directorates of the Institute, I now present a brief summary of the activities.

Syllabus 2012

The Council of the Institute in its 277th Meeting held on 1st October, 2012 has approved the "Syllabus 2012" for introduction w.e.f. 1st December, 2012. Students admitted to the Courses of the Institute, w.e.f. 1st December, 2012 shall pursue Courses under "Syllabus 2012". The First Examination under "Syllabus 2012" shall be conducted in December 2013. The Last Examination under "Revised Syllabus 2008" shall be conducted in June 2015.

Professional Development Directorate

Certification of Documents under Handbook of Procedure and Appendices under Foreign Trade Policy

I am glad to inform the members that on incessant representations of the Institute, Ministry of Commerce and Industry, Department of Commerce vide its Public Notice No. 22 (RE-2012)/2009-14 dated 11th October, 2012 has authorized Cost Accountants for certification of various documents under Handbook of Procedure Vol. I and Appendices under Foreign Trade Policy 2009-14. Accordingly, the Cost Accountants in practice can now certify all Documents and Appendices under the EXIM Policy and Procedure. For full text of this Public Notice, readers may refer to Institute's website.

Quality of XBRL Filing

The Ministry of Corporate Affairs vide General Circular No. 33/2012 dated 16th October 2012 requested the members of the Institute to be more careful while filing the e-forms through XBRL mode with respect to their completeness and correctness. It mentioned number of cases where the proper and correct mapping / tagging is not done by the professionals while filing the financial statements with the Ministry. Few instances of "incorrect" tagging of XBRL documents have been provided in Annexure-I to this circular. The action of incorrect tagging shall be liable to be penalized. Therefore, the members are requested to improve the quality of XBRL filing for financial year 2011-12. Full text of this Circular can be seen at the Institute and MCA websites.

Hiring of professional Cost Accountants (CMAs) for Scrutiny & Review of Cost Audit Reports, Compliance Reports and Cost Data Analysis

It has been decided to use the services of experienced and willing Cost Accountants (CMAs) engaged in public practice, through the Institute, to assist the Ministry of Corporate Affairs in carrying out scrutiny and review of cost audit reports & compliance reports, data mining & analysis, sectoral analysis, etc. with a view to ensuring high quality of audit & assurance and to suggest industry specific input output norms, efficiency benchmarks, deficiencies, improvement areas, etc. The Institute will empanel practicing cost accountants in terms of the Scheme and empanelment criteria. The interested cost accountants who are in full time practice may send their application along with requisite fee to the Institute at its Delhi Office. Complete Scheme along with Eligibility Criteria has been hosted on the Institute website.

Hyderabad Center of Excellence (HCE)

On October 3, an Awareness Program on Filing of Cost Audit & Compliance Report in XBRL was conducted at HCE. Session on Practical aspects of cost taxonomy was conducted by CMA Kunal Banerjee past President, Shri Ankit Varshney, XBRL trainer, conducted the other sessions.

The Program on EPMAS (Enterprise Performance Management and Appraisal Systems) is running into the 12th week. The examination in Paper-II has since been conducted.

CMA M. Gopalakrishnan, the immediate past president, delivered a lecture on the 13th October to the students of EPMAS on key components of performance Appraisal report.

On October 21st, Durga Pooja was performed at the premises of HCE. The Director and CMA A.S. Durga Prasad, Council Member performed the pooja. The Pooja ceremony was attended by members of the Hyderabad Chapter.

Training Programs

The Institute has organized in-house programme for Central Warehousing Corporation Ltd. on Financial Accounting and Impact of IND AS during 26th-27th September 2012. The last Seminar in the series on the topic `Cost Accounting Records Rules and Cost Audit Report Rules' was organized at Kolkata on 28th September 2012 and like other seminars, it was well received by the industry, corporate, professionals including our members. A programme on CARR and CAR was also organized for NCR Chamber of Commerce and Industry, Gurgaon.

For the first time a Residential programme was organized at Vayalar, Kerala on the topic Recent Trends in Corporate Reporting including IFRS during 9th-12th October 2012. Two programmes were organized at Goa during 15-18 October, 2012 on `Emerging Issues in Management of Taxation' and `Activity Based Costing'.

In-house programme was organized for Indian Air Force on Accounting Standards & Costing during 15th-20th October, 2012. The Institute has sent proposal for Induction Training programme for 90 officers of Punjab State Power Corporation Ltd. on residential basis at Delhi NCR.

The 1st Finance & Accounts Technical Training Program of SG/JAG IRAS Officers for Ministry of Railways (Railway Board), Government of India held at Delhi, London and Paris has been successfully concluded on 7th October, 2012. The programme was very well received by the participants and we got excellent feedback from the Railway Board. The 2nd and 3rd batch are confirmed to be held during January and March, 2013.

CEP-2 Directorate in continuation to the series of Awareness Programmes on "Filing of Cost Audit and Compliance Report in XBRL (eXtensible Business Reporting Language)" organized programmes at Hyderabad Centre of Excellence, Pune, Guwahati, Nagpur and Bangalore during the month. Our Key experts CMA Kunal Banerjee, past President, CMA T.C.A. Srinivasa Prasad, Council Member and CMA S.A. Murali Prasad, Management Consultant tirelessly deliberated the sessions for training our professionals.

For successful implementation of the Indirect Taxation, new framework of Cost Accounting Records and new mechanism of Compliance Report and Cost Audit Report our Regional Councils and Chapters have actively organized the programmes at NIRC, SIRC, Gurgaon, Jaipur, Asansol, Lucknow, Thrissur and so on. There was overwhelming response and active participation by members.

On demand and request by Reliance Industries Limited, CEP-2 organized a programme on "New Framework of Cost Accounting Records Rules, 2011 and Companies (Cost Audit Report) Rules, 2011" at Reliance Corporate Park, Navi Mumbai. It was well received and appreciated.

The department is under process of updation of the Online CEP Credit since April 2012 for viewing the status of CEP Credit Hours awarded to the members for attending the CEP programmes organized by Head Office, Regional Councils, Chapters and Corporates. To view CEP Credit Hours on the Institute's website members may please look for Online Membership Application System.

HR Activities

Training:

There was a training scheduled on 4th October 2012 on "Self Development and Team Building"; session was facilitated by CMA T.C.A. Srinivasa Prasad, Council Member and participated by all the Assistant Directors of Headquarters, Kolkata. The next session was on 12th October 2012 on "The Branding of the Institute" (2nd Session) which was facilitated by CMA A.S. Durga Prasad, Council Member was attended by the officers of the rank of Deputy Director (onwards) of Headquarters, Kolkata.

Recruitment:

We have published recruitment advertisement on 17th October, 2012 which is on pan India basis for the position(s) of Dy. Director, Assistant Director, Senior Officer and Officer cadre.

Membership

The scheme of Benevolent Fund has been redesigned to provide more benefits to the members of the Fund. The enhanced benefits in the form of financial assistance have been provided as below:

Grant on death has been raised from Rs.10000/- to Rs.25000/-

For critical illness Rs.15000/- has been raised to Rs.20000/-

International Affairs

The Institute participated in the 1st Pakistan India Management Summit held at Lahore, organized by the Nutshell Forum and Aman ki Asha, during 20th to 21st September 2012. The Institute was represented by a delegation led by CMA S.C. Mohanty, Vice President. CMA Sanjay Gupta, Council Member and CMA J.P. Singh, Additional Secretary were other members of the delegation. The objective of the summit was to promote knowledge cooperation for sustainable development, bridging the gap between the intelligentsia of India & Pakistan and sharing regional best practices. Being one of the Knowledge Partners, CMA S.C. Mohanty, Vice President, expressed his views as one of the panelists in the Technical Session on "*Institutionalising Partnerships*". His views were given due recognition by the media and it was widely covered in the local newspapers of Lahore.

I along with CMA Sanjay Gupta, Council member and Chairman, WTO and IA Committee attended the 1st Annual Meeting of the

President's Communique

Cultural Diversity Platform on Accounting, Finance and Auditing held in Paris on 3rd October 2012, hosted by French National Association of Chartered Accountants (CSOEC) and Federation of Francophone Accountants and Auditors (FIDEF).

CMA Sanjay Gupta, Council member and Chairman, WTO and IA Committee also attended a meeting at Institute of Management Development, Switzerland and discussed issues relating to MRA, Joint Research Project, sharing of expertise and development of Standards with Mr. Steward Hamilton on 5th and 6th October 2012 at Lausanne, Switzerland. He also met Mr Noel Tagoe, Executive Director of Education of CIMA, UK on 9th October 2012 at London, UK to review the MoU with CIMA.

I am happy to inform all the members that Institute of Directors in partnership with the Institute organized London Global Convention 2012 during 10 to 13 October 2012 at London, UK and I got the privilege to deliver a special address to mark the occasion.

I along with CMA S.C. Mohanty, Vice President and CMA Amit Apte, Council Member attended Extraordinary General Meeting (EGM) and other Committee meetings in Sri Lanka during 18-21st October 2012 organized by the Confederation of Asian and Pacific Accountants (CAPA). During the International Conference on 20th October Dr. S.K. Gupta, Director (Technical) presented a paper on Apprehensions regarding Integrated Reporting. The presentation was highly appreciated by the participants.

As decided in the last meeting of the SAFA PAIB committee to organize webinars on varied topics, the Institute organised 2nd SAFA-EEFA webinar on the topic "How can SMPs interact worldwide to help SMEs develop businesses" By Mr. Giulio Veneri on 12th October 2012. The webcast was seen by many SAFA member bodies.

CMA S.C. Mohanty, Vice President along with CMA P.V. Bhattad, Council Member attended various Meetings of International Valuation Standards Council (IVSC) during 25th to 27th October 2012 at Milan, Italy. The Institute is an institutional member of the IVSC. The members also attended the meetings of IVSC Standards Board and IVSC Professional Board at Milan during the period**.**

Technical Directorate

Continuing with the pace it has picked up, CASB has approved the release of exposure draft of CAS on Marketing Overhead and the same was hosted on website of the Institute for public comments. The exposure draft of Guidance Note on CAS on Administrative Overheads was also hosted on the website for public comments.

Directorate of Research

Benchmarking Tools for Panchayati Raj Institution

Indian Audit & Accounts Department is partnering with ICAI for developing benchmarking tools on the basis of the performance of various panchayati raj institutions. For developing the benchmarking tools, various ratios and parameters are to be identified and considered in the context of their efficiency, effectiveness and performance. We have already completed an initial survey for the Pilot Project in this regard in Birbhum District of West Bengal. In the first phase, we have visited seven Gram Panchayats to collect relevant data. We are now in the process of compilation of the data collected during the field visit and will come up with our findings, initial recommendations and plan for our future course of action.

Partnership with ASSOCHAM

We are proud to have been associated with ASSOCHAM as a knowledge partner on the topic "Inter State Trade Barriers – Concerns & Solutions" during a Seminar held on 18th October 2012 at New Delhi. CMA Suresh Chandra Mohanty, Vice President, ICAI shared the stage as key note speaker with Prof. K.V. Thomas, Hon'ble Minister of State (Independent Charge) for Consumer Affairs, Food & Public Distribution, Govt. of India, Shri D.S. Rawat, Secretary General, ASSOCHAM and other eminent dignitaries. CMA (Dr) D.P. Nandy, Director (Research & Journal), ICAI presented a technical paper on this topic in the technical session. CMA Manas Kumar Thakur, Chairman, Research & Publications Committee, ICAI and other delegates of the Institute also attended the seminar. It was a very successful event and more importantly ICAI has been engaged as the knowledge partner of ASSOCHAM in their upcoming events also.

Workshop with the Institute & Central Agricultural University, Imphal, Manipur

A joint workshop with the Institute & Central Agricultural University, Imphal, Manipur on "Project Cost Management in Agricultural Research Projects" was held on 10th September 2012 which was conducted by CMA Chandana Bose, Sr. Director, Research and CMA (Dr) Sumita Chakrabarty, Jt. Director, Research under the guidance of CMA Manas Kumar Thakur, Chairman, Research & Publications Committee, ICAI. The workshop was inaugurated by Dr. S.N. Puri, the honorable Vice Chancellor of the Central Agricultural University who, in his speech, highlighted the importance of cost management techniques for an efficient and successful Agricultural Research Project. Eminent personalities of different institutes also graced the occasion and thanked our Institute for the initiative taken to organize such a workshop for their researchers.

Meeting with the Hon'ble Minister and Officials at Tripura

CMA Manas Kumar Thakur, Chairman, Research & Publications Committee, ICAI met Shri Khagendra Jamatia, Hon'ble Minister of Co-operation & Fisheries, Govt. of Tripura, Shri S. Riyan, Registrar of Co-operative Societies, Govt. of Tripura and Shri N. Remesh, GM, NABARD, Tripura Regional Office on 5-6 October 2012 and submitted a concept note on "Role of CMA in Cooperatives". The meetings were very successful and Shri Thakur approached the Hon'ble minister to engage ICAI to conduct a research study on "Performance Evaluation of Cooperative Societies in Tripura" soon.

I wish all the members and the students a very happy and joyful month of festivals covering Dhanteras, Diwali, Govardhan Puja, Bhai Buj, Chhath Puja and Guru Nanak Jayanti.

With warm regards,

(CMA Rakesh Singh)
31st October 2012

CMA A. S. Durga Prasad
Chairman,
Infrastructure & IT Committee

Dear Professional Colleagues,

It gives me immense pleasure to connect with you through the 'Management Accountant' Journal and share with you the progress made by the Infrastructure & Information Technology Committee to create value added services for the stakeholders of the Institute.

In doing so, I will first dwell upon matters relating to Infrastructure and then on activities on IT. In regard to Infrastructure, I am happy to state the following achievements:

- Hyderabad Centre of Excellence (CoE) – The CoE at Hyderabad has blossomed into a full-fledged academic seat of excellence which was inaugurated on 22nd January 2012. The Advance Study courses and other training programmes for the members are being conducted in this CoE. Work has commenced for additional three floors which will have one auditorium and lodging facilities. This will facilitate the conduct of training programs in house .
- Jaipur Centre of Excellence (CoE) - The committee has recommended to the Executive Committee of the Institute to release fund for setting up of CoE at Jaipur and accordingly application money has been paid to Rajasthan State Industrial Development & Investment Corporation Ltd (RIICO). RIICO has also confirmed the allotment of land to the Institute.
- Land for Aurangabad Chapter - The committee has recommended to the Executive Committee of the Institute to release fund for purchase of land at Aurangabad from CIDCO. Registration of the land has been completed from the Institute's side.
- Renovation of both and Delhi and Kolkata offices have been taken up to give a facelift to the buildings.

With regard to Information technology, we have been able to able to make significant strides. IT plays a key role in improving the efficiency in any organization. To keep pace with the future expansion plans of the institute, the IT infrastructure in the Institute has been strengthened in the last few years and efforts have been made to automate and integrate various functional units of the Institute through integrated web based applications. I am happy to share with you some of the key initiatives of Committee:

1. Online Student Registration system has been implemented across all Regional Councils and Chapters of the Institute. The system is integrated with the Studies and Finance Directorate of the Institute.
2. An online Membership portal has been implemented which facilitates members accessing their records and also make payments related to renewal of membership and also Certificate of Practice. It allows access to new graduates for applying for membership. In addition to this, existing members can also access their CEP hours details online and need not maintain any records of paper based CEP certificates.
3. Webinar facility is created wherein online webinar are conducted by professional experts on key important topics in the area of management accounting. The members may register online through the website and attend the webinar. The archive recording of the webinar are also made available to the members on the website of the Institute. The webinar subscription has now been upgraded to 2 rooms with 200 participants each. Webinars are planned for students also wherein important topics would be addressed by members in service and practice, which will benefit the students.
4. The Video Conferencing facility, which is used for conducting various meetings has been implemented in the Institute connecting following four locations of the Institute at Delhi, Kolkata, Mumbai, Chennai.
5. The Website of the Institute is now very rich in content with the relevant and important information being made available for the students and members. Separate portals have been created for students, members, Training & Placement, Examination and Continuing Education Programmes etc. Under each of the above sections, the information has been classified and made available under appropriate menus/links.

I take this opportunity to request all to kindly visit the website of the Institute to keep abreast of the latest news and developments in the Institute. Last but not the least, I would like to thank the President and the Council for reposing confidence in me and for their valuable support in all our endeavour.

Wishing you all the very best,

With warm regards,

(CMA A.S. Durgaprasad)
Chairman (Infrastructure & IT Committee)
2nd November 2012

Measurement and Accounting for Intellectual Capital

Shyamal Banerjee
Former President, ICAI (formerly ICWAI)
Ex-Sr. Professor, IIM-Calcutta
Member of Indian Defence Acccounts Service (IDAS)

Intellectual Capital: Nature and Characteristics

A capital, in any form, represents a claim to future benefits. "Intellectual Capital (IC)" is a knowledge asset housed in persons (employees), instruments (patents) or structure (customer relation or supply chain). It is essentially abstract and intangible. Sometimes such assets are protected by law such as patents or copyrights under the Patent Act. At other times they have no legal mooring and have to be built and nursed by the organization. Intellectual Capital is also called by the name of "Knowledge Capital" or just as 'intangibles'. The emerging criticality of knowledge capital was foreseen by Peter F. Drucker quite sometime ago. Among many of his pithy remarks he had predicted, - the nineteenth century was fought on the basis of *cost*, the twentieth on the basis of *value* and the twenty-first will be fought on the basis of *knowledge*. He had called the emerging societies as 'knowledge society' which had a chance to flourish or even survive.

Before we try and evaluate and 'account' 'intellectual capital' or 'knowledge or intangible assets' we attempt to identify some 'features' and properties of such assets which distinguish them from physical assets (plant, machinery) or financial assets (bonds, shares, bank deposits) or human assets (employees).

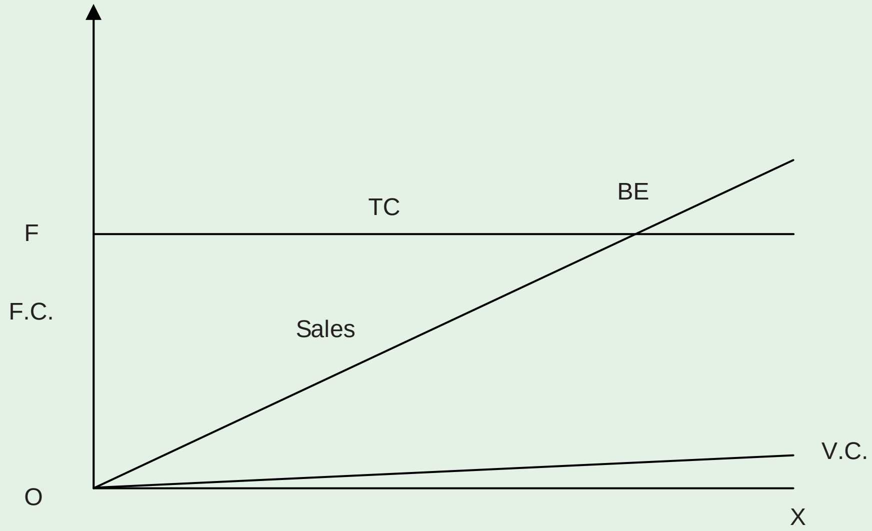
Non Exclusivity

First, the intellectual or knowledge assets are non-exclusive and non-rival. Thus a physical (or human or financial) asset when set up or used at one place cannot be used simultaneously at another site or purpose. Not so with intellectual assets. A patent or software or brand or technology (say, a better way of producing a special steel) once produced or acquired, may be licensed and used simultaneously at countless sites. This property of I.C. makes a critical difference in accounting of their output or benefit-in-use. A pharmaceutical molecule may be invented after a couple of billion US $ in research expense; a software may be developed for space programmes at a huge expense in research; a large oilfield may be located after vast unproductive explorations; a brand or goodwill may be established and then nursed against erosion or competition at great and prolonged cost. The physical cost of the output of such large cost may not be much. The physical cost of the molecule or application of the software, or the cost of benefits derived from the brand-equity is mostly not much compared with the huge expenses that lie behind their creation or development. The accountants or the economists are not unanimous on the accounting or disclosure treatment of either the *output* of the huge expenses or of the *expenses* themselves. The laws and the accredited reporting formats differ between countries and even among corporates within the same country.

Another offshoot of this property of non-exclusiveness and non-rivalry of I.C. is sometimes their near-monopolistic dominance in the markets in which they operate. Google, Amazon, Intel, Cipla command through patents or brands a huge market share which is unachievable by some of world's largest enterprises in physical products such as Walmart, McDonald, General Electric or any of the Fortune 500 corporates. The conclusion - scale of operation is most important for IC companies. The Break Even Point is high but the contribution is immense. The picture in our traditional accounting diagram would look like as under:

Protection of Rights

Accounting of IC must take note of the factor in continuing costs of vigilance and protection of the rights and benefits of the IC assets. Infringement of Patent, Copyright and Trademark Rights is frequent. In certain countries the trademark laws are loose, and in same others they are in position but are not seriously taken and rigorously implemented. Vigilance and protection costs of trade rights and deterrence of counterfeits must therefore



appear as a cost item in the Profit & Loss Account of and IC Company.

High Risk

Philip Kotler, among others, have stressed the fact that creation and commercialization of a product bears very high risk of failure. And while it is so for physical products as well, the level of risk is extremely high for IC products. The reason will be evident if we go through the successive stages of new product development. We reproduce here a chart from Kotler's Marketing Management (The Millennium Edition) which suggests the successive stages (eight) of the product development process.

As one goes through the process involved at each stage and relates it to an IC product, say, in pharmaceutical or software fields, one at once realizes the exceptional hazards that cloud product-clearance at each stage.

Finance Constraint

IC companies have difficulty raising debt finance. Lending institutions have reservations in lending large funds without collaterals in fixed assets. The IC company itself carries high risk and is saddled with high operating leverage in terms of high fixed employees cost. Prudence demands that they avoid high financial leverage and rely on retained earnings besides some limited equity that they can raise feasibly from the market. There is a bit of conflicting duality here. The return on IC tends to be lagged. Unlike physical products they are not directly marketable. The IC product does not sell as it is. Yet, it is a means and carries huge possibility of large almost monopoly profits in the future.

I know two cases here from my personal involvement. One is an IT company in which I was an External Director. For five years it has continued to make a loss on the equity (small) capital of Rs. 5 cr subscribed by its (large) parent company. It has failed to reach the critical scale or to invent some software which is so unique that it could capture a niche market as a monopoly. Or, perhaps, it could not market its product imaginatively and locate the right buyer.

The other case is where I was the Architect and Chief Executive. I headed the marketing division of a major public sector fertilizer company with a command area of the seven north-eastern states (the seven sisters) plus Assam, W. Bengal, Bihar, Orissa, Eastern U.P. and Madhya Pradesh for 12 years (1969 – 80). When I started the marketing division, which was then the first in India, as it was only in 1968 that the government decided to leave the marketing job to the industry, which till then had been in the hands of cooperatives, use of chemical fertilizers was almost absent except some ammonium sulphate for tea plantation. The technology of soil-crop-fertilizer relation was unknown. I had serious trouble convincing even large farmers that use of the right fertilizer in right mix and quantity specific to different crops would be highly profitable. The name and function of the macro nutrients, (N, P, K) and the need for balanced micro nutrients like boron, sulphur, zinc, manganese, molybdenum and the nature of the soil (acidic or alkaline) was unknown.

The Small Case Study

I was in a quandary. I could not sell my fertilizer. Then I decided to demonstrate. There was a farmer in Gushkara, a small place in Burdwan district of West Bengal. By W.B. standards he was a large farmer with a holding of 5 acres. I went and sat with him under a banyan tree on the fairly extensive lawn of his village home and made a proposal. The proposal was that 'I undertake cultivation (of paddy) of half of his plot in my own way and at my own cost, and he cultivate (the same crop) the other half in his own wonted way. Whatever he produces from his own half, that I would guarantee and give him from the half that I cultivate. And if, from my half, I produce more that too would be left with him and given to him.' I wrote out a simple agreement accordingly and signed it with two witnesses. Coming from the head of organization of a government company, he had no way other than to trust it. He had a choice of 'head you win, tail I lose'. The proposal was irresistible. After the season he got from my plot four times the quantity that he produced from his half. The job was done. The farmer had standing and influence. The news spread by word of mouth and gained momentum. When I started marketing the sale was nominal. In a decade when I left it was a million tonnes. Of course support services like soil testing, channel improvement and others were mounted. The source was not only the factories (and new factories came up) but imports organized by the government.

The IC that was generated benefited the nation and profited the farmers. It was not reflected in the national balance sheet or the farmers' book for the simple reason that no such Balance Sheet or books were maintained or reported. Nevertheless huge benefits accrued and despite shortfall in irrigation and defaults in extension administration, the 'green revolution' had its visible impact till at least the end of the seventies.

The Intelligence Gap

Unlike physical assets investment in IC is largely invisible. Also the benefits and value addition that accrue from IC is, as we noted earlier, indirect and amorphous evading separate identification. It works like the ambience which is easy to perceive as hostile or wholesome but is wellnigh impossible to spot or separate. Our corporate (or national) reporting methods and means have remained traditional. There is near-unanimous recognition that the industrial economy of the 19th and first half of 20th century has drastically changed. During that period of history firms could sustain their preeminence by efficient production and marketing and well-directed investment decision. So long as IRR on marginal investment exceeded the marginal cost of capital success and growth was assured. The position has since shifted dramatically during the latter half of the 20th century and now has taken its firm roots where IC has become a critical resource and a key driver of competitive edge and value creation for customers and stakeholders. That is why now, in the present world, traditional cost-focused reporting methods are no longer able to offer an adequate and comprehensive picture of firm performance and project success now has shifted to a different, distinct driver, which may be summed up in one abstract word, - 'creativity'. Japan, ahead of all others, has spotted (and gone all out implementing) this new success-driver. In its various programmes such as Kaizen, 5S+2 or 7S, Zero-defect focus and so on it is making sure that each 'day' be different from and better than 'yesterday.' Differentiation, product positioning and repositioning, brand building, sustainable supply chain, working towards patents and trade rights, converting customers from casuals to loyals to patrons, benchmarking systems and structures are among some of the present focus areas of global and national corporate houses. Each firm is searching for the dynamic best of the day. And this is being done not merely by creating and generating each and everything all by itself but by borrowing and copying and appropriating from others through mergers, licensing, franchises and all kinds of innovative alliances.

Fine! Yet our corporate reporting has lagged behind. The objective of financial reporting is to provide insight and useful information to users to appreciate the financial position and performance of the firm and make economic decisions with respect to it. On this most international standard-setting institutions such as Financial Accounting Standard Board (FASB, 1978), Statement of Financial Accounting Standards (SFAS) and International Accounting Standards Board (IASB) are agreed. These and other similar bodies, all across the world who are struggling to devise a one harmonious International Financial Reporting Standard (IFRS) format for IC acceptable globally to all, seem to be sitting on a fence. They find that, on one side there is the 'fire'; on the other side there is the 'frying pan'. The present position seems to be that the august accredited Accounting Regulatory Bodies of the world are all fuming and fretting but making sure all the time that they do not fall off the fence – simply because they like neither the 'fire' nor the 'frying pan': 'the fire' – reporting may lose relevance, 'the frying pan' – over-liberal, unsafe, anti-conservatism.

Some Measurement Issues

Is it possible there could be a negative contribution to Intellectual Capital (IC)? A physical asset will seldom have a negative value unless; in an exceptional case it poses high risks. A radio-active plant, for example, or an inflammable asset that carries fire hazards. But an IC is quite prone to a possible negative value. The Mind controls human activities and the physical organs obey and do what the mind decides. When a company (managers and employees) decides to do harm to all or any of its stakeholders it certainly creates negative IC. But how or when does it happen? It happens when ethics and transparency is violated, when corporate governance is sullied or compromised. This possibility of managing a company we have not considered so far; nor does the literature (as far as we could gather) on IC seems to have tackled this issue squarely and face to face. One way, to our mind, of factoring in this issue is to include the 'ethical score' of a company in its score-card, whatever the model of valuation that is adopted.

The seat of 'ethics' is the mind. According to the Freudian 'model' of functioning of the mind, the mind has three components, named here in ascending order – the lowest being closest to sensual world, that keeps company with the five physical organs – the eyes, the ears, the nose, the palate (tongue) and the skin that registers the sense of touch. These components are Id, Ego and Superego. Their discrete functions are:

- Id: the part of the mind in which innate instinctive impulses and primary processes are manifest.
- Ego: the part of the mind that mediates between the conscious and the unconscious (we may include the subconscious as well) and is responsible for reality testing and a sense of personal identity.
- Superego: the part of the mind that acts as a self-critical conscience, reflecting social (we may also include moral) standards learned from parents and teachers, (we may also include environment)

We need not confine our understanding of the terms to the succinct phraseology that has been used by the COD, necessarily for brevity. We do have a glimpse of how and whereabouts of the functioning of the mind.

The Hindu science of the mind is somewhat similar but is more elaborate. Let us see how it is. Taking off from the Kapila's Sankhya view, we may divide the mind into four parts. These are:

- Manas: this is the outer part which is juxtaposed with the sensual world through the five physical organs. The physical organs receive the impulses from the outer world and send them to the 'manas' part of the Mind.
- Chitta: this second part of the mind combines the impulses, so received with the vast (infinite) storehouse of impression that lie imbedded in the subconscious. In fact, without one being aware the subconscious is sending up bubbles of thoughts all the time which together with the current impulses registered by 'manas', knock at the door of 'Buddhi', which is the third part of the mind.
- Buddhi: this is the seat of 'conscience' – the critical faculty that discriminates between what we call 'right or wrong', 'just or unjust', 'fair or unfair', the duality (*dvaita)* that permeates the cosmic universe and is the cause of its origin. The ethics of the Intellectual Capital (IC) is decided here. Here we depart from the Freudian model, because visible action is not taken either by "Buddhi" or by "Superego". This 'action' is taken by the fourth and final component of the mind.
- Aham (Atman): this fourth part is *Aham*, who is the doer. Buddhi discerns and advises and Aham acts. We must not go deeper into Hindu Philosophy for, we are told that this Aham itself has a duality – the lower and the upper. The lower one is attached to the world, the upper one unattached and alone. But let that be. We conclude, negative IC is possible (which is happening all the time) and in any IC valuation approach ethics, transparency and corporate governance must occupy a seat of eminence. Of course when brand image is taken in as a component of IC, too, ethics gets factored in and there may be some double-counting when both are given their due weightage in the corporate scorecard. Yet, to our mind, there is no harm even if the all-important factor of 'ethics' is somewhat overweighted.

Model-building for Measurement of IC

We repeat that as the service sector grows (it is now around 62%/63% of GDP in India) and intangibles dominate the national economy (GDP) recognition of Intellectual Capital in every form of business and its appropriate reporting to internal as well as external stakeholders will become both wise and compulsive. Literature which has come up is already voluminous and research interest in it steadily growing. In what follows below we shall draw upon some of the materials available in books, periodical and published papers but not without a critical look.

In building any model of Measurement of IC two variables need to be identified and then linked in a causal relationship. These two variables are:

- The elements of Intellectual Capital (IC)
- An estimate of cash flow during the lifetime of the IC, from each element (in isolation) or in aggregate of the IC.

The same is true of physical capital or tangible capital in the form of tangible assets. They are easily identified and measured. For, they are sourced from three sources, all in easily measured monetary terms. The sources are:

- Equity or ownership fund.
- Borrowed funds (debt capital)
- Retained earnings (PAT less dividend payout).

The task is easy. The cash flow estimates are more complicated. First the working life of each physical asset is, at best, an intelligent guess with the help, historically, of the experience with similar assets in the past. The future cash flow estimate is beset with more uncertainty for, by definition, the future is dark and any prediction is at best a guess work.

But then as we come to IC the inherent difficulties and uncertainties are compounded manifold. We may perhaps do well to bare our hearts and lay our cards, face open, on the table for all to see. That way, at least, no one can accuse us of concealment or bluff.

- The elements that add to or detract from the IC of a firm are so countless, and often so illusive that no one indeed can ever vouch that they have been located.
- The elements work together in a kind of chemical combination where the property of the whole has little semblance to the property of the constituent elements. The IC is a *gestalt* (where the whole is greater than the sum of the parts) of hybrid elements each saddled with its algebraic sign.
- The elements are disaggregable and un-isolable.

There is one even more severe difficulty in measurement and accounting of IC. Intellect is the origin and driver of IC. IC is not the derivative of the financial balance sheet. In fact it is the other way round. The latter in IC intensive companies is largely driven and determined by the former. We are familiar with the measurement of IQ, EQ and SQ. The three variables, -Intelligence, Emotion and Spiritual stance of a person abide in his Mind. The word 'Intellectual' in our theme of IC is used as a surrogate of all the properties of the mind – intelligence (or intellect), emotion and the spirituality. Therefore, in building any model to capture, measure and account (put a value-preferably financial to) the status and growth of the intellectual capital of a firm we need to identify the visible outcome of all the above three properties of the mind. What is the outcome of intelligence (Buddhi)? Obviously, it is the quality of the decision making process of which the core is the investment decisions. Similarly we ask, what is the visible output of the 'emotion coefficient' (EQ) of the firm? It is 'relationship' – both internal and external, an atmosphere of mutual help and cooperation, what Henry Fayol called by the term '*esprit de corps*'.

What, now is the role of *spirituality* (SQ) and what is its coveted visible output within the business sphere of a firm? The one-word answer that comes to mind is '*business ethics*'. Yet, this answer seems too simplistic. What is the content and scope of '*business ethics*' has been and continues to be the '*will-o-the-wisp*' or the '*golden stag*' (*sonar harin*) of Management Gurus. There seems to be as many versions of it as there are management thinkers and writers. So, I thought, why not add my own version here, provided only that the Editor should find it worthwhile to permit the space that it would consume.

To my mind, we ought to try and understand 'business ethics', in its worth as Intellectual Capital, through its various constituents. Each constituent of Ethics has its particular relevance to the different stakeholders. Thus –

1. To the tax payer and the general community a business should not throw up or display an image of the business that it knows it does not possess. This is the condition of transparency.
2. To the consumers the business has a moral responsibility to provide goods and services of the announced quality and at a price that is fair and proper.
3. To the employees, the management ethics includes extension of a fair deal; fair and just standards applied uniformly without favour, prejudice or malice.
4. To the government and other institutions with which the management has dealings, ethical standards imply a fair and truthful presentation of one's case, facts and status in all inter-unit and inter-personal deals and transactions.
5. To the creditors and suppliers the business should give a fair deal, respect agreements and understandings regulating business conduct and affairs, and
6. To the channel members a fair and equal treatment with no idea of exploitation through the use of its power or preeminence.

In general, the business should perform according to the laws, mandates and regulations of the land, use resources with due care, avoid using public power for personal gain, fulfill all assurances truly and faithfully and conduct the affairs of the business in the wider interest of the community consistent with its own primary role of attaining the enterprise goal.

Having said all this we must throw in here some cautionary words. Business ethics cannot be effective unless it is set to tune with the ethical standards of the environment and of the society at large. If the powers of the regulatory or service-yielding machinery – governmental institutional and others – are not used fairly and legally business ethics is bound to be under strain, and power, wherever it lies, has a proneness of its encashment for some illegitimate benefits of the power-wielder. It so happens that a business is often hamstrung when it finds that its legal rights and fair and legitimate dues in the conduct of business are denied of abridged through unfair practices of the regulatory machinery.

Some Financial Measurement Models of IC and Their Accounting Practices

All Models, whatever their approach or format, have the common aim of measuring the financial contribution of an Intellectual Capital. It follows that no single model can be devised to capture the financial contribution of all and every constituent of Intellectual Capital. We shall now

1. consider some of them (as briefly as we may),
2. Suggest *intangibles* that they suit and the present accounting status (generally) of such *intangibles*.
   a. **DCF Model:** Under this model the value of an IC (just as for physical assets) is determined by using the present value of the projected cash flows generated by the asset after factoring in the risk-profile of the asset and the contribution

of other assets and applying the discount rate which reflects the cost of capital of the applicable risk category. This method is commonly used for assets such as technology, software, customer relations, covenants not to compete (assuming it is legal), franchises, supply chain and distribution channels. As for the accounting recognition of such assets it is subject to the conditions specified by the International Accounting Standard (IAS 38). According to IAS 38 a company can only recognize an asset if it is 'identifiable, controlled, probable that future benefits specifically attributable to the asset will flow to the enterprise and the cost can be reliably measured. These recognition criteria apply both to the purchased and self-created assets. If an intangible asset does not clear the above criteria, IAS 38 mandates the outright expensing of the item.

b. **Relief from Royalty (or Royalty Saving) Model:** An Intellectual Capital in the form of intellectual property as defined by the TRIPS (Trade Related Intellectual Property Agreement under the WTO given effect to from 1.1.1995) such as Patents, Copyrights, Designs, Trade names and Trademarks usually involve a royalty payment when such rights are licensed from the rights holders. For a company which owns such an intellectual asset, the value of the asset in terms of this model would be equal to the discounted present value (net) of all the future royalties that would have to be paid for the right to use the asset if it had not been acquired or internally generated. The royalty rate would be decided according to market condition relevant to the asset category. This asset fulfils the recognition conditions under IAS 38 and may be reflected in the Company Accounts.

c. **Comparable Asset Pricing Model:** Certain intangible assets are internally generated as part of management. They cannot be separated or individually costed. Yet their benefits are clear and find their reflection in the firm's overall balance sheet. Some examples are – product brand (Rin detergent cake), corporate brand (Tata, Amul) mastheads and logos, customers' mailing list, internet domains, business process and so on. These are outside the protected list of intellectual property right and, thus, cannot find a place in the accounts. Yet, their valuation is important for internal control, and for strategies to contain their erosion and periodically assessment of their contribution. The value of such assets is estimated based on the actual prices paid (or payable) or expenditure incurred for assets with similar functional or technical features. Obviously such valuation is largely subjective relying on informed judgement.

d. **Avoided Cost Model**: This model is similar to the method of valuing purchased goodwill and is appropriate in the case of acquisition or combination of firms. Available historical information is used and assumptions are avoided. Under this method the value of the intangible asset will comprise the costs avoided by acquiring a firm in possession of an existing intangible asset rather than incurring costs in generating the same asset. In practice the intangible assets are identified and valued by the purchaser as part of the purchased goodwill in a business combination. Such value, as so determined, is reflected in the statement of final position of the company.

e. **Value Based Approach (VBM):** Several VBM approaches have been developed which can all be applied to value creation and value measurement of Intellectual Capital (IC) or intangible assets. They have been devised and patronized by different international consulting firms. We shall mention *five* such approaches here but spend some time (and space) on the EVA (economic value added) model which seems to have the largest backing.

   a. **Marakon Approach:** This approach was devised by Marakon Associates, an international management consulting firm. This approach focuses on shareholder value (wealth) creation. It suggests that shareholder wealth creation may be measured by the simple ratio of market-to-book ratio. More simply, it assumes that the market-to-book values ratio is a function of the return on equity, the cost of equity and, expected growth rate of shareholders' dividend.

      Thus, M/B = (r-g)/(k-g) where,
      M = market value of equity
      B = Book value of equity
      g = the (expected) growth rate of dividends
      It follows, M/B > 1 when r > k. Also value is created in proportion to the spread between 'r' and 'k'. Again, when r > 1, a higher 'g' (dividend) contributes more to the value creation.

   b. **Alcar Approach:** The Alcar group (a management education and software company) postulated this approach. This approach starts with the task of identifying the value-drivers. They have spotted *seven* such drivers:

      i. rate of sales growth
      ii. operating profit margin
      iii. income tax rate

iv. investment in working capital
v. investment in fixed capital
vi. cost of capital
vii. value growth duration.

The value growth duration is the estimated period over which the investment is expected to earn rates of return (r) in excess of the cost of capital (k). thus the impact of an R &D, or a brand or an advertising campaign may be positive (r>k) only for a limited period. The firm will now consider the various strategic options and the value creation of each with alternative feasible values of the above variables.

c. McKinsey Approach: This approach, indeed, is a forceful reminder of the management mindset, its recognition of the 'value drivers' and formulation of strategies that converge and pull together toward the management goal and aspiration. The approach has been defined as 'an approach to management whereby the company's overall aspirations, analytical techniques, and management processes are all aligned to help the company maximize its value by focusing decision making on the key drivers of values'. This stresses a corporate value mindset which has two dimensions:

i. **Value Matrices:** these are answers to *four* questions:
- Does the management know how companies create value?
- Does the management understand how the stock market values companies?
- Does the company expressly include opportunity cost of capital in its measurement?
- Do the metrices bring out economic results, instead of mere accounting results?

This approach stresses that the management must veer to a situation when the answer to all four questions is an emphatic – "Yes".

ii. **Value Mindset:** the Value Mindset of the company is similarly captured by asking *two* questions:
- Does the CEO and the top team set the highest importance to shareholder value creation?
- Does the CEO set and constantly reset strategies to shareholder value creation?

Again, the answer must be 'Yes' to both questions. The approach then selects five areas of activity which are nodal to value creation. These are:

a. **Mission, aspirations and targets:** the company must spell out a 'goal' which inspires its employees and set out value-linked targets that demands the best out of employees.
b. **Portfolio Management:** the company must identify its strategic (core) advantages and build a basket of portfolios that exploit them to the full. It must set out performance indices, constantly improve performance and provide profitable growth avenues.
c. **Organizational Design:** the organization should be designed so that

- Performance units are well-defined and
- Individual accountabilities are well set out.

This alone will enable translation of goals and strategies to actual performance.

d. **Spelling out of Value Drivers:** value-drivers are key performance variables such as customer satisfaction, customer retention, revenue per employee which have a strong correlation with company results. Such key performance indicators (KPI's) need to be identified, institutionalized, regularly monitored and reported.
e. <u>Business and Individual Performance Management</u>: business and individual performance should be systematically monitored for value creation through the KPI's.

d. BCG Approach: this approach is by Boston Consulting Group (BCG), an international consulting firm. This approach relies on *two* indicators:

- <u>Total Shareholder Return (TSR)</u>: this is the shareholder's earning on the stock of a company. It is computed as

TSR = (Dividend)/(Beginning Market Value) + (Ending Market Value – Beginning Market Value)/(Beginning Market Value) = (Dividend +Appreciation in Market Value)/(Beginning Market Value)

- <u>Total Business Return (TBR)</u>: TBR is actually the IRR + Capital appreciation. It is computed as:

TBR = (Free Cashflow)/ (Beginning Value) + (Ending Value – Beginning Value)/(Beginning Value)

e. The EVA Approach: the EVA Approach was developed by the consulting firm Stern Stewart & Co. It is currently the most popular model. Peter Drucker described it as a 'measure of total factor productivity.' EVA may be computed as

EVA = NOPAT – c* x CAPITAL
EVA = CAPITAL (r – c*), where
EVA = Economic Value Added
NOPAT = Net Operating Profit after tax
c* = Cost of Capital

CAPITAL = Economic book value of the capital employed in the firm
r = Return on Capital (NOPAT/CAPITAL)

The Components of EVA

The above expressions for EVA show that EVA is a function of (i) net operating profit after tax (NOPAT), (ii) cost of capital (c*) and (iii) capital employed in the firm. We may have a brief look at the meaning and content of these *three* components:

I. Net Operating Profit After Tax:

a. NOPAT is defined as -
(Profit before interest and taxes) x (1 – tax rate)
This expression for NOPAT separates the financing cost (interest for debt and dividend for equity) from the return on investment (profit or cash flows). Financing cost will be taken care of in the cost of capital adopted for discounting the profits or cash flows.

b. All figures to be considered on post-tax basis.

II. Cost of Capital: capital comprises equity (funded by shareholders) and debt (provided by lenders). Shareholders demand dividend to keep them invested. Lenders need to be paid besides security. Such dividends and interest make up the 'cost of capital' of the company.

Computation of Cost of Capital (c*)
c* = (Cost of equity employed) + (Cost of preference shares at stated rate) + (Pre-tax interest on debt) x (1 – tax rate).

III. Capital Employed:

For our purpose 'capital employed' needs some adjustments to capital shown in the accounting balance sheet. These adjustments would convert the capital assets to their 'economic value' from their 'accounting values'.

The major adjustments

- **R & D:** In GAAP and most other accounting standards R & D expenditure is expensed off the P & L Account. For EVA purpose R & D outlays are capitalized and then amortized over the estimated benefit life (say, 3 to 5 years) of the R & D outlay.

- **Goodwill:** under accounting standards goodwill is amortized over (a fairly short) period. In EVA goodwill is (usually) taken as perpetual intangible asset. Thus for EVA adjustment the amortization amount of goodwill is added back to NOPAT and the cumulative goodwill amortization is added to equity.

- **Pre-project Costs:** in sizable projects there is often a fairly long *gestation period* (period between conception and commissioning – during which expenditure takes place but there is no output and income). In most accounting standards these expenses are capitalized. EVA treats such long-gestation investments differently. Such pre-project expenses are accumulated in a Suspense Account till the project is commercially commissioned. The EVA is not affected by such expenses. The accumulated suspense account balance plus the original investment shows the full opportunity cost of the investment.

- **Expenditure Classification**: large expenses are incurred in employees training and development, brand building, customer relations, channel restructuring, advertising campaign, market share growth with projection of long term benefits. In accounting such outlays are expensed off to current P & L Account. In EVA system they are capitalized and amortized over a reasonable period.

- **Depreciation:** for assets with long life, use of straight line method of depreciation (usually adopted in GAAP and other accounting standards), in computing EVA tempts management to make do with ageing 'cheap' assets in spite of reducing efficiency and creates a bias against new investment. The use of some other method like sinking fund method, where the annual depreciation charge is small initially but rises over the life of the asset may mitigate this distortion.

- **Restructuring charges:** in GAAP (and perhaps most other accounting standards) restructuring charge is treated as a loss and leads to reduction in reported earnings. But restructuring is done for a more productive deployment of capital. This reduction in capital, as a result of restructuring, is treated as a debit to income. But EVA would treat this reduction as a restructuring investment (asset) in the balance sheet, which may be amortized over a period which would be taken care of by the cost of capital saved on the assets which have been removed and by the increased earning as a result of restructuring.

- **Taxes:** companies use written down value (WDV) method for tax purpose. But they use the slower straight line method in their accounts for shareholders. Thus the provision for income tax used in accounting income statements (book taxes) differs from 'cash taxes' actually paid by the company. Actually, the 'book taxes' show what the company would have to pay if it used accounting earnings on its tax returns. In accounting, the difference between 'book taxes' and 'cash taxes' is taken to a liability account (deferred tax account), for payment in future which payment often does not happen. In the EVA system, NOPAT would be computed by deducting only the cash taxes actually paid. The amount held in conventional accounting in 'deferred tax liability account' would be treated as quasi-equity and included as part of shareholders' funds.

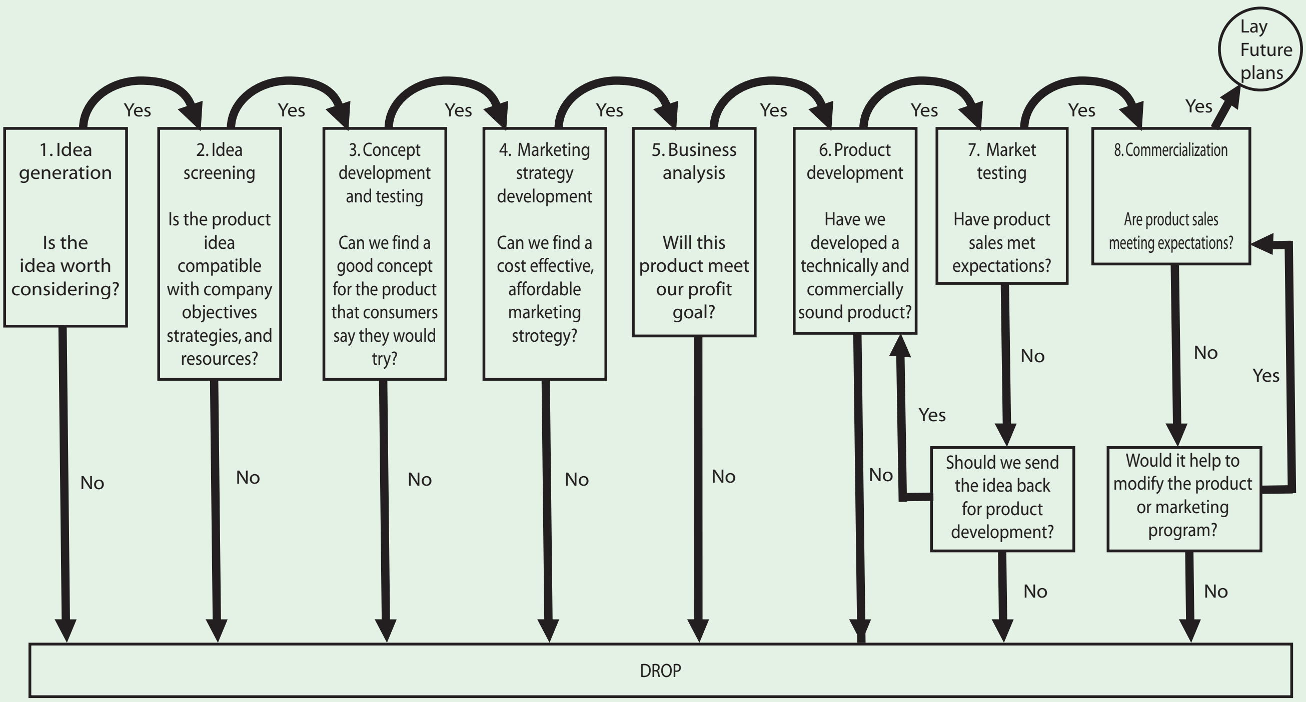
- **Marketable Securities:** regardless of their accounting treatment, in EVA the investment in marketing securities held by a Company is excluded from capital employed in the firm. Similarly, the income from these assets is also excluded from the NOPAT.

Summing Up

Our core interest in this paper is 'accounting for intellectual capital'. In 'accounting' and 'accounting for' any asset we need to have a measure of it. We must put the asset in the balance sheet at a 'value' with a monetary measure. We must also reflect the return on the asset in the income statement. Therefore its measurement is essential. In the case of intellectual capital the asset is intangible with its special problem of valuation. When it is a pure intellectual company like software or music, the whole of the capital is intellectual. The task is simpler. But there is a varying component of intellectual (knowledge) capital in every company. We have noted how the competitive edge of a company is supplied by intellectual (intangible) capital that it constantly builds. The company valuation is most certainly enriched by its technology, structure, business processes, employees quality, smooth and livewire supply chain, R & D, brand image (equity), patents and rights acquired or generated, customer relation, market share, sales force skill and professional excellence. These are hidden assets built and nursed at a cost which work side by side all the time enhancing the visible returns on the physical and financial assets of a company, and wherever possible reflected in the disclosed accounts.

Obviously, thus, the problem exists for their identification, separation, measurement and the treatment in our (conventional) accounting. The Models presented in the paper (hopefully adequate albeit abridged due to concern for space) ought to assist the manager or the CMA in *three* important ways:

- First, they should help identification, separation and valuation of specific kinds of intellectual capital or intangible assets in required quantitative form.
- Second, they should guide the accountant as to whether, and how far, these assets satisfy the conditions, to qualify for reflection in the conventional accounting statements as per current financial reporting standards.
- Finally, the treatment in this paper has kept a constant eye on the balancing between 'relevance' and 'reliability' of the present generally accepted formats of presentation of financial statements.



ACCOUNTING FOR INTELLECTUAL CAPITAL: SOME CONSIDERATIONS

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Typicality of Labour-Scarce Economies

The labour-scarce economies of the West, particularly the USA, UK, Germany and France, have witnessed a growing concern among corporates about how not to waste resources in indifferent qualities of labour and management. Increasing urges to remain ahead of competition especially in the highly slippery world of business have made them cautiously optimistic about conducting their affairs. To remain ahead, industrial, commercial and service organizations have been increasingly emphasizing on creativity, ingenuity and innovation on one hand and new products, new end-uses, new inputs, new processes and new market on the other, and all that is required to be avant-garde. The din and bustle of the competitive world has relegated some of the major objectives that corporates strive for attainment. That there are different meeting points as between the labour-surplus and labour-scarce economies is not always taken into consideration, for developing the relevant rationale in this context. If one were to count the fundamental objectives of all corporates everywhere on one's fingertips in addition to those listed in the MOA, the following would automatically find some place:

a. To make a deliberate attempt to enlarge markets all around so that people in the milieu had an opportunity to take benefits of corporates' efforts towards creation of utilities that would contribute to betterment of quality of life in real terms;
b. To expand purchasing power of the people at large so that they are in a position to take benefit of the conditions so created which would imply suitable stress on enhancement of employment opportunities, a key factor for realizing the goal of expanded market making these objectives a reality;
c. To make sure that corporations did consciously make for social concrescence among all those concerned, albeit differences in earnings, explained by those in the quality of efforts put in;
d. To ensure that creativity and innovative zeal of individuals in the organization did not clash with the fundamental objectives of the company even in conditions of keen competition, pressures exerted by competing organizations, shareholders and others directly or indirectly connected with corporate operating results;
e. To establish congruity between different apparently contradictory corporate objectives and social objectives, generation of income and employment and making good sense out of environment protection and profit;
f. To formulate long term strategies and objectives, appropriate policies and tactics in consonance with the aforesaid which would require a virtual paradigm shift so that the business in effect becomes equivalent to servicing the environment; and
g. To delineate the accounting typicality and specific requirements of different classes of intellectual capital - some formalized in the form of cognizable distinctions like patents or copyrights or trade marks – while some others that are yet in the formative stage and are still in the process of experimentation, but showing high promise.

[The accountant of the future would be required to deal with a bellicose atmosphere putting to test the acuity of his approaches for satisfying competing demands within and outside the organization, so that the whole regimen of the intellectual capital, nay intellectual property rights, yields returns. Tradability being a test, intellectual capital would, it is hoped, find a more solid base allowing the accountant some space to attribute value and calculate return thereon on a regular and systematic basis. It is relevant to mention at this point that intellection rather than imagination would serve as the kingpin in this respect, though the signal contribution of imagination for triggering the intellection process is not to be undermined.]

Some Definitional Issues

Intellectual property and intellectual capital are often used synonymously. In exact terms, intellectual property used for earning further income may be called intellectual capital. Intellectual property embraces many types of innovation, mental activity, creative or artistic effort. The truth of truths is that companies do not innovate, people do. It is therefore important for companies to get into its fold the innovative people, create the ambience by giving them a long rope and cash in on the path-breaking findings that their efforts may bring forth. Innovation is said to that rarest of prizes, often elusive and always difficult to conjure up. Many a time innovation may turn illusory but when it does take shape and becomes visible, it carries the potential of changing one's ways of looking at things. The last decade has witnessed revolutionary changes in the way of life of the people with impacts unrestricted as between countries and as between the rich and the poor. It may be in an intangible, covert, form such as the knowledge and know-how developed from research and experience, and it may be in a tangible, overt, form such as inventions and patents. Reputation of a company built over the years and getting into closer touch with the customers for knowing and acting on satisfying their tastes in a constantly changing environment is also a result of innovation which has been pervasive enough to make one search for its manifestations in different forms and contents; more than all the manifestations, the focus has been increasingly on the source of such innovations, the world of all kinds intellectual activities from which innovations emanate. This is called intellectual property or intellectual capital. It is a truism to suggest that intellectual property is something owned or possessed, and over which there is some measure of control. Its commercial usefulness and provision of adequate exclusivity for giving a business a real competitive edge are the hallmarks. Patents and brands are burning examples of intellectual property, nay, intellectual capital. But patents and brands are not all and even the exclusivity that patents or brands brings forth may not always be a true index of the intellectual capital, for the patents and brands may be either overvalued or undervalued, depending on the bargaining power of innovators and the actual worth that a patent or a brand may command in practice. As far as a patent owner is concerned, he does not have an immediate or automatic right to practice the innovation for his benefits, though he may have a right to exclude others from his patented invention but he may legally use, make or sell the patented invention if no other patents are infringed by his doing so. Even as regards invention, there are conditions that remain attached in the sense that (i) the invention must not have been publicly known earlier; (ii) it must be a non-obvious extension or technical advance over previous inventions; and (iii)it must have industrial use or real-world utility.

Creation of the Right Ambience

In these conditions, accounting for intellectual capital acquires a new light, encapsulating many variants and emitting the right signals for moving in step with whatever is required to stay ahead of competition. Basically concerned with trade-related intellectual property, the traditional accounting patterns would have to give way to an utterly new format for accommodating a whole series of services, different items coming under the term, intellectual capital, and a wide variety of intangible assets that contribute to the innate strength of the corporate. In general, it does have a choice as to what should be the business of business and how to achieve chosen goals. Recruitment of high quality personnel and, more significantly, retaining such personnel, has meant deployment of significant resources so that such people will have found the right ambience in the organization for putting in their innovative ideas, for developing products and processes, in short, to unleash their creativity that would enable a company to surge ahead of the competition. Intelligence, knowledge and experience, as also the personal disposition of individuals as team members, have come to be regarded as commanding high value worthy of cultivation, nurturing and sponsoring, first on a trial basis and then, as an ongoing phenomenon. Since change is the only constant in the world of business, challenge and response figure in a continuum, leap-frogging being a common denominator, at least for those considered to be thrusters, not sleepers. It is, however, not necessary that such change is restricted to labour-scarce economies, nor is it out of place in labour-surplus economies. It becomes more a question of orientation, as to how intellectual capital is deliberately made relevant to the latter, away from the shackles of the so-called appropriate technology. Mobility from the status of developing to developed status over time is not in fact **barred by limitation**. In the meanwhile, there has been an uninterrupted intellectual capital flow from the developing to the developed countries with little effort to value such capital and to put it in black and white i.e., to account for it. The distinct contribution made by intellectual capital of different descriptions thus goes rather unrecognized and uncomputed. Very recently, some hesitant attempts to quantify intellectual capital have been noted in disciplines other than accounting; these involved a good deal of guesswork generally eschewed by accountants.

But in the years to come, the accountants would be called upon to face squarely a virtual paradigm shift in the sense that the components of cost in a product in the near future would more and more lean towards R&D, intellectual assets and services, instead of the traditional stress on materials and labour. Even Activity Based Cost Management has made quite a substantial departure from the traditional approaches to product costing, applied in banks, hospitals, repair services, etc., areas that suffered considerably from inadequate attention all these years. And now, with the services sector picking up continuously increasing momentum, intellectual capital would surely be given its real, rightful place in the world of business especially in accounting. This may not be merely wishful, for the services sector even in India has accounted for around fifty per cent of the gross domestic product. The share of the services sector is likely to grow further in the years to come, raising the possibility of many off-balance sheet items figuring as notes appended to the accounts, if not promoted to the body of the accounts format. Distinct possibilities in this respect are already visible and intangibles, outstripping the tangibles, have created urges to find the right and sensitive accounting formats as a compulsion.

Premium on Intellectual Capital

Evolution of all these concepts - intelligence, knowledge and wisdom as recharged by experience - jointly and severally, and their use for the organization and the economy at large, has in fact underscored the placing of considerable premium on what has been called intellectual capital. This in fact is a monetized, ramified version of the other three, especially knowledge management, which is yet to promote itself from a rather nebulous state, albeit its receiving wide attention in different intellectual disciplines, each seeking virtually a ringside seat. In the ensuing scramble and a virtual hullabaloo, all that the accountant craves for is what is called pou sto, a basis of operation. Three requirements are underlined in this regard. First, to size up all that comprise intellectual capital. Second, to disaggregate the tangible from the intangible, though no grain-chaff distinction applies here. Third, to attach value to them on the basis of some cognizable criteria, maybe not quite exact but clearly perceptible. Generally, the traditional accountant's sensitivity towards all the changes taking place all around has been rather affected and indecisive, to say the least. Accountancy as a discrete discipline has been sluggish in recognizing the quiddity of intellectual capital and its manifestation in practice, as also in developing duly responsive formats so that management is in a position to know and judge all the related issues in the formulation of cognate strategies with respect to acquirement, retention and utilization of intellectual capital for realizing the organizational goals. This has called for a renewed thrust in an area so far dealt with rather perfunctorily. Due assessment of what goes by the brand name of intellectual capital and the contents, methods and processes of accounting to fruitfully accommodate all of them in accounting formats are areas that should engage the serious attention of accountants with particular reference to the specific components of intellectual capital, the way in which such intellectual capital may find fruition while guarding against its idleness or misuse and the different ways in which these could be brought to book, pinpointing the relevant issues which are several indeed if one were to count them. It is a fact that not all patents, brands and other components of intellectual capital receive the care and attention that could effectively put on track the current operations and enhance the differential value of the company. Accounting for all these different components and highlighting them all could alter the strategic position in the highly competitive market This is particularly relevant in conditions in which a company has to account for a large number of items in each category of those classified as intellectual capital.

Accounting Issues: The Primary Concern

In the aforesaid background of development, the accounting issues are primarily concerned with measuring and controlling intellectual capital, especially optimizing return thereon not only today, but also tomorrow and day after. One peculiar aspect to highlight in this regard is that intellectual capital has to fructify continuously in a non-stop effort. No resting on oars! Rather, like **Alice in Wonderland**, one has to run faster and faster to remain at the same place. To gain further ground, the strides have to be longer. Ramification of intellect and acumination of such ramified intellect have several ifs and buts, insofar as both of them are severely tested in practical terms such as:

1. Patents, remembering all the caveats that come to be attached in considering whether a patent is to be allowed or not, though few patents in fact earn royalties, despite the fact that companies working on their own patents would hardly figure in this reckoning;
2. The period for which the exclusivity applies, giving the organization a competitive advantage;
3. The differential outcomes of such patents till the expiry of the period and the capitalized value of such differential outcomes, in about the same, though not exactly similar way, as goodwill is valued in the accounts, for reflection in the balance sheet; and
4. The legal protection of the exclusivity which shows up in many forms like
   - i. protection against piracy;
   - ii. customer loyalty;
   - iii. distinctive product;
   - iv. process identity;
   - v. product inputs; and
   - vi. product components.

N.B. Expiry of the period of exclusivity and, for that matter of the legal protection enjoyed, may create a piquant situation as to how to deal with the exposure and what should be the responses of the accountant. The exclusivity period may, however, provide vital clues to the accountant for applying accounting principles for purposes of valuation of patents even when patent rights have not been sold out or franchised and are meant for internal use. The following paragraphs make a modest attempt to assess the value of intellectual capital and the accounting issues involved in the process of such valuation. A large number of standards, concerned with measurement and reporting, and country variants have already created a maze through which a clear vision is yet to emerge.

Composition of Intellectual Capital

Patents or brands apart, intellectual capital may show up in practice in the form of trade marks, various distinctive designs, trade secrets and know-how, among others. Each of these spells an advantage for the organization and each of them may contain several individual items with many conditions attached to them. The accountant has got to keep track of each of them for due reflection in the accounts. For this purpose, he has to quantify them and put value to them so that a clear idea emerges. It is possible to deride at the discomfiture that the accountant may have to face but the benefits of such an exercise may be seen almost immediately in terms of a boost in the stock prices. A more common picture of the brands as available in current marketing literature would appear convincing. In fact, brand equity and brand valuation are hot in any discussion on marketing. Brand valuation is in effect inclusive of the protection afforded by law and convention. Companies seek to sponsor, develop and effectively nurture intellectual capital towards developing all these marks of distinction aimed at keeping the company ahead of the competition. Perceptual mapping and scenario planning are essential adjuncts in this respect. Methodological alternatives naturally come under focus in the aforesaid context. Valuation processes are not quite similar in all these cases and a generalized picture may seemingly raise many questions and differences of opinion. Accounting for intellectual capital takes into view all these, among others, which are treated as assets. Maybe the deadwood are considered liabilities to be dispensed with in proper time. In the domain of service as well, intellectual capital becomes apparent as customers show distinctive preference for individuals and companies whose superior quality service virtually entices customers even if it is at a premium. There is a gestation period in all this, as much as there are questions of appreciation and depreciation on one hand, and addition and deduction as shown in the cases of physical assets depicted in the schedule attached to the balance sheet on the other. This appears rather simplistic on the surface. However, several complications are encountered as one gets down to the job of sizing up the practical problems involved in, among others, classifying and categorizing them for valuation on one side and cashing in on them on the other. Alternatives approaches exist in the cases of each of these categories and classes.

The Accounting Issues

The accounting issues confronting the organization are several. First and foremost, the question of valuation. The corporate policy may in fact lay down the manner and method of properly recognizing, delineating and demarcating intellectual capital as between the individual and the organization. Continuous renewal and improvement being the key, **kaizen** for that matter, obsolescence remains a threat all the time. Secondly, valuation of intellectual capital remains a contentious aspect in accounting for intellectual capital. "What has the accountants' knickers in a twist is the difficulty of measuring and managing the chief ingredient of the new economy: intellectual capital, the intangible assets of skill, knowledge, and information … What is at stake is nothing less than learning how to operate and evaluate a business when knowledge is its chief resource and result." Lastly, accountants have not shown the necessary thrust in forging ahead with all the constituting elements of intellectual capital and an agreed basis for such valuation, taking into view that a natural motivation to overvalue such capital may develop unless consciously guarded against. Many methods may come up for assessment of which management may select one for each class of intellectual capital. Such methods may include in the case of individuals:

a. differential contribution of individuals to the success of the corporate;
b. capitalized value of patents licensed to this or other organization for royalties; and
c. a stated number of years' purchase of an agreed number of years' average extra revenue earned from differential market responses.

One remembers in the aforesaid context the royalties earned by the patented 'His Master's Voice' from the gramophone company or copyrights on the publications of stories, novels, poems, songs and essays by Nobel Laureate Rabindra Nath Tagore. On the other hand, brand evaluation and brand equity have remained virtual buzz-words in Marketing , as pointed out earlier, though the thrust here is to cash in on the image created in terms of higher price, higher revenue and higher profit, allowed by exclusivity. In the case of corporate organizations, about similar considerations as applicable to individuals would also apply. But the singular distinction lies in the fact that a company may have developed its patents or other differential features for its own use, or it may use the patented innovations of various descriptions as a franchisee. Microsoft has got several thousand patents that have made the corporation a front runner in its class of operations. But the corporation uses 'Intel' as a franchisee, under contractual arrangements with Intel Corporation. Dow Chemical in 1993 created a job of director of intellectual asset management, having in the kitty of the company in-force patents numbering more than 29,000. Two years earlier, Skandia Assurance and Financial Services appointed the first director of intellectual capital, as indicated later. There are indeed many companies in the USA and UK whose portfolio of patents was heavily loaded. But many of the companies have had these patents rather unused or only partially used. Among the Indian companies having quite a number of patents are Infosys, TCS, Wipro, Biocon, Cipla, et al. Capitalized value of royalties may figure in the balance sheet in which case all of the varieties of intellectual capital may be listed and the methods of valuation as adopted indicated against each. Registration fees and other cognate expenses may either be merged in the value of the patents and other distinctive items or shown as debit items in the profit and loss account depending on the nature of the item, the amount at issue and the period of exclusivity granted. This is rather different from valuation of goodwill, as the accounting conventions underline that value of goodwill does not figure in the accounts except when it has been paid for at the time of acquiring a company or one of its segments or only brands. Unrealized value, as of goodwill, does not figure in the accounts in normal course. In the context of valuation of intellectual capital, the same considerations may be relevant for accounting purposes, save for the fact that in the service sector companies the picture may appear contorted especially in calculating return on capital.

Intangible Assets and Intellectual Capital

Intangible assets and intellectual property are usually known as soft assets of a corporate. Generally speaking, intellectual properties are those created by law. Patents, trademarks, copyrights and trade secrets and brands are instances. Intangible assets, on the other hand, may comprise, among others, reputation, customer lists, distribution networks, research and development capabilities, regulatory compliance know-how (such as that involved in the Sarbanes-Oxley Act and International Financial Reporting Standards compliance requirements - that are quite complicated and detailed - have spelt a virtual windfall for the big four audit firms), clinical trial know-how and manufacturing practices. Intangible assets, as understood in the present context, are rather different from those that figure in traditional accounts, considered fictitious assets. While the former do figure in the accounts, the latter do not. Identification of differential revenues and profits and apportioning them to individual items in the category of intangible assets may often call for hair-splitting distinction, when different products are handled through common outlets or they use the same facilities and the sales revenue in individual cases is not a true index of the worth of an individual item in an accounting period. Apportionment, rather than allocation, may be a convenient approach, though not in all cases. Feasibility constraints would also call for proper accommodation in this context. Depending the size of the amounts, some of these items may be clubbed together with a clear mention of the details for the sake of transparency. It is hoped that intellectual capital would not figure in the same way as human resource accounting did. Introduction of standards for both valuation and reporting may over time add substance to disclosure requirements. Audit of these items has to be truly incisive when these items figure in the accounts. Necessary corroborative evidence may also be juxtaposed to lend credence to the details shown in the accounts. Apparently, all these look rather woolly-woolly, though in fact they are more real than apparent, as they spell the difference between one company and another, in terms of actual accomplishments. They effectively contribute - in a way - to the so-called 'invisible hand'. A major concern of the accountant would in such cases would be to identify such contributions and their sources for purposes of accounting and reporting. The currently ruling opinion in this respect is that accounting does not offer an acceptable ground, though as pointed out earlier accounting principles and conventions have already had such compromises and as long as the accounting policies clearly state the premises, the reporting of intellectual capital may not be found extraordinary.

Partial Differentiation?

In the ultimate analysis, return on intellectual capital over time may account for the success or failure of a company especially in the borderless world of business where no favour is given or taken and where short term profit dictates strategy formulation, albeit in the facade of a long term perspective. The movements in the stock prices could be an indicator of value of the intellectual capital, as is commonly cited, along with several other factors. The problem of disintegration of one factor among the several factors that influence changes in stock prices may be solved by way of applying *partial differentiation,* maybe in the same way as applied to finding factor productivity in Indian agriculture in the district-wise **Farm Management Surveys** organized by the Ministry of Agriculture, Government of India. Not that the same model would be applicable in toto in deciphering the influences of different factors acting as push or pull, but that it helps to find new doors of perception; not only that, the chosen methodology may even be applied to disaggregate the items in the regimen of intellectual assets as they spell differential earnings. The result may be inexact but within a range of approximation, this inexactitude may be accepted by the numerate accountant. This apart, it is necessary to acknowledge that an ongoing concern has nothing to do with the goings on in the stock market. However, it may be found prudent by the management accountant to advise management regarding the reality. It is, however, not necessary to disaggregate individual intellectual capital components for the purpose of external reporting. In fact, acceptance of the concept of fair value in accounts has implied compromise on the part of the accountant as far as he is required to estimate what constitutes fair value. Apart from other factors, it is well-known that in recent years the service sector has already been significant and is gaining further prominence and even in this country, a considerable percentage of the GDP is contributed by this sector, as noted earlier. It is imperative therefore that ways were devised to account for intellectual capital covering both intangible and tangible ones, christened as human capital and structural capital as discussed later.

Quantification of Intellectual Capital: A Case

The case presented here was reported in **Fortune** of October 3, 1994. It must be stressed here that Skandia Assurance & Financial Services, the biggest financial services company in Scandinavia, in its first annual report on Intellectual Capital in 1993 did not present the data in the balance sheet form but the figures were presented in groups such as 'customer', 'process', and 'renewal' along with some financial data. Many companies do collect similar data for internal use, but not for external reporting. Skandia did present a comprehensive view of its intangible assets, highlighting the process of transforming human capital, the source of innovation and growth but not an asset the company can own. The director of intellectual of the company insisted that AFS sought to highlight how effectively the company leveraged intellectual capital rather than to highlight how much of it the company had. In his view, it was less important to find a grand total value of intellectual capital than to develop gauges that showed whether the company was moving in the right direction - creating more of the stuff in the year in question than the past year and using it better. The company saw intellectual capital as human capital and structural capital which remained in a process of interaction. Converting human knowledge and ideas into structural capital, the latter implying the adeptness of the company at generalizing them throughout the company. This process adopted by Skandia AFS helped the company to quickly take advantage of the worldwide trend towards increasing deregulation of insurance and other financial services. Worldwide introduction of new techniques and technology allowed the company to open offices in different countries. Though the product line differed from country to country, the speed of payment was common, allowing the company to surge ahead of competition. The company adopted what it called a 'prototype concept', a collection of software applications, manuals, And other structured know-how that could be easily customized to take account of local laws or support any line of financial products. The company used different knowledge transfer strategies for encouraging cross-border sales, offering products developed in one country to customers in another. Those sales at that time accounted for around fifteen per cent of Skandia AFS's premium income. Though the first annual report on intellectual capital had been a short one and it did not present a complete picture of the correlations between intellectual capital indicators and financial performance, it spelt new vistas not only for the managers but also for accountants. And the top brass of the company promised that all these would figure in the annual report on the intellectual capital of the company. A reference has been made to customization as a concomitant feature of intellection. In practical terms, it characterizes knowledge work - whether it is tax auditing, writing scripts for situation comedy, or designing satellites – and satellites are not only made to order but are also enormously complex, expensive and unforgiving, pointing the finger to leverage what is learnt both from success and failure for doing the job better and faster next time. Since most knowledge is less structured, the company recognized the significance of the context of individual cases. Knowledge, according to the company, took the form of wisdom, experience and stories, not rules; for capitalizing this knowledge would call for turning it into usable tools. Systematic searching for 'tangibilizing' hidden values and new images to describe them were a part of the game. Three principles were to undergird the company's thinking in this regard. First, the value of intellectual assets exceeded by many times the value of assets that appeared on the balance sheet. Second, intellectual capital was the raw material from which financial results were made. Last, managers were called upon to distinguish two kinds of intellectual capital, namely, human and structural. The company underscored that brains were what the company ran on. From the inexact to the exact, precise and usable, were the motto on which the company cashed in.

Finale

The foregoing paragraphs have sought to highlight the typicality of intellectual capital with particular regard to exclusivity in the context of knowledge industries in which the processes of what are termed, mentation, intellection and ideation, superscribed by what is called mentalism, that figure either exclusively or conjunctively with several physical products. Depending on the conditions attached to patents, copyrights or trademarks, the highly relevant question of valuation and determination of differential income from a variety of intellectual capital create a problematic contexture. When there are several patents, etc., with a variety of conditions attached to them, individual valuations create a number of problems with respect to own patents and patent rights bought. The latter is rather easier to account for than in cases where own patents, etc., are the cases in point. The valuation problem apart, there is also the issue of depreciation to be charged against the profit earned, periods and conditionality of each being different. Calculation of differential income arising from each patent, etc., and reporting thereon are fundamental issues to contend with. The nature of the problem and its enormity can be imagined when several thousand patents, etc., figure on the list. Total rethinking on the emerging issues is warranted and acumination of sensitivities to the surge of unforeseen problems would be called for.

References:

1. H. Jackson Knight, 'Intellectual Property "101", What Executives and Investors From **Ideas to Assets: Investing Wisely in Intellectual Property**, John Wiley & Sons, Inc., New York, 2002, p.5
2. Ibid, pp 5-6.
3. Ibid,p.7.
4. Cf**. Thrusters and Sleepers – A PEP Study**, George Allen & Unwin, London, 1965. The study noted that the thruster companies, ahead of the competition, were more interested in improving their lot, adopting different innovative techniques and practices, unlike the sleeper companies that were happy with what they were doing.
5. Perhaps it is not entirely true that accountants eschew practices that were not immediately calculable in money terms. Accounting for different derivatives, the many accounting, auditing and reporting standards seeking to grasp the numerous intangible issues and the financial management models concerned with valuation of companies have pushed accountants in an area where intangibles ruled the roost. Valuation of companies, for instance, has brought into play many a method that could lead to finding the intangibles, including intellectual capital, through a process of elimination, by way of deduction from the total value of a company the working capital and fixed assets. What would remain would be the intangible assets and the intellectual capital. The relevance of partial differentiation suggests itself in this context.
6. Robert N. Anthony & Vijay Govindarajan, **Management Control Systems**, Richard Irwin, Chicago, 1995, p 332.The authors aver, 'Compared to the traditional cost systems, which allocated overheads to products based on direct labor hours or machine hours, the newer systems use multiple allocation bases In these newer systems, the word *activity* is often used instead of *cost center*, and *cost driver* instead of *basis of allocation*; and the cost system is called *activity-based cost system*.' Reference may in this regard be made to Thomas A.Stewart, **The Wealth of Knowledge: Intellectual Capital and the Twenty-first Century Organization**, Doubleday, 2001, more particularly Chapter 14, on Management Accounting for the Information Age, pp. 290–324. See also Terence P. Pare, " A New Tool for Managing Costs," **Fortune**, June 14, 1993, pp. 124.
7. Cf. Thomas A. Stewart, Your Company's Most Valuable Asset: Intellectual Capital, **Fortune,** October 3, 1994, p34.
8. 8 Ibid. p34.
9. 2005 was undeniably a good year for the UK's third largest firm. Its annual results for the year ended 30 September, 2005 showed a 20% fee increase on 2004, bringing its total revenues to 1.28 billion pounds. Its rival Big Four firms all enjoyed significant fee increases on the back of, among other issues, International Financial Reporting Standards and Sarbanes-Oxley. But KPMG's increase was the largest. Cf. **Accountancy**, London, February, 2006, p.52.
10. Thomas A. Stewart, 'Your Company's Most Valuable Asset: Intellectual Capital', **Fortune**, October 3, 1994, pp. 36–42.

At The Helm

Our hearty congratulation to Shri Sudhanshu Dwivedi, Fellow Member of the Institute for taking over the charge of Director (Finance) of Purvanchal Vidyut Vitran Nigam Ltd. (A Government of Uttar Pradesh Undertaking & Subsidiary of U.P. Power Corpn Ltd) Shri Dwivedi holds a post graduate degree in Commerce and a Diploma in Management (AIMA, New Delhi). He joined U.P. Power Corporation Ltd. (Formerly known as UPSEB) as Accounts Officer in 1985, and was elevated to the positions of DGM in 2004 and GM in May, 2012. Shri Dwivedi has now been appointed by U.P. State Government as Director Finance w.e.f. 10th October 2012.

We wish Shri Sudhanshu Dwivedi the very best in all his future endeavours.

Accounting for Intellectual Capital

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Introduction:

Globalization has increased the importance of Accounting and therefore, there is a need of harmonization of Accounting Standards. The CRISIL, one of the credit rating agency of India which states that out of about 600 companies studied in India, almost all of them with few exceptions were found to have resorted various earning management games or window dressing of their accounts by resorting to creative accounting tricks like playing with the figures of closing stock, depreciation and provision for contingencies, Employee Stock Option Scheme (ESOPS) etc. According to one of the senior partners of Stern, Steward Research, The Americans G. Bennet steward III," The real, accounting scandals is not that a harmful of companies like Enron and World Com broke accounting rules to inflate their earning but that almost every company is bending the rules to smooth earnings and meet investor's expectations.

Accounting Intellectuals have an important role to play by developing new techniques rules and regulations so that frauds and manipulations and creative accounting practices may be controlled.

Stakeholders are strongly interested in knowing the real value of the company and organizational intangible assets information. Hence, identifying and valuing the intangible resources and providing that information to stakeholders can be considered as important activity within any organization. There is a need of finding out how companies identify their intangible assets in the company and how they report those values. Hence, identifying qualitative and adequate information reporting practices on "Intellectual capital" in the company's annual report is one of the important aspects in the area of intangible assets reporting companies.

Objective:

Knowledge based organizations have been rapidly growing exponentially in the current knowledge based economy situation. Organizational knowledge is explained using different terms like intellectual capital, intangible assets are the most common terms used in the business world. Intangible assets is the result of incorporating information and know how into a organization's productive activities, including that tacit and explicit knowledge which generates economic value for the company. Intellectual capital valuation and reporting is still an ongoing discussion topic in the accounting and finance literature. Therefore, the purpose of this study is to examine the intangible assets reporting practices used in the country and to understand the differences and similarities of intangible assets reporting practices in different countries. Here, an attempt has been made to understand the concept of intellectual capital, elements of intellectual capital, Intellectual Capital Report and accounting standards relating to reporting of intangible assets including intellectual capital.

Review of Literature:

A Selveraj in his article "Knowledge Management", imperative for business published in the Management Accountant, October,2003 (P-731) concluded that knowledge is more valuable and there is growing need to manage it efficiently to capture its full benefits.

Karamjeet Singh and Susima Weligamage in their article. "Intangible Assets Reporting" practices evidence from selected listed companies in Sri Lanka published in the Indian Journal of Accounting, December, 2009 (PP 35-47) concluded that the term "Intellectual Capital" is still not much popular within the business sector in Sri Lanka and the companies which are holding highest market capitalization do not use the word" "Intellectual Capital" to identify their internal, external and human capital.

Ajay Kumar Singh and Nisha Gupta in their article "Measurement of Human Asset", An Empirical Analysis" published in Indian Journal of Accounting- June, 2008 (P.P.13-22) concluded that the most important contribution that the idea of Human Resource Value can make to the

HR manager is in, making him or her examine the concept of an individual's present worth in terms of future services and the probability that the employees will remain in the organization.

CSV Ratna, in the article "Whither Strategic Value" published in Chartered Financial Analyst, August, 2003(P.17) concluded that IT has expanded rapidly and as more and more people used, IT business started considering it as a vital resource.

Intellectual capital:

Intellectual capital has become an imperative resource for creating economic wealth and the competitive advantage of a firm. It can be described as knowledge that may be converted into value. It may be considered as hidden or invisible assets, which drive stakeholder's value. Intellectual Capital is instrumental in the determination of enterprise value and national economic performance. It comprises three basic forms namely human capital, structured capital and customer capital. Human Capital includes knowledge, skills and abilities of employees. It is an organization's combined human capabilities for solving business problems. Human capital also encompasses how effective an organization uses its manpower resources as measured by creativity and innovation. Structural Capital is everything in an organization that supports employees in their work. Customer capital is the strong and loyalty of customer relations. Thus, intellectual capital of a firm is its possession of knowledge, applied experience, organizational technology, customer relations and professional skills that provides it with a competitive edge in the market.

Intellectual Capital Elements:

The elements of intellectual capital framework consist of three main categories as follows:

An analysis can be conducted to identify intellectual capital elements used in the selected companies with special reference to statement related to intellectual capital.

Accounting For Intellectual Capital:

Intellectual Capital Valuation and reporting is still an ongoing discussion topic in the accounting and finance literature. As per accounting point of view, intellectual capital can be defined as the difference between the value of its tangible net assets and its market capitalization. However, Market Capitalization Value often fluctuates and this definition can be problematic in identifying and recognizing intellectual capital.

Most of the companies in India have ignored the human resource accounting. However, Infosys Ltd has been following human resource accounting. The company has used the Lev and Schwartz Model to compute the value of human resources. The evaluation is based on the present value of the future earnings of the employees and on the following assumptions.

i. Employee compensation includes all direct and indirect benefits earned both in India and abroad.
ii. The incremental earning based on group / age has been considered.
iii. The future earnings have been discounted at 12-96 percent (previous year 13.63%) as the cost of capital of the company.

Table 2 revealed that the value of human capital of the company has increased from Rs. 28334 crore in 2005 to Rs.46637 crore in 2006 which has increased by 65%. The value of human resources per employee has also increased from Rs.0.77 crore to Rs.0.88 crore. The employee cost has reduced from 12.49% to 10.29% and the return on human resource value has reduced from 6.52% to 5.32% due to increase in employees.

Intellectual Property:

Knowledge is an important resource and a vital component of the company's products and services. The companies rely upon a combination of patents, copyrights, trademarks, design laws, trade secrets, confidentiality, procedures and contractual provisions to protect intellectual property. Thus, intangible assets have been receiving considerable attention from corporate leaders in recent years. External assets are the market related intangibles that enhance the fitness of the company for succeeding in the market place, i.e. customer loyalty and brand values. The brand value of Infosys Ltd as on 31-3-2006 was Rs.22915 crore which was 28 percent of market capitalization of the company. Thus,

Table–1 Intellectual Capital Elements

Internal Capital	External Capital	Human Capital
Intellectual Capital	Brands	Know – How
Management Philosophy	Customers	Employee
Corporate Culture	Customer Satisfaction	Education
Management Process	Distribution Channels	Training
Networking Systems	Business Collaborations	Work –related Knowledge
Financial Relations	Social Responsibility	Entrepreneurial Spirit

Sources, Guthrie, Petty & Yougvamich .K and Riccesi F (2003) Intellectual Capital Reporting

Table–2: Human Resource Accounting of Infosys

	31.3.2005		31.3.2006	
Particulars	Employees	Value Rs. Crores	Employees	Value Rs.Crores
Software Delivery	34747	26550	49495	43336
Support	2003	1784	3220	3301
Total	36750	28334	52715	46637
Software Revenue		7130		9521
Total Employee Cost		3539		4801
Value Added		6053		8027
Net Profits		1846		2479
Key Ratios				
Software Rev./HR Value		0.25		0.20
Value Added/HR Value		0.21		0.17
Value of HR Per Employee		0.77		0.88
Employee Cost (HR(%)		12.49%		10.29%
Return on HR (%)		6.52%		5.32%

Source: Annual Report of Company 2005-06

brand equity is the value addition provided to a product or a company by its brand name. It is the financial premium that a buyer is willing to pay for the brand over a genetic or less worthy brand. Therefore, brand, equity is the result of relentless pursuit of quality in manufacturing, selling, service, advertising and marketing.

Accounting Standard and Intellectual Capital:

Accounting standards are written policy documents issued by expert accounting body covering the aspects of recognition, measurement, treatment, presentation and disclosure of accounting transaction in the financial statements. An intangible asset is an identifiable non – monetary asset, without physical substance held for production or supply of goods and services for rental to others or for administrative purposes. AS 26 applies among other things to expenditure on advertisement, training, startup Research and Development activities, Rights under Licensing Agreement for motion picture, video recording plays, manuscript, patents and copyrights. The criteria are that expenditure should provide future economic benefits to an enterprise.

Accordingly, computer software is considered as an intangible asset. An essential criterion for recognition of an intangible asset is identifiable control, future economic benefits and cost can be measured reliably.

Disclosure under AS 26 for each class of intangible asset distinguishing between internally generated and others, useful lives, amortization method, rates, gross carrying amount, description existence and amount of commitments for acquisition of intangible assets. Planning stage expenditure is akin to research cost and recognized as expense when incurred. Expenditure arising onward development stage complying with the development criteria should be recognized as an intangible asset.

Conclusions:

Intellectual capital can be described as knowledge that may be converted into value. It has become an imperative resource for creating wealth and the competitive advantage of a firm. It may be considered as hidden or invisible asset which drives stakeholder's value. Intellectual capital is instrumental in the determination of enterprise value and national economic performance. It comprises three basic forms namely human capital, structural capital and customer capital. Thus, intellectual capital of a firm is its possession of knowledge, applied experience, organizational technology, customer relationships and professional skills that provides it with a competitive edge in the market.

Intellectual capital valuation and reporting is still an ongoing discussion topic in the accounting and finance literature. As per accounting point of view, intellectual capital can be defined as the difference between the value of its tangible net assets and its market capitalization. AS 26 provides for accounting disclosure and treatment of intangible assets in India. Most of the companies have ignored the human resource accounting aspect. However, Infosys Ltd has used the Lev and Schwarts model to compute the value of human resources. It is based on certain assumptions. External assets are the market related intangible that enhances the fitness of the company for succeeding in the market place. i.e. customer loyalty and brand value. The brand value of Infosys Ltd as on 31-3-2006 was Rs.22915 crore, which was 28 percent of the market capitalization of the company.

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Accounting for Intellectual Capital: A Case Study of Select IT Companies in India

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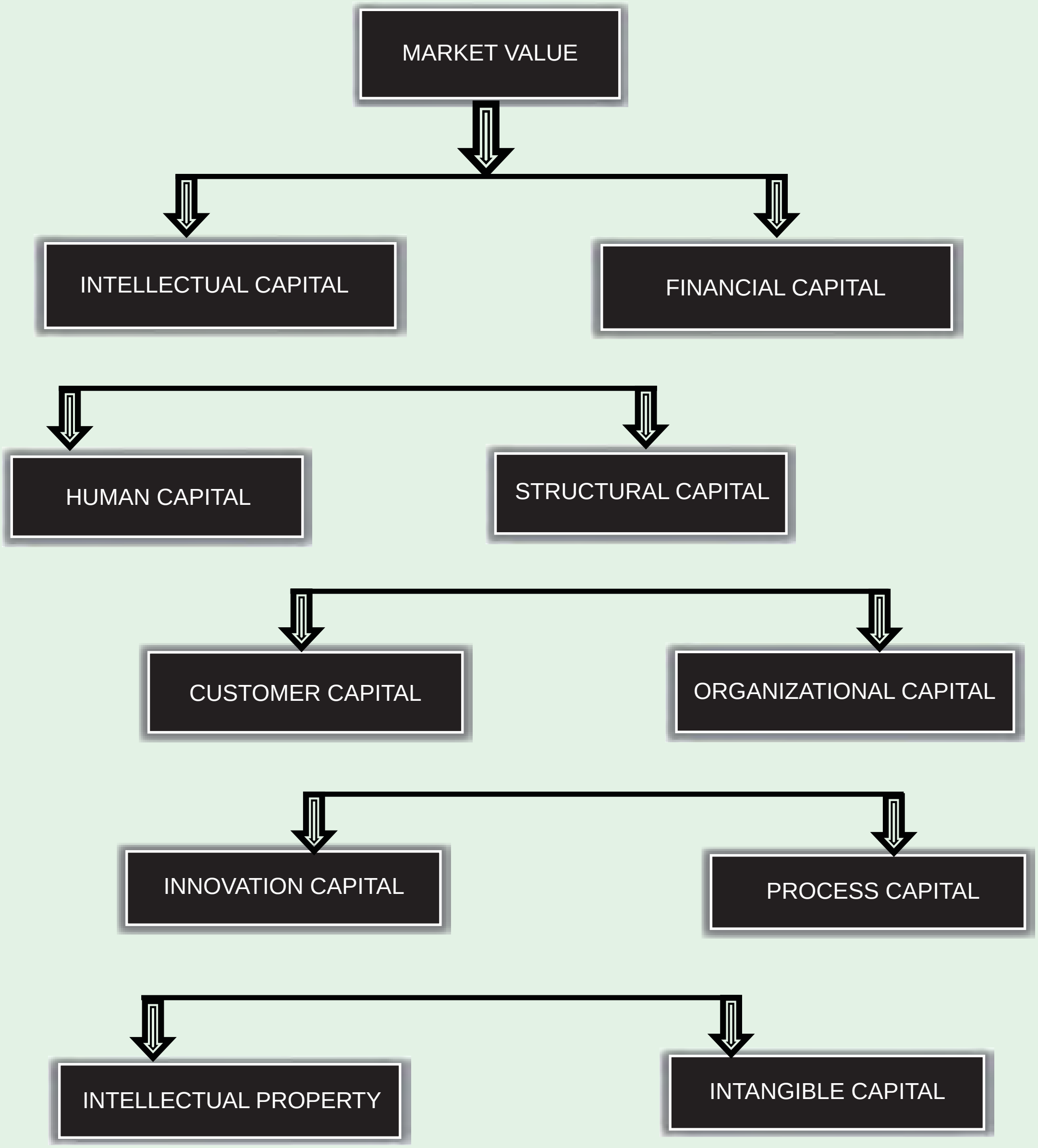
Introduction

Today's business world is becoming competitive and complex with rapidity. In this complex situation sustainability becomes the main challenge for an organization. Companies are now trying to be more flexible and innovative in their operations and strategies. Businesses are being conducted based on new economic models. They seem to be depending more on intangible assets than on traditional hard assets. These intangible assets are often termed as intellectual capital. Intellectual capital is the intellectual force or capability of an organization that drives the other productive resources and adds value to the business structure. Most common forms of intellectual capital (IC) that exist and work for an organization are human intellect or knowledge, relational attributes and structural capital. These core components of IC allow organizations to execute their strategies to achieve better business performance. It originates from the coordination between an organization's human capital, its innovativeness, and competencies to enable it to make differences in the market place. With time global economy is also changing. It is becoming more dependent upon service driven industries than on traditional manufacturing industries. Besides that business environment is now becoming knowledge based and intellectual capital oriented. As a result, the service driven companies are finding enormous niches to explore and fit into the current market place. And they are mostly dependent on their intellectual capital than on the conventional asset structure. Thus it is quite imperative now for the companies that are depending mostly on intellectual assets to develop and encourage practices for valuation and accounting of intellectual capital to report their periodic results to the investors more clearly. However, it is at the same time also inevitable that intellectual capital at the organizational level has different forms and identities. It is not only the individual knowledge that works as intellectual capital for an organization but there are other varieties too, such as organization culture, customer relation, managerial prospects etc that are generally rooted deep in the organizational structure and collectively determine the way in which an organization should proceed and thereby constitute the elements of IC in an organization. Thus, IC refers to a set of intellect based assets which helps an organization in developing competitive advantages. From accounting perspective IC has its own importance and significance. Nowadays, companies should have genuine philosophy regarding their intellectual capital to survive in market competition. Therefore, IC is not merely an asset like all other usual assets that an organization generally holds, but it is something extraordinary that has enormous value impact for an organization today. The following exhibit 1 identifies how intellectual capital exists in different forms in an organization and how it combines the other organizational components to create a strategic alliance among all parts of an organization to facilitate various organizational activities as per Skandia's model:

From the above exhibit it is clear that the value of a firm depends upon its financial capital and intellectual capital. IC represents a composition of human capital and structural capital of an organization. Structural capital is formed by the two important factors viz. customer relation and organizational trust. Customer relationship includes all forms of relationships that a company generally holds with its customers. It includes customer loyalty, customer satisfaction, company name and image etc. And on the other hand, organizational capital can be built through innovative ideas and technological expertises. The example of such capital may exist in the forms of licensing arrangements, financial relations etc. Again for generating

Exhibit 1: **Skandia's model of intellectual capital**



innovative ideas and strategies two things are must- one is intellectual property and the other one is intangible capital. Some of the key components of intellectual property are know-how, technical expertise, and problem solving capability i.e. creativity and entrepreneurial skills. Culture, on the other hand, is of fundamental importance for creating intangible capital because it provides an organization the ultimate framework in which it operates as an independent entity, in order to achieve the overall objectives.

Since "intellectual capital" has become the new buzzword in business world today, this paper aims at examining the current practices of intellectual capital measurement in India through a case study on selected Information Technology (IT) companies in India. IT industry is well-known for its intellectual capital. It is one of those industries which rely mostly on intellectual capital rather than on other traditional hard assets and hence the focus is on IT industry here.

The remainder of the paper is organized as follows. *Section 2* sketches the objectives of the paper. *Section 3* discusses the research methodology of the present study. Time series analysis and cross sectional analysis on intellectual capital valuation of the concerned companies have been done in *Section 4 and* an elaborative analysis on accounting procedures for IC by the selected IT companies is done in *section 5*. Finally, recommendations are drawn in *Section 6*.

Objective of the Paper

The *general objective* of the paper is to examine the present state of intellectual capital measurement procedures in an intellectual capital based industry of India. *More specifically,* the paper attempts to:

- explore the amount of intellectual capital owned by the selected IT companies in India;
- identify the accounting aspects of intellectual capital by such companies;
- identify problems of valuation and accounting of intellectual capital, if any and suggest policy measures;

Research Methodology

The study is primarily explorative in nature. The *explorative* part is based on the existing literature on the subject. This includes the discussion on the concept, scope and components of intellectual capital. To corroborate the explorative observations, a sample of three leading IT companies ***(Wipro, TCS and Infosys)*** is drawn from the IT industry of India. The focus of the case study is on firm level analysis, for which financial data are being collected from the websites of the concerned IT companies and other relevant secondary sources. A time frame of three years from ***2009-2012*** is selected to make a time series and cross sectional analysis between these companies regarding the valuation and accounting measures taken for their IC. Though there are several other methods such as Return on Assets (ROA), Direct Intellectual Capital Method (DIC), and Balance Scorecard etc available for valuation of intellectual capital but here, Market Capitalization Method (MCM) method is taken to value intellectual capital of the selected IT companies just because of the fact that it is based on the capital markets premium and can invariably signify the positive difference between a company's market capitalization and its shareholders' equity as the company's intellectual capital.

Valuation of Intellectual Capital by Some Selected Indian IT Companies

This section makes a time series analysis of the value of IC of the three major IT companies in India viz; Wipro, TCS and Infosys for the time span starting from 2009-10 to 2011-12 and thereafter makes a cross sectional analysis of the same during the said periods. For identifying the amount of IC held by the selected IT companies' three main steps are followed. Firstly, their market capitalization is taken as the main basis. Secondly, their net worth or share holders' equity is considered and thirdly, the difference between their market capitalization and share holders' equity is measured to identify the amount of IC held by them during the said periods. All the amounts are expressed in terms of 'Billion Rs'. Thus, the following exhibit 2 shows the calculation of IC owned by the selected IT companies during 2009-10, 2010-11 and 2011-12 accordingly:

Exhibit 2 Time Series Analysis of Valuation of Intellectual Capital of the Selected IT Companies

Intellectual Capital of Wipro

	2009–10	2010–2011	2011–2012
Market Capitalization	1038	1179	1082
Share Holders' Equity	196.549	240.371	286.163
Market Capitalization — Share Holders' Equity	1038–196.549	1179–240.371	1082–286.163
Intellectual Capital	841.451	938.629	795.837

The above table shows that during 2009-10, the amount of IC held by Wipro was 841.451 Billion Rs. while this went up to 938.629 Billion Rs. in 2010-11and followed by 795.837 Billion Rs. in the last financial year i.e. 2011-12.

Intellectual Capital of Tata Consultancy Services Ltd

	2009-10	2010-2011	2011-2012
Market Capitalization	1527.90	2317.15	2287.6
Share Holders' Equity	184.67	245.05	295.79
Market Capitalization — Share Holders' Equity	1527.90-184.67	2317.15-245.05	2287.6-295.79
Intellectual Capital	1343.23	2072.1	1991.81

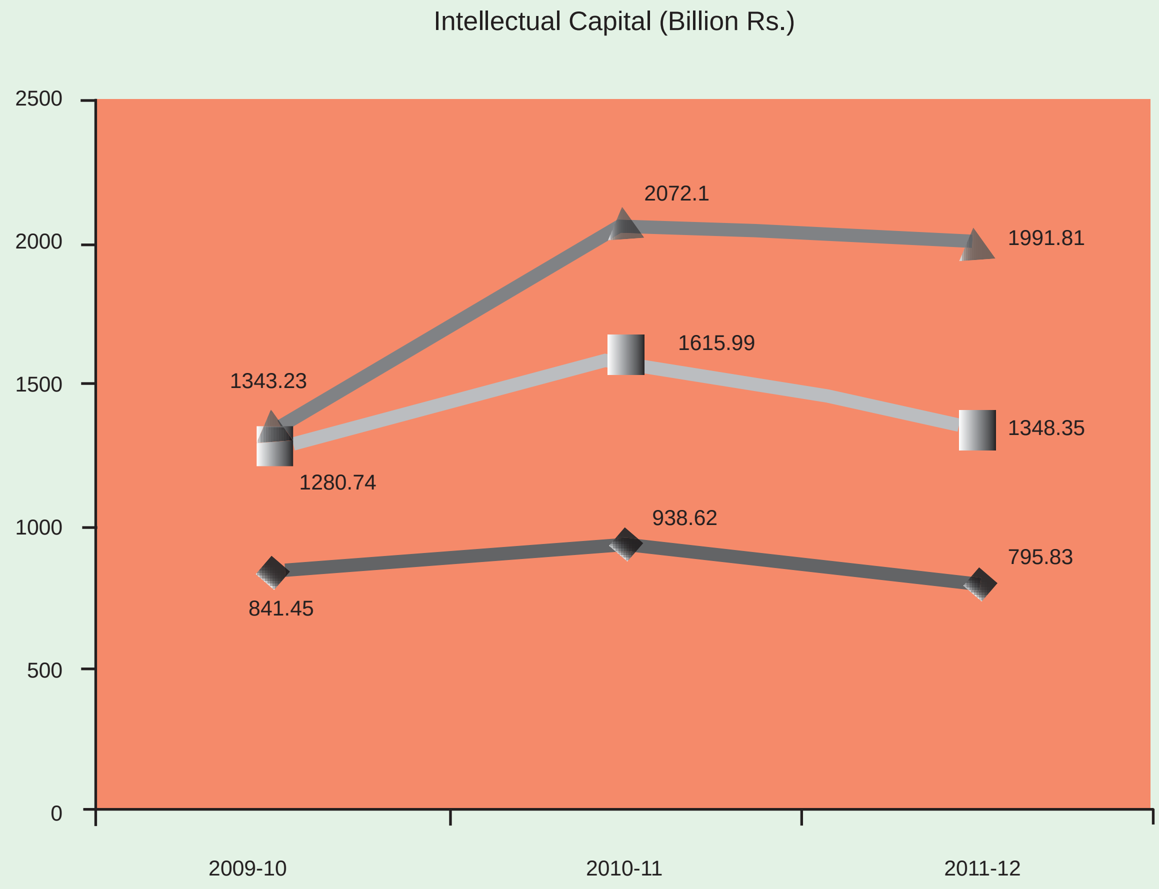
The above table shows that during 2009-10, the amount of IC held by TCS was 1343.23 Billion Rs. while this went up to 2072.1 Billion Rs. in 2010-11and followed by 1191.81 Billion Rs. in the last financial year i.e. 2011-12.

Intellectual Capital of Infosys

	2009-10	2010-2011	2011-2012
Market Capitalization	1501.1	1861	1645.92
Share Holders' Equity	220.36	245.01	297.57
Market Capitalization — Share Holders' Equity	1501.1-220.36	1861-245.01	1645.92-297.57
Intellectual Capital	1280.74	1615.99	1348.35

The above table shows that during 2009-10, the amount of IC held by Infosys was 1280.74 Billion Rs. while this went up to 1651.99 Billion Rs. in 2010-11and followed by 1348.35 Billion Rs. in the last financial year i.e. 2011-12.

Exhibit 3 Cross Sectional Analysis between the Selected IT Companies regarding Value of IC



The above exhibit 3 brings a cross sectional analysis regarding the value of IC of the selected IT companies during 2009-10, 2010-11 and 2011-12. The first trend line from below shows IC position of Wipro for the said time span and the second and third trend lines from below show the trend of value of IC, held by Infosys and TCS respectively for the three consecutive financial years starting from 2009-10 and up to 2011-12. It depicts that though these companies are operating in the same dimension and fall under the same industry, but TCS is in better position in respect of possession of intellectual capital for the examined fiscal years. Since this paper is only concerned with IC valuation and its accounting aspects by the selected Indian IT companies, the reasons behind such variation in IC value of the respective companies are not analysed here and the cross sectional analysis ultimately reveals the fact that there certainly exists some amount of IC in an IT company's assets structure irrespective of its name, business volume, revenues, asset and liability structures etc. Thus, it has been clearly observed that all the three leading Indian IT companies have been vastly depending upon their IC during the examined periods and this analysis certainly proves that IC plays an important role in creating and sustaining business value for these IT companies.

Accounting of Intellectual Capital by the Selected Indian IT Companies

This section reveals the accounting aspects of intellectual capital as followed by the selected IT companies in India. It tries to explore how these companies account for IC in their financial statements to depict the true and fair view of their business. It is already said above that quite often the knowledge based assets are termed as intellectual capital in today's accounting world. Since assets are nothing but the reflection or mirror image of the liabilities in the balance sheet, so every single asset should be supported by the correct and corresponding amount of liability. Therefore, if the positive difference between a company's market capitalization and its share holders' equity results into its IC, then such IC should have some corresponding background or entries in the financial statements to maintain parity with the basic accounting procedure i.e. assets generally have two parts; one is its gradual decrease in terms of utility to be shown in income statement and the other is its future expected benefit to be shown in balance sheet. Now how these companies are dealing with their IC in their financial statements is being described and analysed in the following segment.

Accounting of Intellectual Capital by Wipro

After analysing the financial statements of Wipro Limited for the financial years 2009-10, 2010-11 and 2011-12, it has been observed that Wipro generally shows its IC in different forms in its financial statements. Every year it incurs a huge amount for paying its employee cost as salary which is shown in the income statement. Again the amount spent for employee training and development is shown as a part of training and development cost. Further the company is also observed to be spending a huge amount as a part of its regular product research and innovation. The company clearly shows its patent, trademark, copy rights and other similar kind of intangibles in its balance sheet. It is also found that Wipro is incurring for maintaining and developing its client base which signifies the development of relational capital and it certainly forms an integral part of the company's overall intellectual capital base. Besides that, for maintaining and developing its client base Wipro Limited has been continuously working on different projects like 'Customer Co-Innovation', 'Integrated Cloud Services', and 'Analytics & Information Management' etc. Thus Wipro incorporate its IC in its financial statements.

Accounting of Intellectual Capital by TCS

TCS is highly intended to form an effective intellectual capital base over the years. For this it has taken some policy measures. Intellectual property management programme, invention valuation programme, collaborative mining of invention etc are to mention a few of such steps. However the financial statements of TCS clearly show that the company uses to account for its IC mainly through its profit and loss statement and balance sheet. Instead, the company incurs every year a huge amount of investment for software development, software licensing and for similar kind of intellect based activities. Beside this recruitment and training expenses are done each year for further development and betterment of human capital. For maintaining and developing relational capital a separate expense in the name of 'communication expense' is every year charged against profit. Other intangible assets like patents, copyrights, trademark etc are shown in the balance sheet and the portion impaired or amortised is shown in concerned financial statements as per the specific accounting guidelines.

Accounting of Intellectual Capital by Infosys

Infosys follows a separate strategy to follow up its IC. It is mainly concerned for developing its relational capital through maintaining a strong client base. For doing so it has to incur huge amount every year for developing new infrastructure capital, new processes and new technologies etc. These are nothing but the expenses done for bringing IC into existence. Beside this Infosys follows a strategy for nurturing its intellectual talent also. It considers intellect as an integral part of its business. It nurtures talent by understanding its nature and thereby creates a brand image for its own. This image is certainly forming a part of the company's intellectual capital base. For giving intellect or individual knowledge a right shape like TCS and Wipro, Infosys similarly spends much on training and development of its human capital. Infosys has built up a research and innovation group consisting of technologists and intellectuals for conducting regular research on newer product development and technological advancement and for which it is incurring a good portion of its revenue every year and the technology or IT products developed from this programme are naturally shown in the financial statement accordingly. All these initiatives and acts certainly prove Infosys's attempts in nurturing its IC and accounting aspects of its intellectual assets as well.

Findings and Recommendations

The above study reveals that IC resides in the heart of the IT industry. It mixes human intellect with various other attributes like customers, processes, databases and IT systems together to convert human knowledge into wealth generating resources. Therefore, the present concerns for the IT companies are to identify, manage, measure and protect their IC in a better way. Again it has been found in the above analysis that the selected IT companies are incorporating their intellectual assets in their financial statements in the same way as they include and show their traditional hard assets. However, there is nothing wrong with it to show the yearly amount spent for developing and training for IC in the income statement and the other intellect components as intangible asset in the balance sheet but the questions that are being raised presently can be summarised as follows:

- Is this kind of traditional accounting practice enough to show a clear view regarding IC of the concerned companies?
- Are financial accounting and traditional valuation techniques able to cope with the new value drivers properly?
- Are mere valuation of intangibles and charging of expenses required for developing those assets in the income statement sufficient enough for making IC accountable?

To address these issues what is needed is a modernized corporate reporting framework that will enable IT companies to manage these new intellect drivers in a systematic way. As IC is quite different in terms of its features, elements and nature from the other traditional assets so it is difficult to deal with and therefore, the areas in which the Indian IT industry should take a serious look for accounting of their IC are:

- whether the items capitalized are intellect based or not;
- how organizational culture works effectively throughout the organization;
- identify the factors on which relational capital of the organization is based;
- how the organization is dealing with its human capital;
- how effectively human capital is engaged in order to influence future earning capacity of the organization;
- whether research and development activities are being carried on properly keeping the market demand in mind;
- how innovation is to be brought in to develop intellectual property;
- how human knowledge is being used to combine processes and technologies together to develop new IT products;
- whether the existing organizational structure is in line with the present intellectual skills and abilities;

Thus it can be concluded that the above mentioned points if are taken into consideration further then it may help the IT companies certainly to make their present IC accounting more practical and contextual. However, more and more researches on this issue should also be encouraged to explore more simplification and specification of IC accounting to make it more crucial and significant.

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Notification

In pursuance of Regulation 16 of the Cost and Works Accountants Regulations, 1959, in exercise of powers conferred by sub-section (1) (c) of Section 20 of the Cost and Works Accountants Act, 1959, the Council of the Institute of Cost Accountants of India has removed from the Register of Members, the names of the members vide Notification No.16-CWR (8866–12319)/2012 dated 14th August, 2012 for non-payment of prescribed fees, the details of which are uploaded on the Institute’s website www.icwai.org

Accounting for Intellectual Capital

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Introduction

IP Accounting or intangible asset accounting is gaining importance in today's knowledge based economy as 80% of the global wealth consists of intangibles. The technology and innovation determine the economic growth, the level of job creation and the economic competitive strength of a nation. The same principle applies to a company for its survival and growth as knowledge management has become the key factor in any organization.

The major focus of the success of any organization is counted on the basis of the efficiency of its research and development (R&D), the percentage of turnover spent on the R&D, the number of invention disclosures, the patent applications, the number of patents granted, the number of licenses executed for commercialization and the amount of royalty earned. Thus the shift in approach is happening to look at R&D from cost centre to a profit centre and therefore the need for accounting for intellectual capital.

The Global economy including India is moving from the one based on physical assets to one that is increasingly driven by intangible assets. One of the biggest structural advantages that India is seen to have—demographic dividend—is based on an intangible asset, services sector contributing 55% (excluding construction) of gross domestic product (GDP) compared with 16% for manufacturing, large investments are ought to be made in intangible assets.

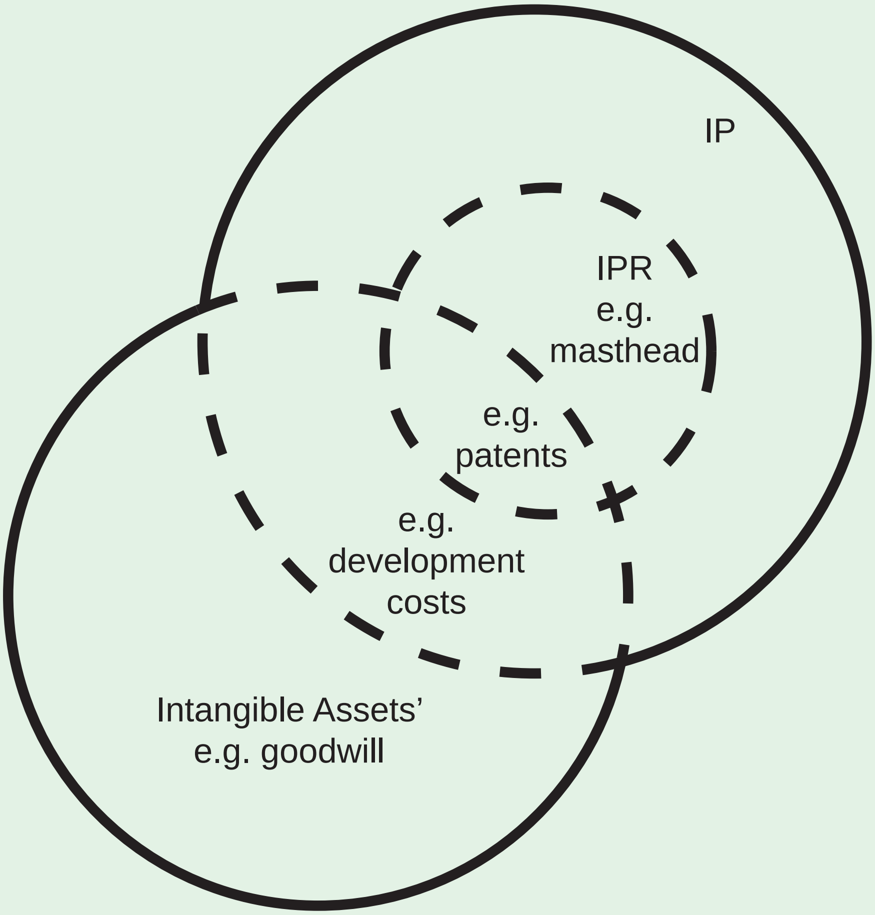
The biggest assets of enterprises today are economic competence, including brand equity, firm-specific human capital, networks joining people and institutions, and organizational know-how that increase enterprise efficiency. However, the policy frameworks and regulatory institutions are still tailored to a world in which physical capital drove growth. Banks and financial institutions are still driven by physical assets based lending, although there is likelihood to provide financial support based on collateralization and securitization of intangible asset.

We are now moving from the Information Age (circa 1971-1991), the Knowledge Age (1991-2002) towards the Intangible Economy (2002-present), whereby the primary factors of production are now seen as knowledge, collaboration, process-engagement and time quality, which put together is called intellectual capital. There are three distinct categories of intellectual capital:–

- Human Capital which includes the know-how, capabilities, skills, and expertise of organization members;
- Structural Capital (or organizational capital) which includes intellectual property (patent, trademark, copyright etc) and infrastructure assets
- Relational Capital includes the connections of outsiders with the organization, such as customer loyalty, market share, rate of new customer acquisition etc.

The value of some leading global companies resides almost entirely in their knowledge capital. It has been estimated that physical assets account for only about 5% of Google's worth. Therefore, it is quite evident that the traditional accounting practice of recording of financial transactions is unable to record the effect of intellectual capital in the financial statements.

The global economic crisis which started in US in 2007-08 after the housing bubble in 2006 and which has further escalated to EU area, has thrown new challenges in the financial sector. Firms are now looking at various other ways to raise capital for their businesses and leveraging intangibles has been one of the ways. RBI recently permitted banks to finance telecom companies bidding for spectrum. This move followed the government's decision to allow telecom companies bidding for airwaves to mortgage spectrum to raise funds



from banks. This new drive by permitting banks to finance investments in an intangible asset such as spectrum and seeking bank's recourse to it in the event of a default, RBI had moved forward on intangible asset financing. Though there are several challenges in leveraging of intangibles and they are –

a. **Recognition** of the intangibles
b. **Evaluation**
c. **Accounting**
d. **Financial reporting**

Meaning and Definition

Accounting is an art and science of recording financial transactions by use of recognized rules, principles, concepts, conventions and standards.

Intellectual Property is defined as an intangible form of property, as opposed to personal property or real property, which is concrete and much more easily defined. IP is the result of the creation of the brain or the mind, which is then manifested or interpreted in a form that has a physical existence and possesses exclusive property rights. Examples include images, symbols, names, designs, industrial processes and business methods used in commerce; inventions; artistic, literary and musical works; and software.

Intellectual Property Rights can be defined as the statutory rights conferred to person or persons for the IP created under various provisions of the law such as patent law, design law, trade mark law, copyright law etc.. Creator enjoys an exclusive right over the use of his/her creation for a certain period of time.

Accounting Standards and Guidelines

First, we will deal with the problem of intangible accounting. In recent time the business entities have started recognising the limitations of traditional, transaction-based accounting and they have been sometimes moving to measure and disclose the 'fair value' of their intangible assets. This, in turn, leads them to use a broader set of metrics, now including measures for customer, human and structural capital. These metrics are derived by decomposing market

Various forms of Intangible Assets:

Type of IPRs	Subject Matter	Duration of Protection
Patent (Patent Act 1970)	New, Non-Obvious (Invention) & Industrial Applicability	20 Years
Copyrights & Related Rights (Copyright Act 1957)	Authorship, Artistic Performance, Phonogram & Broadcasting	Life of the Author plus 60 Years
Trade/Service Marks (Trademark Act 1999)	Signs or Symbols to Identify Goods & Services	8 Years
Industrial Designs (Design Act 1911)	Ornamental, designs for Clothing, Automobiles, Electronics etc	10 Years
Integrated Circuits & Layout Design	Original Layout Designs	10 Years

capital into current and future growth value components, and enables the measurement of future value creation streams. Indeed, there has been no shortage of attempts to develop such stand-alone measurement frameworks, and currently, there are at least 80 different value and performance measurement schemes on offer, of which some of the international standards and guidelines are as follows –

- International Organisation for Standardisation (ISO) - ISO 10668 on Brand Valuation
- IFRS
  - International Financial Reporting Standard - Business Combinations (IFRS 3).
  - International Accounting Standard – Impairment of Assets (IAS 36).
  - International Accounting Standard – Intangible Assets (IAS 38).
- US GAAP
  - Statement of Financial Accounting Standards - Business Combinations (SFAS 141)
  - Statement of Financial Accounting Standards - Goodwill and Other Intangible Assets (SFAS 142)
  - Statement of Financial Accounting Standards - Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144)
- IVS 210 on Intangible Assets was published by the International Valuation Standards Council ("IVSC").
- Indian Accounting Standards, AS 26 (Intangible Asset) and AS 14 (Business Combination)in India
- USPAP are mostly used in US, and they are standards covering the valuation of assets issued by The Appraisal Foundation. Standards 9 and 10 of USPAP 2012-2013, commencing on page U-71 covers the appraisal of a business enterprise or intangible asset.

The above mentioned standards and guidelines on accounting and valuation of intangibles only consider the Intellectual Property Rights (IPR) such as patent, trademarks and copyrights but the competitive intangibles such as knowledge assets, relationship assets remain ignored.

IP Asset Registers

Specific IP registers are ideal for recording registrable forms of IP such as patents, trademarks and designs. Specific IP registers facilitate monitoring of critical dates (e.g. renewal dates) and minimise the risk of the rights lapsing or being placed at risk through unintended activity or inactivity. An additional benefit of a specific IP register is that it provides an understanding of the various IP assets held at a whole-of-agency level.

Maintaining the Register:

An IP register may be maintained by collecting data at relevant 'trigger points' in the lifecycle of the IP. Trigger points include creation or acquisition of IP, registration of IP or product development and contracting. It may be appropriate to assign responsibility to a particular position to update the register at each critical point in the IP lifecycle so as to ensure continuity in record keeping.

Reporting to meet agency needs and other obligations

Information captured in the register may enable agencies to fulfil multiple requirements including reporting requirements. The agency's IP registers need to generate useful information to assist in IP management in order to comply with government and agency requirements and meet the overall objectives of the agency. Reports available from the record keeping systems will usually be tailored to meet the specific needs of the agency as identified in its IP implementation plan.

Disposing of IP Records:

Deciding which records to make and keep is primarily the responsibility of each agency. Apart from strategic and operational needs, there may also be specific legal requirements that agencies must observe.

IP Income and Expenses

IP Accounting involves recording income/ expenses in books. Only IP that generates direct cash flows in a commercial transaction is considered for accounting purposes. The main source of Income from Intellectual Property come is Royalty & Fees for Technical Services. There are four elements in IP Accounting as discussed below:

a. Revenue Income: Income arising due to transfer of right to use IP without corresponding transfer of the ownership in IP e.g. in the form of licensing amounts to revenue income from IP.
b. Capital Receipts: Where a taxpayer sells part of their fixed assets the receipt will generally be on capital account. For example, in case of transfer of technology/ assignment capital gain arises.
c. Revenue Expenses: Expenses incurred on Research & Development of IP until it fulfills the criteria to be recognized as an Intangible asset are revenue in nature and to be charged off to Profit & Loss Account.
d. Capital Expenditure: Amounts spent on acquiring intangible assets are capital expenditure

Expenditure incurred in Development phase or acquisition of patent or other intellectual asset is capital in nature and to be shown in Balance Sheet of the company as an Asset.

Accounting Standard (AS) 26, 'Intangible Assets'

Standard is applicable from 1-4-2003 and deals with the features for recognition of intangible assets on the two criteria namely –

i. Research phase and;
ii. Development phase

Broadly speaking, the expenditure at research phase is charged to revenue. However, an intangible asset at the development phase of the research may be recognized based upon its technical feasibility on the basis of the invention disclosure and its patentability study, based upon novelty, inventiveness and commercial or industrial applicability. These types of intangible assets are recognized as internally generated asset have to be distinguished from other acquired intangible assets.

The standard also specifies the rule of amortization which is generally spread over a period of ten years. According to AS 26, the intangible assets can be classified into following categories –

- brand names;
- mastheads and publishing titles;
- computer software;
- licenses and franchises;
- copyrights, and patents and other industrial property rights, service and operating rights;\
- recipes, formulae, models, designs and prototypes; and
- intangible assets under development

Recognition of Intangibles

Legal intangibles that are developed internally are not recognized and only if purchased from third-parties are recognized. Most of the firms do not record the value of the brands and goodwill in their balance sheets because they are largely internally generated. As a distinct type of intangible asset, goodwill would come in for example in an acquisition, where it represents the amount of money a company has paid or would pay over the fair value of the net assets to acquire another company. Under IAS38 and IFRS3 <u>fair value is defined as 'the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction'.</u>

Mergers & Acquisitions (IAS 38, IFRS3-SFAS141 & AS 14) –

Business combinations occur where an acquirer buys the shares of another firm creating a parent/subsidiary structure or the acquirer buys net assets that form another business. In both cases, the goodwill will form an asset in the financial statements of the acquiring firm. Once the acquisition cost has been allocated to acquired assets (including intangibles) and assumed liabilities, any remaining amount is then recognized as goodwill. Goodwill is, therefore, the cost of the business combination less the fair value of the target's assets and liabilities at the acquisition date.

Amortisation of Intangibles

Under IAS 38 intangible assets are classified into –

- Indefinite life: no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity. <u>An intangible asset with an indefinite useful life should not be amortised</u>
- Finite life (same as SFAS 142 & AS 28): a limited period of benefit to the entity. <u>The cost less residual value of an intangible asset with a finite useful life should be amortised on a systematic basis over that life</u> –
- The amortisation method should reflect the pattern of benefits.
- If the pattern cannot be determined reliably, amortise by the straight line method.

- The amortisation charge is recognised in profit or loss unless another IFRS requires that it be included in the cost of another asset.
- The amortisation period should be reviewed at least annually.

Depreciation on intangible assets (know-how patents, copyrights, trademarks, licenves, franchises or any other business or commercial rights of similar nature acquired on or after 1-4-1998)as per section 32(1)(ii) of Income Tax Act of India is allowed at the rate of 25%. Enhanced depreciation of 40% is allowed on plant and machinery which is used in the manufacture of article or thing other than specified using specified indigenous technology subject to certain conditions. Certain assets, such as computer software, enjoy higher tax depreciation at 60 percent. Goodwill is normally amortised over five years.

Capitalisation

IAS 38 specifically prohibits capitalisation of the costs of some internally generated intangible assets, even if they meet the development criteria mentioned above. Such costs must be expensed when incurred and include expenditure on:

- internally generated brands and internally generated goodwill
- mastheads
- publishing titles
- customer lists
- and other items "similar in substance" to the above

Revaluation

Intangible assets may be carried at a revalued amount (based on fair value) less any subsequent amortisation and impairment losses only if fair value can be determined by reference to an active market. Such active markets are expected to be uncommon for intangible assets. Examples where they might exist:

- production quotas
- fishing licences
- telecom licences
- mining licenses

Under the revaluation model, revaluation increases are credited directly to "revaluation surplus" within equity except to the extent that it reverses a revaluation decrease previously recognised in profit and loss. If the revalued intangible has a finite life and is, therefore, being amortised the revalued amount is amortised.

Subsequent Expenses

Subsequent expenditure on an intangible asset after its purchase or completion should be recognised as an expense when it is incurred, unless it is probable that this expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance and the expenditure can be measured and attributed to the asset reliably.

Key differences between AS 26 and IAS 38

In principle, AS 26 is mostly in line with IAS 38. However, there are a few key differences which are noted as below -

- AS 26 assumes that the useful life of an intangible asset does not exceed 10 years. Under IAS 38 intangible assets may have indefinite useful lives
- AS 26 does not permit for revaluation on initial recognition. IAS 38 permits the use of the revaluation model after initial recognition of an intangible asset.
- AS 26 permits only the "cost" basis of recognition of an intangible asset. Whereas, IAS 38 permits an option to choose either the cost basis or fair value basis for initial recognition of intangible assets acquired by way of government grant.
- AS 26 is not clear how to treat subsequent expenditure on an in-process R&D project acquired in a business combination. IAS 38 clearly provides guidance for the same.

Intangible Valuation

Accounting takes care of only the legal intangible and not the competitive intangibles. Competitive intangibles not only create the legal intangibles but also create value and indicate a company's future potential. In a mergers & acquisition deal, a purchaser is willing to pay a higher price than the book value of the company's assets, because he wants to acquire company's important intangible assets. Thus, it becomes imperative to value the intangibles both the legal (for accounting purposes) and the competitive. However, no method for valuation is wholly satisfactory and most require managerial judgement and discretion. Thus:

- Cost approach asks: how much did it cost to create the brand? Here, the inputs that would be required include design costs, trademarks and copyright. This, however, may understate the actual value of the brand.
- Market-based approach provides indications of value by studying transactions of property similar to the property for which a value conclusion is sought.
- Income approach
  - Price premium method
  - Volume premium method
  - Income split method
  - Multi-period excess earnings method
  - Incremental cash flow method
  - Royalty relief method

1. Top 10 brands, 2008

Reporting of Intangibles

Revised Schedule VI to the Companies Act, 1956 (Act), which, prescribes the format for presentation of Balance Sheet and Statement of Profit and Loss by companies was introduced in 1960 and is almost as old as the Act itself. However, it has been revised keeping in mind the accounting advancements does not provide the fair presentation of the financial information. The revised Schedule would apply to all Indian companies till they are required to follow IFRS-converged Indian Accounting Standards (Ind ASs) from 1st April 2011. However, the revised Schedule does not apply to banking or insurance companies. The revised Schedule VI requires separate disclosure of tangible and intangible assets. The disclosure for fixed assets is to be segregated into:

a. Tangible assets;
b. Intangible assets;

- Goodwill
- Brands /trademarks
- Computer software
- Mastheads and publishing titles
- Mining rights
- Copyrights, and patents and other intellectual property rights, services and operating rights
- Recipes, formulae, models, designs and prototypes
- Licenses and franchise
- Others (specifying nature)

c. Capital work-in-progress; and
d. Intangible assets under development: The (aggregate) amount of intangible assets under development has to be disclosed separately as a separate item on the face of the balance sheet under 'fixed assets'.

Tax aspects relating to Intangible Capital

Income Tax Act, 1961:

Section 2 (14), capital gain is a tax charged on capital assets. Capital assets consist of any property held by an assessee, whether related to business or not, which is used to make money. Thus capital gain is applicable to IP, as well. The application can occur either through a Long Term Capital Gain @ 20% or a Short Term Capital Gain at normal tax rates. It can be exempted only on investments in bonds like National Highways Authority of India (NHAI) or Rural Electrification Corporation Limited (RECL).

Royalty or any sun received by a Non- Resident Intellectual Property Right owner for licensing of IPR is deemed to be Income arising in India and Tax at Source shall be deducted by the licensee from the royalty payable, subject to the benefits of Double Taxation Avoidance Agreement.

As per Section 35(1)(iii):

Weighted deduction of 125% is granted to assesses for any contribution made by any person to:

a. research association which has as its object the undertaking of research in social science or statistical research or
b. University, College or other institute to be used for research social science or statistical research.

Such association, university, college or other institution has to be approved and notified in the Official Gazette, by the Central Government.

As per Section 35(ii)(a):

Weighted deduction of 125% is granted to assessees for any sum paid to a company to be used by it for scientific research. Conditions attached are as follows:

- Company has to be registered in India,
- The main object of the company must be scientific research & development,
- Company has to be approved by the Chief Commissioner of Income tax and
- Fulfils other conditions specified.

Deduction of Rs. 3 lakhs or actual income (whichever is lower) is allowed to authors having Income from writing books being work of literary, artistic or scientific nature as per **Section 80QQB**.

Deduction of Rs. 3 lakhs or actual income (whichever is lower) is allowed to individual having Income from patent registered on or after the 1st day of April, 2003 under the Patents Act, 1970 as per Section **80RRB**.

TDS on royalty and Fees for Technical Services will not only be dependent on the particular payment but will also be affected by the provisions of the relevant Double Tax Avoidance Agreement ("DTAA") which India has with the country to which the payment is being made and the judicial decisions and the Advance rulings on the subject must be interpreted – **Section 195.**

Under **Section 90**, Double Taxation Avoidance Agreement (DTAA), on Interest, Royalty and Fees for technical Services, source country can collect a certain percentage of Income as per DTAA.

An important change has been inserted in existing provision of Section 92B by clarifuing the meaning of International Transaction especially by giving a very elaborate meaning of the term "Intangible asset" under sub-clause (ii) of Explanation to **Section 92B**.

The other tax implication on transactions involving IP Assets or IPR may be on the following taxes namely:

VAT/ Sales Tax:

Service Tax:

Section 65(55b) defines "intellectual property service" as under -

"intellectual property service" means -

a. transferring, temporarily; or
b. permitting the use or enjoyment of, any intellectual property right".

A holder of an intellectual property right shall be liable to pay service tax and shall be treated as an assessee for service tax purposes.

Export of Service is however exempt from Service Tax. In case of Licensing of IPR by foreign owner for use to a person in India, then the service receiver is liable to Service Tax under Reverse Charge Mechanism due to import of service.

Balaji Auto Ltd. v Commissioner of Central Excise (2004) 179 ELT 481 it was held that amounts received towards transfer of technology or royalty is not liable for service tax.

Custom Duty:

Import Duty is payable on imported goods. Goods include all moveable property. However, tariff cover only tangible goods. Intangible Property Rights' value will form part of the value of Tangible goods as per Valuation Rules.

Excise Duty on goods:

Central Excise duty is an indirect tax levied on goods manufactured in India. Drawing & Design relating to machinery or technique are 'Goods' even if payment is made for technical advice or Information Technology, which is an intangible asset. Transaction value: includes the value of engineering, development, artwork, design work, plans and sketches. The Valuation Rules, 2000 will be the basis of valuation.

Stamp Duty:

Transfer of Intellectual Property Rights in the form of License, assignment, sales etc. come in the purview of Indian Stamp Act, 1899. Stamp Duty is also payable in case of IPR transfer from Holding Company to Subsidiary Company. Instrument relating to Sale of Copyright are exempt from Stamp Duty.

Benefits of Intangible Accounting

Recognizing (or even disclosing) the fair value of currently unrecognized intangible assets has at least two major merits –

- Intangible assets as collateral. The value of unrecognized intangible assets is the willingness of lenders to accept such assets as collateral for loans. In a report by Reuters in September 2002, a bank, UCC Capital, has developed a niche by lending money for bonds secured by companies' regular income from patents or fashion logo licensing. Also, major banks have made loans to corporations secured not by traditional assets, but rather by trade names and patents. In at least one case, a bank accepted specific intangible assets as collateral, and determined the value of these assets by appraisal.
- Insured values of intangible assets. The potential losses that threaten the value of IP include infringement, loss of royalty stream, invalidation, unenforceability, or loss of ownership. The amount at risk is the IP value itself,

which is based on factors such as income, competitive advantage, and other intangible benefits generated by the IP. Thus, a formal valuation taking into account all relevant factors regarding an item or portfolio of IP is required to insure its value for a specific amount. The amount determined for IP in the formal valuation may be the amount to be insured. (The value of IP used for collateral on loans could also be insured, providing protection to lenders.)

- Other benefits include
- Improve overall decision-making and effectiveness of management
  - Help in IP due diligence
  - Helps to monitor performance of intangibles
  - Proper Report to Stakeholders can be presented
  - Act as a Guide to Investment decisions
- Proper accounting for IP helps to get tax advantage as and when applicable

Concluding Remarks

In knowledge based economy, human resource play the most important role. According to a World Bank study 64 per cent of the global economic resources comprise Human Resource as against only 16 per cent being Capital resource and the remaining 20 per cent being the natural resource. The intellectual capital is the product of Human resource and therefore there is a need for proper accounting for intellectual capital of all the organizations. Sometimes, an organization is declared sick as the financial net worth is negative under the conventional mode of accounting whereas the organization may have tremendous amount of intellectual capital. Tata group acquiring Land Rover and Jaguar at a price of US $ 2.5 Billion Dollar is a live example for a sick unit belonging to Ford Motors. Therefore there is a need for framing an independent regulating agency for intangible asset accounting similar to cost records apart from mere financial records.

Kolkata, the 28th September, 2012

NOTIFICATION

18-CWR (1627-1631)/2012: It is hereby notified in pursuance of amended Regulation 18 of the Cost and Works Accountants Regulations, 1859, that in exercise of the powers conferred by Regulation 17 of the said Regulations, the Council of the Institute of Cost Accountants of India has restored to the Register of Members, the name of:

1. Shri Senapiratti Padmanabha Krishnamurthy, BA, ACMA, 36, 1st Main, 11th Cross, Prashanth Nagar, Bangalore – 560 079, (Membership No. 4095) with effect from 21st September, 2012,
2. Shri Prem Bhushan Khanna, BCOM(HONS), FCMA, Flat No. 1203, Pearl Court 2, Essel Tower, Gurgaon – 122 002, (Membership No. 5072) with effect from 25th September, 2012,
3. Shri Atul Kinra, BCOM(HONS), ACS, FCMA, House No. 3159, Sector 38D, Chandigarh – 160 036, (Membership No. 7355) with effect from 21st September, 2012,
4. Shri Asutosh Mahapatra, MCOM, LLB, ACMA, Manager (Costing), Birla Jute Mills, P.O. Birlapur – 743 318, Dt. 24 Pgs. (S), W.B., (Membership No. 10713) with effect from 27th September, 2012, and
5. Ms. Pinki Jajoo, MBA, ACMA, 9, Cheyne Drive, St. John's NL, Canada A1A5J6, (Membership No. 18452) with effect from 22nd September, 2012.

(Rakesh Singh)
President

Intellectual Capital Resources as a tool for Realizing Strategic Competencies

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Introduction to Intellectual Capital

Marr and Schiuma (2001) defined Intellectual Capital as group of knowledge assets that are attributed to an organization which significantly contribute to an improved competitive position by adding value to their defined key stakeholders.

Intellectual capital refers to composition of all such assets that are created by the organization out of the significant contributions made by their human assets. In other words, it is sum total of such values that are generated by the knowledge resources of any enterprise that significantly contributes for their growth in form of strategic assets providing them with competitive edge in their existing market space and facilitating in diversifying the same.

Process of Developing Intellectual Capital base

Developing Intellectual Capital base for any organization requires the following.

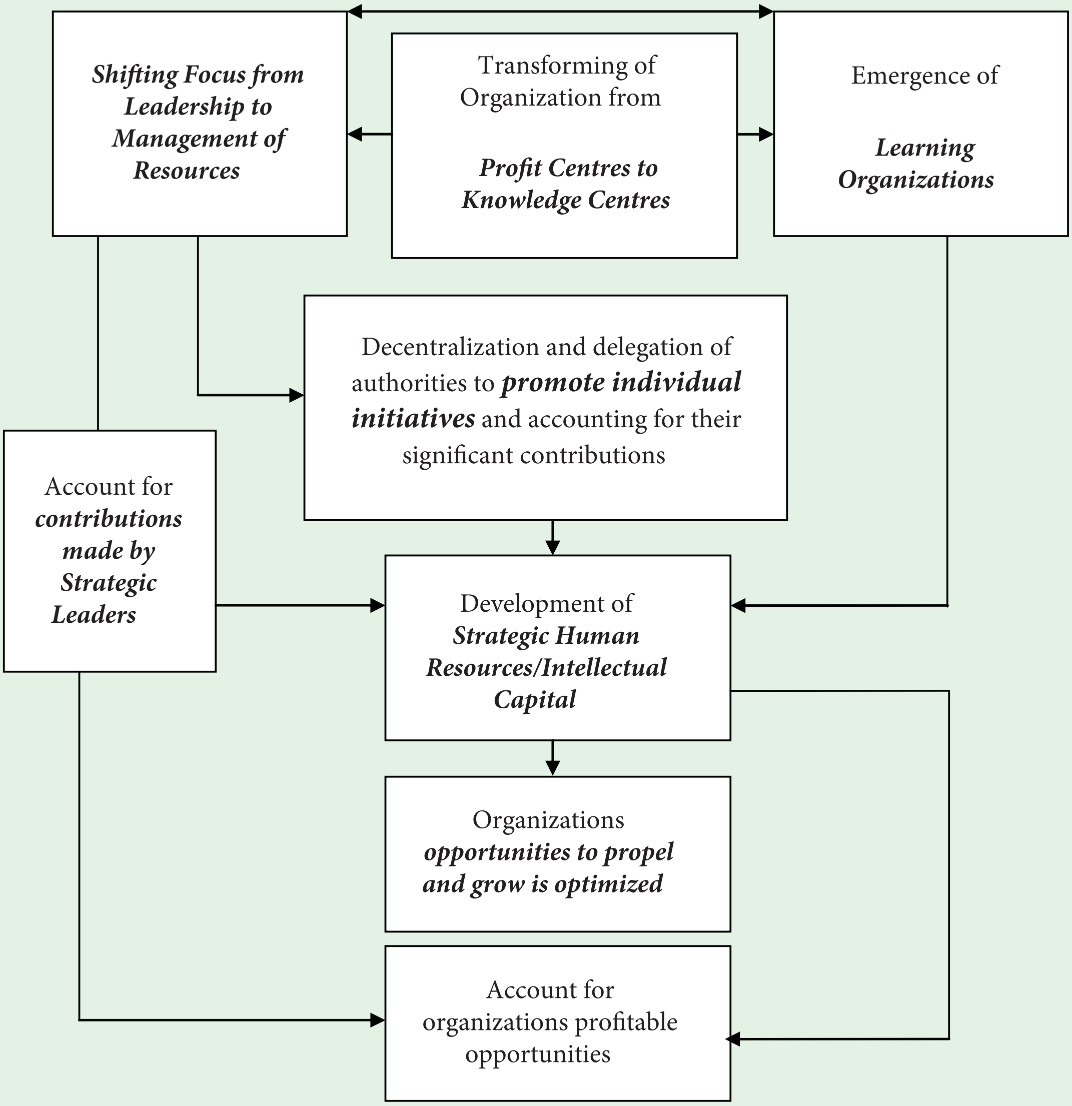
1. Creation and development of Strategic Human Resources
2. Accounting for contributions made by the Human Capital towards business turnaround
3. Providing Strategic position/space for the Intellectual capital resources developed by the organization on their financial statements
4. Transforming organizations into knowledge centres
5. Development and enhancement of quality standards to match global competencies and integrating the same into organizations attitude for providing propelling opportunities for their Human Resources by creating such environment within the organization
6. Providing pivotal importance to the intellectual capital base on the strategic agenda of any enterprise irrespective of their scale of operations

Further, Market conditions in the current context of developments observed – as an influence of free reign economic system is inducing the modern organizations to transform their business centres from a mere profit making centres to knowledge centres for realizing the potential opportunities available for them in the markets both at the domestic as well as at the international levels.

The following model indicates how transformation of organization to knowledge resources centres can help in development intellectual capital resources which in turn contribute significantly for development of strategic leadership, followed by brief evaluation.

A close observation of the above model reveals the following.

1. Each and every organization has to realize the incessant need for development of strategic human resources which can act as strategic assets to contribute for significant development of their intellectual capital resources that can bring turnaround to their operations and add value to their operations, such that, the competitive barriers created by the organization can provide them with all the benefits of sustainable growth and help them to foster to the dynamic needs of the industry/market.
2. Transformation of organization into learning centres and integration of their resources for directing them towards common objectives i.e. to provide for utmost customer satisfaction will provide them with opportunities to emerge as centres of quality with competitive excellence.
3. Every organization will have to develop measures for internal audit to provide for accountability of significant contributes made by their resources within the ambit of their corporate objectives such that, it creates all the avenues for the organization to develop strategic leaders within the organization,



who in turn, can motivate all their resources towards accomplishment of organizational objective. This requires the organization to undertake steps for promoting setting individual objective which in turn has to be integrated into organizations objective in compliance with the industry and market dynamics.

Undertaking steps for development of such strategies within their organizations will help them in development of their strategic assets.

Some Studies and Contributions identifying the importance of accounting for Intellectual Capital (Human Assets) by the organizations

Intellectual capital[1] has to be considered as knowledge resource which has to either created or acquired from the most competitive resources that can help the organization in transforming their internal resources and directing them towards accomplishment of their goals. This requires the organization to create distinguished position for their human resources on their balance sheet and accounting them as intangible assets. All such expenditure incurred for recruitment, selection, training, induction and their development has to be capitalized and the organization will have to see how much of such value created can be written off, or how much of such value has been added to the goodwill of the organization by such resources are also to be accounted scientifically.

Brooking (1997)[2] identified the importance of human capital of the organization and opined that every organization will have to take all the necessary steps to protect the interest of their human resources and account for their contributions to the organization failure to do so, the organization will lose all the competencies that is gained due to their human resources. Wall et al. (2004)[3] identified the need for development of structural capital base by the organizations to incorporate the value of their human capital as a part of their corporate culture which necessarily carry a higher value that their material value and identifies the need for development of measures for creating basis for such valuation scientifically. Roos et al. (2005)[4] shows how human resources/capital of the organization carry higher value along with other intangibles such as goodwill, copyrights, patents (created with the help of superior R&D), and shows how motivated manpower can create value to their operations, which in turn creates value to the organizations stakeholders. Tayles et al. (2007)[5] in his study identifies how human intelligence created as a part of organization strategy to create intellectual capital base by creating harmonious relationship within the organization can help them in fostering to the dynamic needs of the industry and help them in creating customer loyalty as an outcome of relationship building initiated by them to convert their stakeholders in networking partners. Marr and Moustanghfir (2005)[6] in their study show how accounting for intangible stock, i.e. intellectual and knowledge resources by the organization acts as very vital resource for achieving organizational objective, for which they call each and every organization to bring in transformation in their attitude towards their intellectual capital resources that they carry with them in the organization. Philip et al. (2001)[7] in their study identified the perception towards intellectual capital by Irish organizations in light of market volatility experienced by them, and showed how they are considering their intellectual capital (human resources) as a vital resource for creation of organizational value, and further, identifies that these organization were found consistently demonstrating a composition of the human, internal and external components of intellectual capital, especially to match with the global competencies that threaten their operations when remained unmatched.

Lilly, S Martha and Reed, O Ronald[8], in their study identifies the flaws in the accounting standards for reporting intellectual capital on their financial statements, either to treats such expenditure incurred for creation of their intellectual assets base as revenue expenditure or capitalize the same. The study suggests, regardless of acquiring their intellectual capital internally or externally they will have to be valued using comparative values (pre and post acquisition) as the stakeholders most of the times evaluate the performance and assign credit worthiness based only on the organizations reported financial facts. Hence organization while valuing their intangibles (including the human assets) will have to have scientific basis of evaluation as undervaluing such assets will make the value of the organization understated, and further, suggests for development of efficient accounting standards that can help them in realizing optimal value for their operations and create value for the stake held by the stakeholders with the organization. Moolman, Sindiswa[9], in his dissertation work titled ***Intellectual Capital: Measurement, Recognition and Reporting,*** identified the problems faced by the organization in measuring and recognizing intellectual capital in their financial reports and opined that it should not be limited as a requirements in respect of Statutory Disclosures, and only Discretionary and Contextual Disclosures are recommended for organizations operating on any scales, and concluded based on the content analysis that organizations were found using discretionary and contextual disclosures for communicating information regarding their intellectual capital, which is unscientific. Cleary, Peter et al. (2007)[10] in their study developed conceptual framework for identifying, developing and integrating the intellectual capital into the financial statement using structural equation mode, and identified the need for putting it on the agenda of management accounting system. This will help the organization to identify the coefficient relationship existing between the management accounting system present in the organization, development of structural capital to incorporate human assets on the financial statements, and its contribution to business performance. Though the study exhibited coefficient of relationship established to be less statistically significant it was concluded and supported the claim that identification and valuing for real value of the human assets will significantly contribute to organizational competence as shown by a number of earlier works.

A close observation of all the above studies identifies a need for development of Measures/Models for Accounting, Auditing for Measuring the Intellectual Capital of the organization on a broader perspective and not limit themselves in accounting few intangibles on the balance sheet such as Copyrights, Trademarks, Patents, Goodwill etc., but should necessarily account for their ***Human Capital*** so as to determine the quantum of value created over a period of time by them since the time of their induction, and also develop measures as to how to account for expenditures that are incurred for development of such resources for the organization. The following model helps us in understanding the nature and extent of value created by the human/intellectual assets of the organization.

Creation of Human Assets/Intellectual Assets of the organization for Strategic Value Added

A close observation of the above model discloses the following.

1. Each and every organization whose objective is to provide for sustainable competitive positions in the market space will have to have a distinguished position for their human resources while valuing their intangibles (assets).
2. Development of Strategic Human Resources will have to be considered on a pivotal importance for creation of strategic assets for their operations.

3. Every such strategies designed by the organization will have to be necessarily integrate the real value of their human capital so that realistic goals are set which when accomplished can help the organization in realizing their corporate objectives within in the ambit of their philosophies such that their organizations accomplishments are within the values or standards set for their operations.
4. Development of Strategic Assets such as Intellectual Property Rights, to include Patents, Copyrights, Trademarks, Goodwill are within the objective of organization to create strategic value to their operations and should always follow scientific measures as specified by IFRS (International Finanical Reporting Standards) as specified by IASB (International Accounting Standards Board) time to time which requires a necessary convergence with IAS (Indian Accounting Standards) which still is very much in nascent stage in India.
5. Rigorous measures have to be initiated by the organizations for develop internal audit system in compliance with the set external audit standards, to ensure the value at which the Intellectual Capital/ Assets are reported on their balance sheets are not showcasing inflated financial positions. This is very much essential as most of the organizations today are following discretionary and contextual measures to report their human resources on their financial statements, which will have to be made statutory and within the specifications of IFRS (especially for the organizations carrying operations in global markets).

Conclusion

Compliance with audit standards and accounting for value created by the human capital will enhance the real value of the organization and would enhance the credibility among the stakeholders. This will help the organization in enhancing their brand equity in the market and leads to a collinear impact on both consumer market and capital market, which in turn creates long term sustainable competitive positions in the market. Further, valuation of human resources have to be scientific and IASB has to develop measures that can integrate the human capital into the accounting statement so as to protect the interest of the stakeholders by providing transparency for the basis on such valuation. Making reporting of human assets on the balance sheet statutory rather than discretionary as financial statements without inclusion of human assets value will be undervaluing their assets which might lead to irrational opinion towards the organization leaving the organization to underperform both in the domestic as well as in international markets.

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QRB Invites Views / Suggestions

The Quality Review Board invites views and suggestions with regard to the quality of services being rendered by the Cost and Management Accountants either in employment or in professional practice.

The members of the industry associations / corporate / regulators / members in practice are requested to give their feedback in the prescribed questionnaire by following the link given below **latest by 30th November 2012**:

http://eicwai.org/qrb/instructions.aspx

JP Singh

Additional Secretary and

Secretary, Quality Review Board

Intellectual Capital: an Emerging Issue in the Global Accounting Arena

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Introduction

The new millennium is known as economic millennium, which is based on knowledge management. Knowledge is a critical element that changes the business strategy and it has been recognized as one of the most important success factor of a business firm. In the developed economies we have seen a shift from the industrial economy, to a knowledge economy, in which Intellectual Capital (IC) is al precious resource and a key determinant of competitive advantage, economic success and value creation in business firms. In the knowledge-based economy organizations are forceful globalised competition for their survival. With development of technology and information in this millennium has extended change in human life and information relies on observable IC. It is often described as intangible assets for moving towards sustainable growth in values. It is well known that knowledge economy is mainly based on intellectual assets. In the beginning in this millennium IC appeared as a major source of competitiveness for firms. In the recent times, most of the organizations, particularly high tech and knowledge intensive are based on IC. In fact, the good IC system can bring the positive influence in performance of business enterprises.

In this article we will provide an overview of how the topic of IC has evolved in the field of accounting, and then discuss its definitions and the current standards as well as the latest learned thinking. To accommodate the transition into new economic reality, the US Financial Accounting Standard Board (FSAB) and the accounting Standard Board of the UK (ASB) are reviewing the intangibles issue and plan to write new guidelines for reporting on its value. The International Federation of Accountants (IFAC, 1998), for instance, note that the knowledge is the primary competitive factor in business; that it is a non-traditional intangible resource; and that the accumulation, transformation, creation and valuation of this resources lies at the heart of IC management. The Organization for Economic Co-operation and Development (OECD, 1999) describes IC as the economic value of two categories of intellectual assets of a company: (a) Organizational (Structural) Capital; and (b) Human Capital. It plays a potential role in organization's value promotion.

FASB is preparing two guidelines on *"Business Combination"* and *"Goodwill and Intangible Assets"* which will require American companies to periodically determine the fair market value of their intellectual property. Revising the practices and standards concerning goodwill is not easy. There are many controversial and costly reporting issues involved. Regardless of the difficulties, the accounting profession has come to realize that this change must be made. As these standards are accepted and become operational, they will be a major force in moving IC from being an interesting but relatively minor concern to being a major financial reporting and strategic consideration (www.virtuailes).

Objectives of the study

The objective of the study is enquiring that the IC influence the performance of the organization. The specific objectives are as under:

1. To study the measurement of IC.
2. To identify and assess the accounting for IC.
3. To study the effects of IC on organizational performance.
4. To recommend suitable suggestion for the development of accounting for IC.

Methodology

The study is explorative and empirical in nature. The study is based on the data, which are entirely secondary in nature. Secondary data are collected from different source, viz. books and journals, published financial statement, study reports, newspapers, internet, reports of SEBI, FASB, and OECD etc. For analyzing the data, some accounting and statistical tools have been used in the present study. The relevant data have been collected from the annual report of Granules India Limited for the period 2009-10 to 2011-12.

Literature Review

At the beginning of the new millennium many academicians, researchers and professionals are attempting to explore the concept and applications of IC in depth. The concept of IC was first developed by Jon Kenneth Galbraith in 1969.

Bontis and Bontis et al. (2000) pointed at the positive relationship between IC component and industry performance. They also observed that IC is based on various intangible resources such as employees' skill, education, competence, knowledge, brand name, customers' relationship and organization structure.

James Guthrie (2000), in his study "The management, measurement and the reporting of IC" observed that, if efforts are not made towards incorporating the value of intangibles like internal structure, external structure and employees competences into a formalized reporting framework then, many public and private sector organizations, the management reporting and financial statements will become increasingly irrelevant as a tool supporting meaningful decision making.

Chen, M C (2004), in his study "Intellectual Capital and Competitive Advantages: The case of TTY" categorized customer capital as market-finding ability, marketing level and customers faithful and also observed that, both current values of organizations relation and potential value in future. He believes that structural capital can help supportive personal develop intellectual performance and also work performance of organizations.

Marr and Spender (2004), "Measuring Knowledge Assets: Implication of the Knowledge Economy for Performance Management" has pointed out the booms after the two World Wars created sellers' market in most of the developed countries. In this condition traditional cost-focused reporting methods were unable to provide adequate picture of performance. Stakeholders are more demanding, which leads to increasing innovation speed and decreasing product life cycles. Differentiation and innovation become critical and capabilities such as Research & Development, creativity, brand image, copyright and patents are essential to achieving a competitive advantage.

Blaise M. Sonnier et al. (2006), "Accounting for Intellectual Capital: The Relationship between Profitability and Disclosure" their study focused on the relationship between the performance matrices of high technology companies and their level of IC disclosure. They also evaluate the relationship between these variables and level of IC disclosure by traditional sector firms would be insightful.

Anuradha K. T. (2008), "Analysis of Annual Report as an Instrumentation of Intellectual Capital Reporting: A Case Study of Indian Institute of Science" the analysis focusing exclusively on annual report risk capturing an incomplete picture of the amount of reporting organizations are engaging in, and thus an incomplete picture of the practices .

Khalique et al. (2011), in their study "Intellectual Capital and its Major Components" observed that IC is incorporating six major components of IC. They argued that IC mainly encapsulated six major components namely human capital, structural capital, customer capital, technology capital, spiritual capital and social capital.

Intellectual Capital (IC)

IC is **knowledge** that can be exploited for some money making or other useful purpose. The term IC combines the idea of the intellect or brain-power with the economic concept of capital, the saving of entitled benefits so that they can be invested in producing more goods and services. IC can include the skill and knowledge that a company has developed about how to make it goods or services; individual employee or group of employees whose knowledge is deemed critical to company's continued success; and its aggregation of documents about processes, customers, research results and other information that might have value for a competitor that is not common knowledge (techtarget.com).

Collective knowledge (whether or not documented) of the individuals which is used in an organizations or society. This knowledge can be used to produce wealth, multiply output of physical assets, and gain competitive advantage and to enhance value of other type of capital. IC is to be classified as a true capital cost because (1) investment and replace of people tantamount to investment in plant and machineries, and (2) expenses in education and training to maintain the self life which are equivalent to depreciation cost of physical assets. IC includes customer capital, human capital, intellectual property, and structural capital (businessdictionary.com).

In the knowledge-based era intangibles are becoming the dominant value of the organization, which raises the

Table 1: Components and Indicators of Intellectual Capital

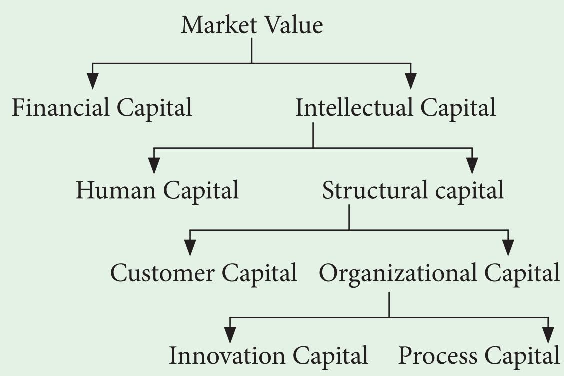
Human Capital (Employee Competence)	Structural Capital (Organizational Capital)	Customer Capital (Relational Capital)
• Knowledge & Skills • Education & Training • Work-related knowledge • Work-related competencies • Innovativeness • Proactive & reactive abilities • Communities of practice…….	• Trademarks • Patents • Copyrights • Business processes • Management philosophy • Information system • Research findings • Corporate culture…	• Customer relations • Customer loyalty • Distribution channels • Favorable contracts • Franchising agreements • Business collaboration • Repeat business….

question of whether the traditional accounting framework is worth its saline either for valuation or for navigating the organization. While the term "goodwill" contains many of the aspects of IC, it has serious drawbacks. "Goodwill" is based on industrial-age business model, when intangibles held considerably less value. Additionally, goodwill is treated as an asset with a limited life and so can be amortized. The thing with intangibles is that they can have renewable value. The knowledge that goes into a piece of software can be used innumerable times without any loss of its value and perhaps with a gain (virtuailes.com).

In recent time technology and process become more significant differentiating factor in the business firms. IC is likely to become an even stronger force in the market place. Some of the subsets of IC include human capital, information capital, brand awareness, intellectual property, etc. The most widely used definition of IC is "knowledge that is the value to an organization". That definition suggests that the management of knowledge creates IC. Its main elements are human capital, structural capital and customer capital. One of the most comprehensive definitions of IC is offered by the Chartered Institute of Management Accountants (CIMA): "The possession of knowledge and experiences, professional knowledge and skill, good relationships, and technological capacities, which when applied will give organizations competitive advantage".

Classification is made for IC into three broad areas of intangibles, viz., Human Capital, Structural Capital and Customer Capital. Some examples of IC are shown in Table 1.

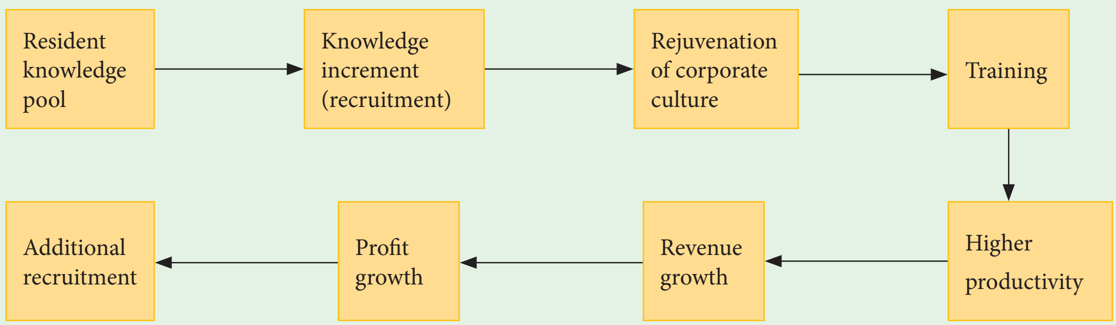
The Granues Intellectual Capital(IC) Model



Human Capital

Human capital is a cumulative collection of employees' experiences, knowledge, training and initiative taking. It is firm's collective capability to extract the best solutions from the knowledge of its employee. It is important because it is a source of innovation and strategic renewal.

How Human Capital Reinforces Business Sustainability



Source: Granules India Limited, Annual Report, 2012

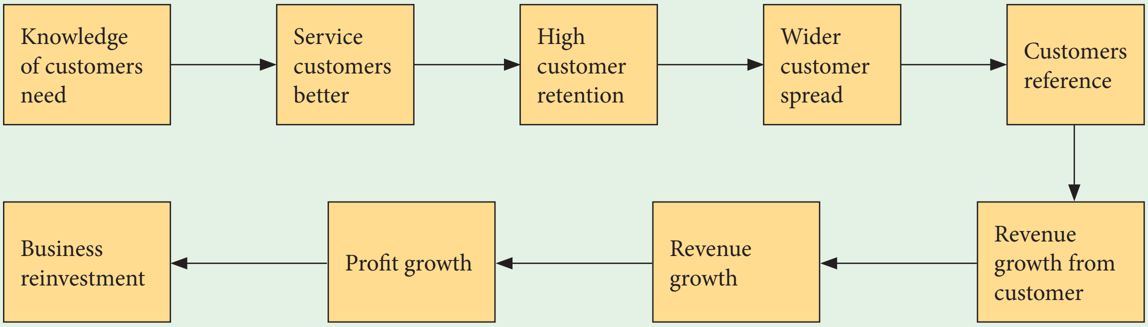
Structural Capital

An investment in assets helps an organization at various levels: entrenches an organization's foothold in regulated markets, improves productivity and helps aggregate, protect and disseminate knowledge. It is facilitated by an investment in a company's structural capital. A company can believe that investment in people must be complemented by an investment in relevant physical assets for the accretion of intellectual to be effective and encompassing. In turn, the effectiveness of structural capital is influenced by the contemporariness of assets, their synergies as well as companies ability to maximize their effectiveness. The structural capital refers to things like proprietary software system, distribution networks, and supply chains.

Customer Capital

Customer capital comprises the cumulative value of customers' relationship, customer loyalty, endurance, accounts size, and revenue predictable among others. Customers loyalty, target marketing, longevity of relationships and satisfaction are all measurable elements of this form of IC.

How Customer Capital Reinforces Business Sustainability



Source: Granules India Limited, Annual Report, 2012

Measurement of IC

The measuring IC is needed for both internal and external purposes. Measuring IC for internal purposes would require effectively manage its resources and cost control. On the other for external purposes would require verifiable information that provide to the existing and potential investors and other external information users of the company to make decisions about the organization. It is difficult to measure IC its existence and benefit should be reported in the corporate reports. In order improve annual reporting and to bring in the benefits of reporting on IC, different studies recommended a number of financial and non-financial measurement models that may be used to measure IC.

IC Measurement models:

1. Financial Measurement Models:
   a. Market to net book value model
   b. Value added approach model
   c. Discounted cash flow model
   d. Comparable transactions model
   e. Avoided cost model
   f. Relief-from-royalty model
   g. Value chain scoreboard model
2. Non-financial measurement models:
   a. Human resource accounting model
   b. Balanced scorecard model
   c. Intangible assets monitor model
   d. Knowledge assets map model
   e. Skandia navigator model

Selected models are discussed as under:

Market to net book value model

The IC is measured as the difference between the market value and the book value of the company at given point of time, (i. e. IC = Market Value – Book Value of company).

Value added approach model

The part of value creation process of business is form IC. Value added model refers to the Economic Value Added (EVA). The additional value of the output is representing the value contributed by the IC assets. The model is thus, a measure of the surplus value created on an investment (Kannan & Aulbur, 2004).

Value Added = Value Output – Value Inputs.

Discounted cash flow model

IC may be measured by using the discounted cash flow model. Under this method the value of assets is determined by using the present value of the estimated earnings that will be generated by the assets after taking into consideration the relative risk of that particular asset, and the discount rate that reflects the time value of money of the company invested. This method is used to measure IC for the annual reporting of the true value of the business.

Comparable transactions model

IC is the part of internally generated intangible assets. Internally generated intangible assets are including brands, methods, customer relation; internet domain etc. according to Olsen et al. (2007), under this model, the value of intellectual assets is based on the actual price paid for assets with functional or technical attributes similar to the subject assets.

Human Resource Accounting Model

Human Resource Accounting (HRA) is the method of calculating changes in manpower of the organization. HRA develops useful management information systems in which cost and benefits on investments on human resources are given special attention. In all sunrise industries, there are adequate systems and procedures to measure costs and value of human resource development. According to Eric Flamholtz defines HRA as "It is the measurement of the cost and value of people for an organization". S. M. Shukla's model takes into account the expenses incurred by the employer over employees, which are grouped under four categories for treatment in HRA.

Expenses on Human Resources

Recruitment | Training & Development | Remuneration | Compensation

The following tables are compiled from the relevant data collected from annual report of Granules India Limited for our study purposes.

Performance analysis of Granules India Limited

Table 2 indicates that revenue per employee increased from Rs.60.72 lakh in 2009-10 to Rs.67.02 lakh in2011-12. Revenue per employee increased from Rs.60.72 lakh in 2009-10 to Rs.67.02 lakh in2011-12. The company's total experience of employees in person days increased from 4206 in 2009-10 to 5209 in 2011-12. Average attrition rate is less than 20% which is better than the industry rate.

Table 3 indicates that the company's overall recruitment increased 27%, there was a marked 45% increase in PG recruitment. As a result the proportion of PG in the overall corporate mix increased from 27% in 2010-11 to 30% in 2011-12. The proportion of Inter & below employee declined 32% in 2010-11 to 30% in 2011-12. The company employed 11 Ph. D. as of March 31, 2012.

Table 4 indicates that the proportion of employees of age 30yr. and below increased from 49% to 64% in the three years leading to financial year 2011-12.

Observations

All tabulated data are collected from the Annual Report 2012, of Granules India Limited. Granules Limited fused its divers companies into generate IC that catalyses organizational growth and prosperity. Employees of Granules Limited is composed of executives, workers and support staff. The company made selective recruitments to address growing volumes, reinforce capabilities and plug up competence gaps. The company's goal is to combine the value-added experience that senior members can bring along with the enthusiasm of young professionals.

The major findings of the present study have been observed, mentioned as under:

- Granules employees increased
- Average age gradually declined.

Table 2: Net sales (Revenues) & Employees Profile (Experience)

Financial Year	Net Sales (Revenues) (Rs. in crore)	Employees	Revenue per employee (Rs. in lakh)	Outside Experience (person year)	In-house Experience (person year)	Total Experience (person year)	Attrition Rate
2009–10	386.2	636	60.72	2335	1871	4206	21%
2010–11	405.7	663	61.19	2457	2070	4528	20%
2011–12	563.0	840	67.02	2888	2321	5209	17%

Source: Granules India Limited, Annual Report, 2012

Table 3: Employees Academic Split of Granules India Limited

Financial Year	No. of Employees	Academic Split					
		Ph. D.	CA/ICWA/CS	PG	Graduate	Diploma	Inter & Below
2009-10	636	4	5	169	228	28	202
2010-11	663	11	4	163	258	18	209
2011-12	840	11	4	237	309	29	250

Source: Granules India Limited, Annual Report, 2012

Table 4: Percentage of Age Profile of Granules India Limited

Financial Year	No. of Employees	Average Age (Yr)	Percentage(%) of Age				
			< 25	25–30	31–35	36–40	> 40
2009–10	636	34	15%	34%	21%	11%	19%
2010–11	663	33	21%	33%	19%	10%	17%
2011–12	840	32	28%	36%	17%	8%	11%

Source: Granules India Limited, Annual Report, 2012

- Revenue per employee increased
- The company's overall recruitment increased. As a result the proportion of PG in the overall corporate mix increased.
- The proportion of Inter & below employee declined.
- The proportion of employees of age 30years and below increased during the study period of 3years.
- The proportion technically qualified new employee increased.
- The company's total experience of employees in person days increased during the study period.
- Attrition rate gradually declined.

Conclusion

The concept of accounting for IC, i.e. measurement, management, disclosure and reporting of IC is relatively new. Traditional cost based accounting information needs to be complemented with information on the intangible value drivers. The IC doesn't appear on the balance sheet but it has more value for organization than physical assets. Managements, policy makers, researchers and accountants have still to struggle with its concepts and detailed application. If managers manage the knowledge effectively, their organization will enhance IC. The performance of the firms can augment or decline depending on how will they create, capture, and leverage their IC.

Suggestions & Recommendations

Accounting and reporting of IC has a very strong impact on the drivers of future earnings, but unfortunately, it is largely ignored in the accounting & reporting practices. Therefore, we recommend that corporate sector must create a culture that emphasis the importance of IC in achieving competitive advantage in the business world. After the study of accounting for IC a strong recommendation, therefore, comes for adopting voluntary IC accounting and reporting practices, especially for knowledge-based firm where competitiveness of the firms are determined by their intangible assets. We also suggest to the professional bodies at national and international level should also join hands to develop a universally accepted valuation system and harmonized approaches for accounting and reporting of IC. It is the best time is grown for national and international professional bodies to develop the understanding and to develop new rules and guidelines for accounting and reporting that will guide them more clearly to a well-off future.

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Measurement and Accounting of Intellectual Capital in Financial Reporting

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Introduction:

In information age, the success of an organization depends on effective use of intellectual capital, as it is a valuable resource like as tangible assets in an organization, growing its importance day to day with tremendous creativity and potential for future cash flows. In some instances, particularly companies in which intangibles, innovation and knowledge were very extensive, the former values were more than the latter. This "hidden value" existed to be accounted for, not least to ensure that its existence did not unduly compromise the operations of the capital markets. The traditional accounting method play an important role in measuring and reporting tangible assets, but these methods in knowledge-based organizations in which knowledge constitutes a major part of its assets, cannot recognize and report the existing knowledge in them. The non-recognition of such assets as intellectual capital in the financial statements may results in a huge difference between the market value of the company as perceived by the investors and the book value of the company as reported in the financial statements, though the value of the intellectual capital of a company is not necessarily equal to the difference between the market value and the book value of the company, accordingly, it has become necessary to conduct a critical analysis of the value of intellectual capital as well as of the challenges in respect of the accounting for these assets. The IASB (2010: A845) states that the difference between the market value of an entity and the carrying amounts of its identifiable net assets may capture a range of factors that affect the value of the entity. A company that has generated goodwill in the form of an internally generated intangible asset is not allowed to recognize this fact in its financial statements as this asset would not meet the recognition criteria of an asset. Hence, it has become necessary to find a way of reporting this value to both the users of information and the capital providers. Unfortunately, this disparity may create the impression that financial reporting does not provide an accurate picture of a company's operating assets. In addition, investors are not able to rely solely on the financial statements in order to make investment decisions. It is the market value that drives an investor's decision in respect of whether or not to invest in a specific company; therefore they need significant changes (Anthony Rojas, 2007). Due to some constrain in traditional accounting standards, practices and principles information relates to intangible assets are not yet treating properly into accounts and reporting into financial statement, specifically the intangible assets which are generated internally (*knowledge, brands, competitive advantage, patents, customer relationships, human capital, research and development, and trademarks*). It is mainly reflected (incompletely) in fiscal notes attached to financial statements (Masve & Smith, 2000), which violet the Accounting Principle of Disclosure, and in consequences of that value of the firm are not properly displayed. In order to adjust the gap between the market value of the firm and the book value of the firm at a reasonable level and represent a reliable value of firm in the financial statement, needs of measuring and accounting of intangible assets has been arisen. This has discussed with the help of International Accounting Standard (IAS 38) and International Financial Reporting Standards (IFRS). For better understanding of the study, intellectual capital has been properly define and classified. Some important recommended models are discussed to measure and reporting of intellectual capital in financial statement.

Intellectual capital: an overview of definitions and classifications

In literature relate to intellectual capital, there are different definitions about this term and thus there is no single and the same definition about it. Some important definitions of intellectual capital are as follows:

- Edvinsson & Sullivan (1996) defined IC as knowledge that can be converted into value for the company.
- Brooking (1996) defined IC as the combination of all intangible assets which enable the company to function.
- IC is, according to Skandia AFS, the possession of knowledge, applied experience, organizational technology, customer relationships and professional skills that provide Skandia AFS with a competitive edge in the market (Edvinsson, 1997).
- Bontis (1998) defined IC as the pursuit of effective use of knowledge as opposed to the information which serves as a raw material.
- Stewart (1999) defined IC as intellectual material: knowledge, information, intellectual property and experience that can be used for the generation of wealth. While these definitions seem to adopt different approaches to IC, some observations are in order with respect to their common elements. IC consists of intangible resources. These intangible resources form a nexus: IC accounting should tackle valuation and reporting issues through the interconnectivity of IC components. IC reporting also has to face the particular challenge that a firm may not always hold proprietary rights over these resources. For example, there are proprietary rights over trademarks but not over the firm's organizational culture or the employees' skills, despite the fact that these IC assets also contribute to value creation.

Classifications of intellectual capital:

Intellectual Capital is a broad concept which is often split into different categories – most commonly it is classified as human, relational and structural capital. A discussion on the three classes of intellectual capital will follow after Figure:

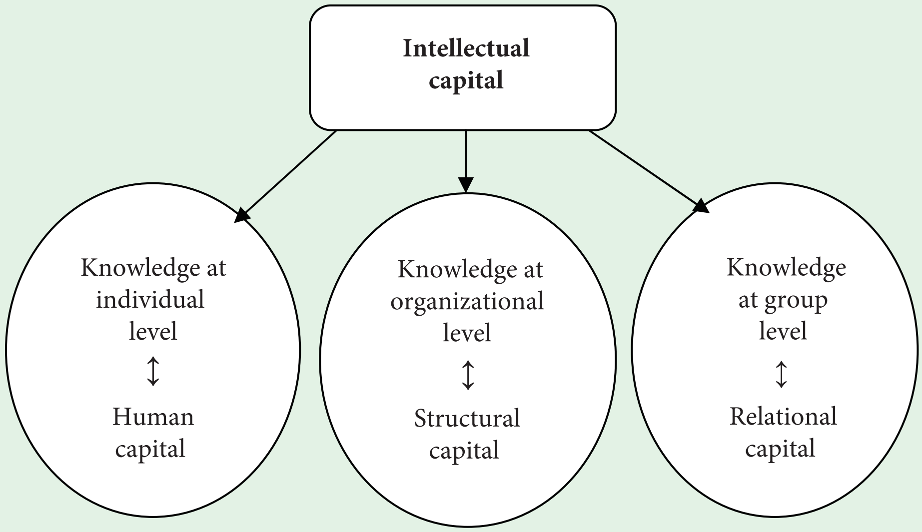
Human capital: Human capital is defined as the knowledge, skills and experience that employees take with them when they leave. Human capital forms the foundation of intellectual capital and without that intellectual capital cannot be implemented (Chen & others, 2004). Without intellectual capital, there is no innovation in products, services, and commercial processes (Riahi Balkauie, 2003). Some of this knowledge is unique to the individual; some may be generic. Examples are innovation capacity, creativity, knowhow and previous experience, teamwork capacity, employee flexibility, tolerance for ambiguity, motivation, satisfaction, learning capacity, loyalty, formal training and education.

Structural (Organizational capital): Structural capital is defined as the knowledge that stays within the firm. It is an institutionalized knowledge that belongs to the organization and is stored in cases such as: databases, instructions. Rus and colleagues (1997) believe that structural capital refers to "whatever remains in the organization when employees leave there". According to them, structural capital covers organizational capital such as: intellectual capital, cultural capital, innovation, processes, and it also includes innovation and expansion of capital like: taking out a patent on products and training efforts. This capital is owned by the organization and although through supporting human capital, creates a good ground for better performance on the part of employees.

Relational (Customer Capital): Relational capital is defined as all resources linked to the external relationships of the firm – with customers, suppliers or partners in research and development. It comprises that part of human and structural capital involved with the company's relations with stakeholders (investors, creditors, customers, suppliers), plus the perceptions that they hold about the company. Examples of this are image, customer loyalty, customer satisfaction, links with suppliers, commercial power, negotiating capacity with financial entities and environmental activities.

Needs for measuring and accounting of intellectual capital:

The increasing importance of intellectual capital and the growing number of companies that needs to reliably feel on measurement and accounting of intellectual capital to provide *true and fair* view of the firm's financial position, real value of the firm and performance to the users. In addition, to measure future economic benefits that will flow from the intellectual capital. The recognition of such assets as intellectual capital in the financial statements will reduce the gap between the market value and the book value of the company as reported in the financial statements, which results a representation of more reliable value of the firm. It will help to the investors to rely solely on the financial statements to make investment decisions. It is the market value that drives an investor's decision in respect of whether or not to invest in a specific company. If accounting rules would not adapt to the increasing need to provide relevant information about investments in IC, accounting will lose its relevance and operation of capital market will be effected. Seetharaman *et al* (2002:132) note that it would definitely not be in a company's interests to ignore the existence of intellectual capital and not to make a concerted effort to measure and manage this asset. Capital providers might make investment decisions based on the information recorded in the annual financial statements of a company and this may result in incorrect decisions that may harm the company if the information recorded in the annual financial statements does not accurately reflect the



Human capital	**Relational capital**
➢ Know-how	➢ Brands
➢ Education	➢ Customers
➢ Vocational qualification	➢ Customer loyalty
➢ Work-related knowledge	➢ Company names
➢ Occupational assessments	➢ Backlog orders
➢ Psychometric assessments	➢ Distribution channels
➢ Work-related competencies	➢ Business collaborations
➢ Entrepreneurial élan innovativeness and proactive and reactive abilities	➢ Licensing agreements
	➢ Favorable contracts
➢ Changeability	➢ Franchising agreement

Structural capital

Intellectual property	**Infrastructure assets**
➢ Patents	➢ Management philosophy
➢ Copyrights	➢ Corporate culture
➢ Design rights	➢ Management processes
➢ Trade secrets	➢ Information systems
➢ Trademarks	➢ Financial relations
➢ Service marks	

financial position of the company, especially in the case of companies holding more intellectual capital than physical assets.

International Accounting Standard (IAS 38): Intangible assets

International Accounting Standard Committee (IASC) has taken the lead in establishing this premise. It applies, among other things, to expenditures on research and development (R&D) activities. IAS 38 does not apply to financial assets, insurance, contracts, mineral rights and the exploration for and extraction of minerals and similar non- regenerative resources. Investments in, and awareness of the importance of, intangible assets have increased significantly in the last two decades.

The main features of IAS 38 are:

- An intangible asset should be recognized initially, at cost, in the financial statements, if, and only if: the asset meets the definition of an intangible asset. Particularly, there should be an identifiable asset that is controlled

and clearly distinguishable from an enterprise's good will.
- It is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and
- The cost of the asset can be measured reliably.

This requirement applies whether an intangible asset is acquired externally or generated internally. IAS 38 also includes additional recognition criteria for internally generated intangible assets and the requirements reflect those of IAS 9.

If an intangible item does not meet both the definition, and the criteria for the recognition, of an intangible asset, IAS 38 requires the expenditure on this item to be recognized as an expense when it is incurred. An enterprise is not permitted to include this expenditure in the cost of an intangible asset at a later date. It follows from the recognition criteria that all expenditure on research should be recognized as an expense. Some development expenditures may result in the recognition of an intangible asset.

After initial recognition in the financial statements, an intangible asset should be measured under any one of the following two treatments.

- Benchmark treatment: historical cost less any amortization and impairment losses; or
- Allowed alternative treatment: revalued amount (based on fair value) less any subsequent amortization and impairment losses.

Intangible assets should be amortized over the best estimate of their useful life. The standard does not permit an infinite useful life. It includes a refutable presumption that the useful life of an intangible asset will not exceed 20 years from the date when the asset is available for use. Required disclosures on intangible assets will enable users to understand the types of intangible assets that are recognized in the financial statements and the movements in their carrying amount. IAS 38 also requires disclosure of the amount of research and development expenditure recognized as an expense during the year (IAS 38).

IAS 38 is applicable to an entity's external acquisition or internal generation of R&D costs- a major hurdle. A twenty year life of intangible assets limits the notion of an infinite life; yet, it allows for a more reasonable recovery time for the investment.

Intangible Assets in IFRS:

IFRS have been primarily focused on communication between companies and investors. The standards have been issued by the International Accounting Standards Boards (IASB) and contained both the accounting standards themselves and their interpretation together with the conceptual framework for preparation and submission of accounting statements. Intangible assets are dealt with by IAS 38 – Intangible Assets, including criteria for recognition, appreciation and publication of intangible assets. Intangible assets are defined as identifiable non-cash assets without physical essence.

If an item is recognised as intangible asset it is first priced by its acquisition costs. Further expenditures after this recognition usually do not meet the asset definition and therefore are recognised as costs. Acquisition costs, costs of employee training, costs of advertising and sale support, costs of moving or reorganization of enterprise are thus directly recognised as costs. Expenditures once recognised as costs cannot be activated anymore in future. Accounting standard distinguish among four types of acquisition of intangible assets and two types of in-house generated assets. The types of acquisition of intangible assets are as follows:

- The most frequent type of acquisition is purchase from a supplier. The acquisition price may be represented by the price stipulated by the purchase contract or in the invoice. Acquisition price may include: import duty, nonrefundable taxes, employee wages directly related to launch of operation of the asset, costs of experts (expert assessors, legal experts etc.) and costs related to testing of correct function of the asset.
- Another type of intangible asset acquisition may be acquisition in the context of business combination. The asset is then priced by the real vale as to the date of acquisition (as follows from IFRS 3 standard – Business Combinations).
- State subsidy is the third form of intangible asset acquisition. As this acquisition is often for free or for a symbolic price, the asset is priced either on the basis of its real value or on the basis of its nominal value increased by all costs directly attributable to the asset launch of operation.
- And the final basic type of intangible asset acquisition is the asset exchange – exchange for another non-cash asset or a combination of a cash asset and a non-cash asset. The asset is then priced on the basis of its real value, if the transaction is commercial, and the real value of the asset can be determined reliably. If the asset exchange fails to meet any of these conditions then the asset is recognised in the accounting value of transferred asset.

The two basic types of in-house generated intangible assets include the in-house generated goodwill and intangible assets generated by in-house activities.

- In-house generated goodwill represents items not meeting the definition of intangible assets but generating future economic benefits. Goodwill is often pointed out with employee knowledge, quality of product or service, environmental aspects of company activity etc. In-house generated goodwill cannot be recognised as asset and cannot be included in the balance sheet. Goodwill is not separable from the enterprise, does not follow from contractual or legislative rights and cannot be priced reliably.

- As for intangible assets created by in-house activities of the company they are represented by the research and the development generated assets:

The research stage is represented by activities related to acquisition of new knowledge, examination of use of this new knowledge, search for and selection of alternatives, for new materials, devices etc. The research stage is not recognised in the company intangible assets pursuant to IAS 38. The reason is the fact that in this stage the company is unable to determine the future economic benefits of the asset. The research expenditures are recognised as costs of the period in which they were incurred.

Measuring and Reporting of Intellectual Capital:

According to management literature, it is not likely to manage something which cannot be measured and reported. Of course there have been already many attempts to measure and report intellectual capital. In order to assist organisations to improve their annual reporting and to reap the benefits of reporting on intellectual capital, researchers recommend a number of financial and non-financial measurement models that may be divided into four general categories:

- **Direct intellectual capital practices**: these methods predict dollar value of intellectual capital through identifying their components. As intellectual capital components are identified, they can be evaluated continuously and directly. They can determine the final value of the organization intellectual capital through a combination.
- **The investment market value:** This method focuses on calculating the difference between company market value and book value of shares and it categorized the calculated difference as non-tangible assets or intellectual capital.
- **The return of assets method:** in this method, the average income before corporate tax in a definite period is divided on the average of the value of physical assets in the same period. Then the resulting number is compared with the average of the return of industry assets. If the resulting difference is zero or negative, the company has no intellectual capital surplus to average of industry and it is assumed that its intellectual capital equals to zero. But if the resulting difference is positive, it is assumed that the company has intellectual capital surplus to the average of industry and it is positive. The difference (positive) is multiplied to the average of physical assets value of the company in the same period to determine the average annual income in excess. By dividing the resulting annual income in excess to the company average cost of capital, the value of corporate intellectual capital is estimated.
- **Methods of score (credit) card:** in this method different components of intangible assets or intellectual capital are identified and for each of these indicators are provided and or they are displayed in corresponding graphs. The methods of score(credit) card are similar to direct intellectual capital assets but the difference is that in these methods there is no estimation of real value of non-tangible assets.

Some important methods of reporting intellectual capital are suggested bellow:

- Incorporating intangible assets and intellectual capital in the organization accounts and balance sheets.
- Providing intellectual capital statements as a condition attached to the financial statement.
- Providing two balance sheets, one for reflecting traditional assets and the other for reflecting intangible resources of the organization such a: intellectual capital, brand and etc. Since already there is no complete agreement among experts regarding to the above solutions, therefore no national or international guidelines exists in the field of intellectual capital reporting.

Conclusion:

The traditional accounting method play an important role in measuring and reporting tangible assets, but these methods in knowledge-based organizations in which knowledge constitutes a major part of its assets, cannot recognize such assets into accounts. The non-recognition of such assets as intellectual capital in the financial statements may results in a huge difference between the market value and the book value of the company as reported in the financial statements. Some recommended models have been discussed regarding measurement and accounting of intangible assets in accordance with IAS 38 and IFRS in order to adjust the said gap and represent actual financial position of the of the organization. According to the importance of intangible assets in information-based economy, inefficiency of traditional accounting in measuring and reporting intellectual capital components (human, structural, and communicational) can be clearly understood and therefore they need significant changes for proper accounting. Since intangible assets have been created using internal facilities in organizations and are not reported in traditional financial statements of the organization, appropriate measures for measuring and reporting these assets with the goal of more informed decisions by the shareholders, investors and analysts seem to be necessary. So it is suggested that depends on the importance of intellectual capital in the organizations, measuring and reporting of intellectual capital should be addressed seriously. It is also suggested that in order to have consistency in procedure and having comparability in measuring and creating intellectual capital, Accounting Standards Committee revise standards relate to measuring and reporting intangible assets, and by creating new capacities pave the way for achieving a common theoretical framework. As long as IC accounting is not distinctly identified beyond intangible assets accounting, the theory and practice of IC accounting will be considered as a very important but not sufficiently prominent issue in the field of intangible assets accounting.

References:

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Denial Of CENVAT Credit

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Introduction

Rule 3 of CENVAT Credit Rules, allows a manufacturer of final goods or provider of output service to avail and utilize CENVAT credit on excise duty, service tax paid on inputs, capital goods and input services. To avail CENVAT credit Rule 3 is to be complied with. Rule 4 specifies conditions for allowing CENVAT credit. These conditions are also to be complied with in availing CENVAT credit. In case of exempted goods or exempted services Rule 6 is to be complied with. Rule 7 specifies the manner of distribution of credit by Input Service Provider. Rule 9 species the documents to be prepared and maintained for availing the credit. Many a litigation arises on interpretation of these rules and in many a case the Department denied the credit to the assesses. In this article the various aspects that led to denial of credit by the Department.

Invoice Containing All Particulars

In 'Commissioner of Central Excise, Bangalore – I V. **Bhuwalka Alloys Private Limited' – 2012 (281) ELT 213 (Kar)** it was held that the material on record clearly discloses that the dealer who has issued the invoice has shifted the premises and that the premises from where the invoices were issued are the premises where the dealer did not have any office or business activity going on. However there is no denial of the fact that the inputs which were produced by the appellant is duty paid and they were received and consumed by the assessee in the factory premises. The assessee was required to give all the particulars of the goods procured by them and the details of the duty paying document. The invoice produced by the assessee contains all the necessary particulars. The authority has not recorded any finding that there is no such dealer in existence or that no inputs were supplied by him or that any duty was paid on such inputs. There is also no finding that the inputs were not received in the factory premises or it was not used in the manufacturing process. In the absence of any such finding and all those facts having been established the Tribunal held that the benefit of CENVAT credit cannot be denied to the dealer who has paid the duty. The Court did not see any justification to interfere with the well considered order passed by the Tribunal.

Non Endorsement in Bill of Entry

In 'BHEL V. Commissioner of Central Excise, Bhopal' – 2011 (274) ELT 39 **(Tri. Del)** the appellant imported a consignment and bill of entry was filed in the name of its International Operation Division and the imported goods have been received in the appellant's factory at Bhopal and credit of Rs.628351/- has been taken. The Department denied the credit on the ground that the International Operation Division of the appellant has not endorsed the Bill of Entry in the name of the appellant's factory which is in violation of the procedure prescribed by the Board vide Circular No. 179/13/96-CX, dated 29.02.1996. The Tribunal held that the Bill of Entry was in the name of the appellant only. It did not mention the factory address instead mentioned the address of International Operation Divisions. This does not make the document being not in the name of the appellant. The appellant has produced the Store Receipt Voucher (SRV) as evidence for receiving the material in the factory which has been duly noted by the Commissioner. Therefore, the finding that in the absence of endorsement in the Bill of Entry by the International Operations Division, it was not possible to ascertain as to whether the goods covered by the Bill of Entry were received and used in the assessee factory cannot be appreciated.

Constructive Delivery of Inputs

In the above said case another issue of denial of CENVAT credit in respect of inputs procured by the appellant from Hindustan Copper Limited, which were not received in the factory of the appellant but directly sent to the job worker. Since the same has not been sent from the premises of the appellant under challans to the job worker it is in violation of the procedure prescribed in Circular No. 33/33/94-CD,8, dated 4.5.1994. The Tribunal held that the explanation that the appellant have taken constructive delivery of the inputs and instead of receiving it in their factory and then again sending to the job worker has directly sent it to the job worker deserves to be accepted. The fact that the job worker has processed the material and sent the intermediate goods manufactured using the inputs following Notification No. 214/86 has not been refuted. In the given facts and circumstances of the case, the transport of material directly to the job worker's premise to avoid payment of extra period and the same time, cannot lead to denial of credit.

Non Mentioning of St Regn. No.

In '**Lakshmi Automatic Loom Works Limited V. Commissioner of Central Excise, Coimbatore' – 2011 (274) ELT 375 (Tri. Chennai**) the demand has been raised on the ground that the credit was taken on the strength of documents on which the input service suppliers had not mentioned the service tax registration number, categories/ classification of services, address of the person receiving services including the detail of invoices and bills. The Tribunal found that the address of the suppliers as well as the category of service and the address of the recipient of the service is clearly mentioned. Non mentioning of the service tax registration number by the input service supplier cannot be a ground to deny credit to the assessee. As regards credit of Rs.23,301/- has been denied on the ground that the assessee did not produce any document to prove the point that the sale take place at the point of destination (port) and the ownership of the goods remain with the appellants till the delivery of the goods. However, there is nothing to contradict the stand of the assessee that the sale takes place when the goods are laden on the board the vessel at the port and given the removal of places is the port, the assessee is entitled to the credit.

Fabricated Invoice

In '**Trimurti Ispat Limited V. Commissioner of Central Excise & Customs, Nagpur' – 2011 (274) ELT 435 (Tri. Mum**) the invoice in question on which the credit has been taken were issued by M/s Tata Re-rolling Mills and on investigation, it was found that M/s Tata Re-rolling Mills had not taken any manufacturing activity in their factory and issued fabricated invoices by manipulating statutory records. Therefore the credit availed by the appellant was not admissible to them. The appellants are rightly denied credit and they are liable to pay penalty as well as interest.

Complying With Rule 3

In '**Natco Pharma Limited V. Commissioner of Central Excise, Hyderabad – II' – 2011 (274) ELT 438 (Tri. Bang)** CENVAT credit was denied to the assessee on the ground that the credit was taken on non dutiable inputs. The Department contended that according to Rule 3 a manufacturer of final product claiming credit of duty paid on his inputs is liable to establish that duty was, in fact, leviable on such inputs under Central Excise Act read with the First Schedule to the Central Excise Tariff Act. No excise duty was leviable on the materials received by the appellant from their suppliers and therefore any credit of duty thereon cannot be claimed by the latter. The assessee contended that they satisfied the legal requirements by availing CENVAT credit on their inputs on the strength of the invoices which contained all the necessary particulars of goods and also clearly showed the duty having been paid on the goods. The Tribunal held that the inputs were covered by valid invoices and the assesseec complied with Rule 3. Therefore the benefit of CENVAT credit cannot be denied to the appellant.

Material Evidence to Deny Credit

In 'Commissioner of Central Excise, Ghaziabad V. Central Electronics **Limited' – 2011 (271) ELT 586 (Tri. Del)** the Tribunal held that apart from alleging that the inputs were neither brought into the factory nor any manufacturing activity or processing thereon in the factory premises of the respondents was carried on no other material placed on record by the Department so as to deny the benefit of credit on such inputs to the respondents. It was the specific case of the respondents that the goods were subjected to payment of duty they were duly received by the respondent, they were utilized in the final product manufactured by the respondents, and the final product was a dutiable product. All these facts were never in dispute in the entire proceedings and being so, the Tribunal dismissed the appeal filed by the department.

Delay in Taking Credit

In '**Commissioner of Central Excise, Ahamedabad V. Pierlita India Private Limited' – 2011 (273) ELT 535 (Tri. Ahmd)** the respondent had taken credit of service tax in respect of GTA and maintenance & repair services for the period from 31.12.06 to 29.02.08 in the month of March 2008. Proceedings were initiated by the Revenue denying the credit so availed on the ground that the credit was not availed immediately after the payment of bills and service tax. The Original Adjudicating Authority disallowed the credit and the first Appellate Authority decided in favour of the assessee. The Tribunal relied on circular issued by the Department in F.No. 345/2/2000-TRU,dated 29.02.2000 in which it has been observed 'the idea is that if the manufacturer desires he can take the CENVAT credit at the earliest opportunity when the inputs are received in the factory. This, however, does not mean, not is it even intended that if the manufacturer does not take credit as soon as the inputs are received in the factory, he would be denied the benefit of CENVAT credit. Such an interpretation is not tenable. In view of the above the Tribunal dismissed the appeal.

Crossing SSI Exemption Limit

In 'Eureka Conveyor Belting Private Limited V. Commissioner of Central **Excise, Jaipur**' – 2011 (272) ELT 285 (Tri. **Del)** the appellant claimed SSI exemption under Notification No.8/03-CE, dated 1.3.03. Since they crossed the SSI exemption limit on 11.10.07 the appellant informed the same to the department and they started maintaining statutory records as per the Central Excise Rules and claimed the credit on the inputs lying on 11.10.07 in respect of inputs accounts in process and input containing in finished goods. On physical verification by the Officer, it was found that inputs gone into process and finished goods could not be verifiable inputs account in process and input containing in finished goods was denied. The Tribunal held that as per Rule 3(2) the appellant is entitled for credit on the inputs in work in progress and inputs containing in finished goods as on the date the input work in progress lying in their stock and on the date of crossing SSI exemption limit. Accordingly the appellant is entitled for credit on the inputs containing in work in progress and inputs containing in finished goods.

Credit on Supplementary Invoice

In 'Commissioner of Central Excise, Mumbai V. United White Metal Limited' – 2011 (272) ELT 268 (Tri. **Mum)** the appeal is against the impugned order wherein CENVAT credit taken on the strength of the supplementary invoice was denied on the ground that no goods have been received, the credit cannot be taken. On perusal of the agreement, the Tribunal found that while fixing the price, there was an agreement between the supplier and the appellants that a minimum quantity of cracked ammonia gas will have to be lifted on a price so fixed, but there was further a clause that if the appellants failed to lift the required quantity, the price of the cracked ammonia gas will be charged and extra amount for that shall be charged from the appellants for which these supplementary invoices have been raised on the appellants on which the proper duty has been paid by the supplier. The supplementary invoice has been raised for the minimum agreed quantity by the appellant is nothing but the exalted amount of the goods received by them. Therefore the appellants are entitled to take the credit on the strength of the supplementary invoices.

Ancillary or Incidental Process for Manufacturing a Final Product

In 'ESS ELL Cables Company V. Commissioner of Central Excise, Daman' – **2012 (279) ELT 563 (Tri. Ahmd)** the appellants imported 'super enamelled copper wire' from Sri Lanka and are engaged in manufacturing of 'super enamelled copper wire'. The factory premises were inspected. The Department was of the view that the appellants were not undertaking any manufacturing activity and hence they were ineligible for CENVAT credit taken on the CVD paid on imported copper wire/rod. A show cause notice was issued for denial of CENVAT credit availed by the appellant and interest and penalty. The assessee contested the show cause notice but the same was rejected and the demand was confirmed along with interest and penalty. Hence the present appeal. The Tribunal held that the appellant has been carrying out a detailed process, which can be construed as an ancillary or incidental process for manufacturing a final product i.e., 'super enamelled copper wire' or 'submersible winding wires'. The Adjudicating Authority has not considered the important piece of evidence which was recorded by the officers during the visit of the factory premises of the assessee which clinches the case for the assessee. The assessee is in consonance with the provisions of Rule 3 of CENVAT credit rules, 2004 which requires manufacture by using inputs 'in' or 'in relation to' the manufacture of final products.

Authenticity of Documents

In '**National Chemicals & Dyes Co., V. Commissioner of Central Excise, Allahabad'- 2012 (278/ ELT 687 (Tri Del)** it was held that the availment of CENVAT credit has to be justified on the basis of document as specified in Rule 9 of the CENVAT Credit Rules, 2004. Apparently it refers to the invoices to be the basis for claiming the credit. In this case the invoices is in favour of the appellants were dealer's invoices and the same did not disclose all the information in relation to the valuation and duty element suffered by the products which accompanied the invoices. At the same time it is not also in dispute that the deficiency was sought to be made good by the appellants by producing the invoices issued by Panipet Refinery to the depot in relation to the same good. Neither the adjudicating authority nor the Commissioner (Appeals) had even doubted the credibility of any such copies of invoices. The fact that the goods were actually received in the factory was not in dispute. The Tribunal held that the denial of CENVAT credit is unjustified.

Denial on Provisional Assessment of Bill of Entry

In 'Monarch Catalyst Private Limited V. Commissioner of Central Excise, **Thane – I' – 2012 (278) ELT 668 (Tri. Mum)** under Rule 9 of CENVAT Credit Rules, the documents specifically been prescribed on which the credit could be taken by the manufacturer. Under Rule 9(1) at Sl. No. 'e' the main document mentioned is 'Bill of Entry'. It does not state that the Bill of Entry should not be provisionally assessed or Bill of Entry should be finally assessed. Bill of Entry, whether it is provisional or final, is the document on which the CREDIT can be availed by the manufacturer. Section 2(4) of Customs Act provides that Bill of Entry means of Bill of Lading referred to Section 46 of the Customs Act.

Section 2(2) provides that assessment includes provisional assessment, reassessment and any order of assessment in which the duty assessed is NIL. When goods are cleared against a Bill of Entry, the Bill of Entry has to be assessed either provisionally or finally. Provisional assessment is also an assessment. Goods cannot be cleared from the Customs unless the Bill of Entry is assessed. Therefore the entry at Rule 9(1)(e) will include Bill of Entry either provisionally assessed or finally assessed. There is no reason to deny the credit to the assessee merely on the ground that Bill of Entry was provisionally assessed by customs authorities. The Tribunal set aside the order passed by Commissioner and allowed the appeal.

Sending Samples by Courier

In 'Commissioner of Central Excise, **Vapi V. Parle International Private Limited' – 2012 (278) ELT 625 (Tri. Ahmd)** the Tribunal found that there is no dispute that courier service was used for sending samples to the customers for approval and for communication with their head office to send documents and other correspondences. The Tribunal was unable to understand how the Original Adjudicating Authority could reach the conclusion that in such a situation courier service does not have nexus with the manufacture and the clearance of final product and the service is beyond the stage of manufacture and clearance of goods. Sending samples to customers and correspondence with head office from the factory are definitely activities relatable to manufacture and therefore clearly the courier clearly falls under the definition of category of input services. If it is viewed that it is admissible only up to the place of removal, there is no indication anywhere in the records or there is any evidence to show that the courier service was clearly recognizable as the one which was received after the removal had taken place. What is required is nexus with manufacture and when the service is clearly identifiable to show that same has not been received after the place of removal, credit cannot be denied. The Tribunal rejected the appeal.

Conclusion

The above illustrations/cases are not exhaustive. There are still many cases in denial of credit in interpretation of rules. The service tax regime has witnessed a vast change in this financial year. Therefore all the provisions relating to availing of CENVAT credit are to be updated by the professionals and to advise their clients in order to avoid denial of credit by the department.

Kolkata, the 28th August, 2012

NOTIFICATION

18-CWR (1620-1623)/2012: It is hereby notified in pursuance of amended Regulation 18 of the Cost and Works Accountants Regulations, 1959, that in exercise of the powers conferred by Regulation 17 of the said Regulations, the Council of the Institute of Cost Accountants of India has restored to the Register of Members, the name of:

1. Shri Siba Prasad Sengupta, BSC, BCOM, ACMA, Flat No. 309, 110, Mandeville Gardens, Kolkata – 700019, (Membership No. 718) with effect from 28th August, 2012,
2. Shri Narendra Presendra Sinha, BSC, LLB, FCMA, 2/1, Nehru Nagar (East), Dist-Durg, Bhilai – 490020 (Membership No. 3849) with effect from 24th August, 2012,
3. Shri Dilip Kashinath Kajgaonkar, BE, NBA, FCMA, Prithvi-Sarovar Apartment, 1137/6, Model Colony, Shivajinagar, Pune – 411016 (Membership No. 8274) with effect from 15th August, 2012,
4. Shri Neeraj Mohan, MCOM, ACMA, Block No. 39, House No. 4, Shakti Nagar, Delhi 110007 (Membership No. 10531) with effect from 24th August 2012.

Sd/-
(Rakesh Singh)
President

Goodwill as an Intangible Asset

T.C.A. Ramanujam
Chief Commissioner of Income Tax (Retd) &
Former Member, Income Tax Appellate Tribunal

T.C.A. Sangeetha
B. Sc, M.L.

With effect from the Assessment year 1999-00, depreciation is allowable on specified intangible assets. Section 32 (1) (ii) lays down that depreciation should be allowed on the following intangible assets:

1. Know how
2. Patents
3. Copy rights
4. Trademarks
5. Licenses
6. Franchisees
7. Any other business or commercial rights of similar nature.

The law lays down that depreciation is allowable only on those intangible assets which are acquired on or after 1.4.1998 and is allowed at 25%. The term 'know-how' is defined but the other items of intangible assets are not defined.

Section 32 comprehensively defines terms relevant for granting depreciation allowance.

Explanation 3 states that the term 'asset' shall mean an intangible asset, being know-how, patents, copyrights, trademarks , Licenses, Franchises or any other business or commercial rights of similar nature.

Now look at Explanation 4, "for the purposes of this sub section, the expression 'know-how' means any industrial information or technique likely to assist in the manufacture or processing of goods or in the working of a mine, oil-well, or any other sources of mineral deposits". In the light of these definitions controversies had arisen regarding the claim for depreciation on goodwill.

Palkhiwala's commentaries 9th Edition expressed the opinion that the general words, "any other business or commercial rights of similar nature" should be interpreted *ejausdem* generis and should derive the colour from those preceding the specific words. The residual category should include trade name, invention, model, design, secret formula or process.

The Kerala View

The matter regarding claim for depreciation on goodwill was considered by the Kerala High Court in Ravindran Pillai's case 237 CTR Kerala 80. A longstanding hospital was sold as a going concern with the name, logo, trademark, staff and equipment. Intangible assets were mentioned in the schedule to the sale deed at a figure of Rs.2 crores. Depreciation was claimed on this amount under the head 'goodwill'. Negativing the claim, the Assessing Officer held that there can be no erosion in goodwill and there can be no question of wear and tear. The general impression was that goodwill appreciated with the passage of time. This argument of Revenue was rejected. It was pointed out that on account of inflation, even tangible assets like building and machinery fetched a higher price in later years though in the company;.s books of accounts depreciation is written off. It was also argued that the Act took into account the possibility of appreciation and still allowed depreciation. The Kerala High Court ruled that the entitlement for depreciation on intangible asset cannot be negatived on the ground that no erosion in value takes place on account of the user of the asset in business. It is the reputation that brings patients to the hospital. Payment of a huge amount towards goodwill ensures the maintenance of such reputation. The right to use the name of the hospital itself amounted to transfer of goodwill. The matter was decided in favour of the party claiming depreciation.

The Madras View

The Madras High Court considered this matter in the case of India Cements Limited 339 ITR 31. India Cements acquired a plant from Coromandel Fertilizers for a consideration of Rs.105 crores. In the assessment of the company, the Assessing Officer estimated 10% of the purchase price as representing goodwill and excluded this amount for purposes of computing depreciation. It was noticed by the Madras High Court that Coromandel

Fertilizes was making losses from the 1st year, though it had a trade name. It had no assets to quote. A loss making cement plant was purchased. Under these circumstances there can be no question of goodwill. The Madras High Court held that there was no basis at all for deducting 10% of the purchase price towards value on goodwill. The departmental appeal was dismissed and depreciation was granted on the entire sale consideration.

Supreme Court Decides

The matter has reached finality by the Ruling of the Supreme Court in Commissioner Income Tax vs. Smifs Securities Ltd., 252 CTR 233. This judgment was delivered in the end of August 2012. The question to be decided was whether goodwill is an asset within the meaning of Section 32 of the Act entitled to depreciation. In accordance with a scheme of amalgamation of YSN shares and securities (P) ltd with Smifs Securities Limited, assets and liabilities of the transferor company were transferred and vested in the transferee company. Extra consideration was paid in this arrangement which was sanctioned by the Calcutta High Court. Such excess consideration over and above the value of tangible assets was claimed as payment towards goodwill for acquiring the reputation of the amalgamating company. Arguments centered on the interpretation of Explanation 3 defining the term 'asset'. The Supreme Court applied the *ejausdem* generis principle and held that goodwill is an asset under Explanation 3(b) of Section 32(1) of the Act. The Court also took note of the fact that no amount was actually paid on account of goodwill. It however agreed with the view that the difference between the cost of an asset and the amount paid represented the value of goodwill and that the company in the process of amalgamation had acquired a capital right in the form of goodwill because of which the market worth of the assessee company stood increased. The Supreme Court pointed out that only question raised in Revenue;s appeal was whether goodwill is an asset within the meaning of Section 32 of the Act entitled to depreciation.

Conclusion

There have been several orders of the Income Tax Appellate Tribunal on the issue of depreciation on goodwill. This is the first time that the highest court in the land has considered the matter and decided the same in favour of the taxpayer. Several conclusions can be drawn. There can be no question of goodwill in the case of a losing company. This conclusion will also be subject to riders regarding the reasons for the loss. When mergers and amalgamations take place, great care is required in drafting the scheme and submitting the same to the High Court for approval. It is always better to identify the amount on which calculation of goodwill is based. As we know, it is difficult to measure the value of goodwill. Accountants usually resort to valuation by adopting 3 years purchase price. There are well recognized principles for evaluating goodwill. By proper valuation of goodwill; a lot remains to be gained by way of 25% depreciation for the new entity. All cases deciding that goodwill is not entitled to depreciation should be considered as no longer good law. The Supreme Court has finally given its approval in favour of the view that goodwill is an intangible assets entitled to depreciation.

Benevolent Fund for the Members of The Institute of Cost and Works Accountants of India

Benevolent Fund for the members of The Institute of Cost and Works Accountants of India was created with the noble cause of extending grants and financial assistance of prescribed amount to the members and beneficiaries of the Fund for medical treatment, financial distress and death.

In the recent past, although the grants and financial assistance could be extended to the eligible members and beneficiaries of the Fund in time, it would have been possible to provide enhanced benefits if the membership of Fund had been larger. We, therefore, appeal to those members of the Institute of Cost Accountants of India who have not yet become members to apply for Life Membership of the Fund immediately. The members are also requested to arrange for donations for the fund to provide support to this noble purpose. For details and application form, please visit the Institute's website:www.icwai.org.

Tax Titbits

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Gaar—Shome Committee Report

An Expert Committee under the Chairmanship of Mr. Parthasarathy Shome has just submitted its report on GAAR, which forms part of the amendments by the Finance Act, 2012. The Committee has noticed that these amendments had ***"generated world-wide opprobrium not only against the unpredictable approach to administration of the Indian tax authorities but also of policy makers who enact laws. The outcome is a widely held view that India is not a good place for investment at the moment".*** Report on GAAR gives comparative provisions in the other countries with number of amendments suggested to make the rule more palatable with as many as twenty seven illustrations indicating instances where GAAR would be applicable or not applicable replacing the twenty four illustrations earlier issued by the Income-tax Department, but only found to be "insufficient or confusing" by the Committee presided over by Finance Secretary vide Business Line dated 10th July, 2012. The Report proposes a number of amendments not all strictly confined to GAAR, but making its application easier.

The Report starts with usual discussion on the subject of avoidance in contrast with evasion. It has pointed out that U.K. has yet to adopt the draft rule recommended to it, limiting applicability of the Rule only to "exceptional cases where there is clear evidence of an extremely aggressive arrangement to escape tax." But there is no such limitation in GAAR as imported in our law even after the proposed amendments to make them less unacceptable. The following are the major recommendations in brief:

1. Tax avoidance will not be inferred merely because tax savings is one of the main purposes. It should be either a main purpose or a dominant purpose.
2. The entire arrangement need not be discarded, if it could be partially salvaged as permissible. Part acceptance should, however, be permissible only where
   i. Transfer pricing rules are not applicable,
   ii. Where there is adherence to the form, and not to substance.
   iii. Where the transaction lacks commercial substance and
   iv. Where the transaction is not *bona fide*.
3. An overall view will be taken. The three circumstances listed under section 97(4), which will be required to be ignored as not avoiding application of GAAR, are (i) period of time, (ii) fact of payment of tax and (iii) where there is an exit route. An amendment is proposed, so that these circumstances need not to be totally ignored.
4. Lack of definition of "connected person" is proposed to be remedied by confining its meaning to associate enterprise under section 92A and related party under section 40A(2) of the Act.
5. Limitation of Benefit (LOB) clause is suggested for all treaties. Till such time it is incorporated, treaty override will continue to be recognised.
6. Advance ruling should be extended also to residents who are parties to an international transaction with a time limit for such ruling being stipulated at six months.
7. A negative list which will not be treated as avoidance is one of the useful recommendations. They are as under:
   i. Selection of one of the options offered in law. For instance –
      a. payment of dividend or buy back of shares by a company
      b. setting up of a branch or subsidiary
      c. setting up of a unit in SEZ or any other place
      d. funding through debt or equity
      e. purchase or lease of a capital asset
   ii. Timing of a transaction, for instance, sale of property in loss while having profit in other transactions

iii. Amalgamations and demergers (as defined in the Act) as approved by the High Court.

iv. Intra-group transactions (i.e. transactions between associated persons or enterprises) which may result in tax benefit to one person but overall tax revenue is not affected either by actual loss of revenue or deferral of revenue."

It has been explained that underlying assets, which are listed shares alone will be outside the purview of GAAR.

8. Another major recommendation is that exemption for transfer of capital assets under section 10(38) should be extended to stock-in-trade, so as to avoid controversy as to whether shares are held in the capacity of an investor or a dealer.
9. Deferment of GAAR from one year to three years is recommended to attune foreign investors to "paradigm shift in tax policy", while giving time for training of the officers with international benchmarked modules and for putting in place the appropriate procedures and processes. Such postponement may even be understood as amnesty for tax avoidance for three years!
10. Though the Committee was unable to accept the recommendation excepting arrangements prior to the date on which GAAR is made effective, it has recommended that those investments existing for five years, though vulnerable under the GAAR, will be protected by grand-fathering the tax saving earned five years earlier.
11. Tax Residency Certificate of Mauritius should be acceptable and Circular No.789 of 2000, which was withdrawn, should be given life.
12. A threshold limit of tax benefit of Rs.3 crores for application of GAAR has been suggested.
13. Where tax avoidance could be tackled by application of Specific Anti Avoidance Rule (SAAR) like transfer pricing, neither GAAR nor LOB should be applied.
14. No adjustment should be allowed consequent on application of GAAR rule as compensating relief in respect of the same amount for other entities, but it is recommended that it can be allowed to the same assessee either in the same year or in different years.
15. GAAR will not be applied for purposes of withholding tax on the undertaking of the deductor to indemnify the Government in case it becomes applicable and that too after prior approval of the Commissioner for detailed reasons to be recorded by him.
16. Where a non-resident is prepared to abide by the domestic law opting to forego treaty benefits, GAAR should not be applied.
17. Training programmes for officers and taxpayer education are suggested to foster greater trust between the tax administration and the taxpayers.
18. A number of procedural recommendations have been made regarding show cause notice, the strengthening of the approving panel, time limits at each stage, forms to be used and requirements of reporting in tax audit report.

A list of twenty seven illustrations warranting either applicability or otherwise has been listed. Even so, fresh litigation with reference to them is not ruled because of excessive reliance on them either by the taxpayers or by revenue. .

Retrospective Amendments Relating to Indirect Transfer—Draft Report

It is in the light of the wide spread criticism of the drastic amendments made by the Finance Act, 2012 to upset the law settled by the Courts including the Apex Court with retrospective effect from 1.6.1976 and apprehensions as to its effect on Foreign Direct Investments (FDIs) that Shome Committee was required also to report on retrospective amendments relating to indirect transfer. A draft report has since been made on 9th October, 2012 with many welcome proposals. The Committee has expressed itself to be against any unanticipated fundamental changes in tax provisions without prior warning and consultation. As regards retrospectivity, it has expressed itself that retrospective application of tax law should occur in exceptional or rarest of rare cases, to cover following objectives:

"First, to correct apparent mistakes/anomalies in the statute; second, to apply to matters that are genuinely clarificatory in nature, i.e. to remove technical defects, particularly in procedure, which have vitiated the substantive law; or, third, to "protect" the tax base from highly abusive tax planning schemes that have the main purpose of avoiding tax, without economic substance, but not to "expand" the tax base. Moreover, retrospective application of tax law should occur only after exhaustive and transparent consultations with stakeholders who would be affected."

The following are the main recommendations:

1. Where the amendment is not clarificatory, while it tends to widen tax base, it should be applied only prospectively. Where it is required to be applied retrospectively, it cannot be applied in the hands of a representative assessee as the burden of compliance on its part borders on impossibility of performance. Where it is applied, there should be neither levy of interest nor penalty. The question of penalty in such cases should not arise even on merits, while interest, one should expect, is bound to be waived even in normal course.
2. Explanation 5 to section 9(1)(i) is sweeping in nature, so as to require limitation of its application, where there is not merely an economic interest, but also where

there is substantial interest by way of participation in ownership, capital, control or management. Fifty per cent (50%) interest should be the test for substantial interest for this purpose. "Look through" should be understood in valuation of share of a foreign company ignoring the intermediaries. Transfer for purposes of the Explanation should be understood as confined to assets located in India to be taxed on proportionality basis, so that underlying assets may well be taxable in case of a non-resident holding substantial interest.

3. To avoid undue hardship to small shareholders, there will be no liability where such shareholder has less than 26% of the total voting power.
4. Exemption may be provided to a foreign company where the investment in India is in the form of frequently traded listed shares subject to SEBI and RBI guidelines.
5. Intra-group reorganization should not attract tax, where there is continuity of ownership to the extent of 75% through amalgamations and demergers and 100% in other forms of restructuring.
6. Investments made by non-resident investors through Foreign Institutional Investors (FIIs) by way of Participatory Notes (PN) should be made specifically exempt, if made subject to SEBI guidelines.
7. Private equity investors making investments in India with Private Equity (PE) Fund in the form of units should be spared liability in India as long as such investor does not have more than 26% capital or voting power in the Fund and the Fund itself does not have more than 50% assets in India compared to its global assets.
8. The Committee is not against taxation of underlying assets in India as expected under Explanation 5 to section 9(1)(i) subject to its other recommendations. But such deeming under Explanation 5 should be confined to taxation of capital gains and not to dividend.
9. Liability under the domestic law consequent on the amendments is, however, subject to provisions under the Double Taxation Avoidance Agreement as regards capital gains in respect of investments and this may be made clear by way of amendment to law, rules or by way of circulars.

Licensed Software

Amendment to Finance Act, 2012 relating to definition of royalty providing for "look through" and covering the transfer of all or any right for use or right to use a computer software by insertion of Explanation 4 to section 9(1)(vi) with retrospective effect from 1.4.1962, has created widespread apprehensions for software business. There was a promise of consideration of their grievance. Notification No. S.O. 1323(E) dated 13.06.2012 spares deduction of tax at source in respect of payment for acquisition of softwares to a case, where the transferor is a resident and where he has acquired them by payment for the same from another resident or a non-resident after deduction of tax either under section 194J or 195 and files a declaration from the transferor to that effect. Though the Notification is limited to tax deduction at source, non-liability by treating it as royalty could be inferred on resale of software, though the condition of prior tax and proof of the same are matters which go beyond the law and expects the impossible for a purchasing dealer for resale, a matter which may require clarification or adjudication.

But the Notification is welcome to the extent to which it concedes the possibility of non-liability in respect of standardized software known as "branded software", "off-the-shelf software" or "shrink-wrapped software". This would require to be made more explicit by a Circular, while even in respect of specialized unbranded software, which alone could be treated as targeted by the Explanation, liability would need to be reconciled with the decisions of the Supreme Court for purposes of sales tax and import duty in Tata Consultancy Services v State of Andhra Pradesh (2005) 271 ITR 401 (SC), Bharat Sanchar Nigam Ltd. v. Union of India (2006) 282 ITR 273 (SC) and Sprint RPG India Ltd. v. Commissioner of Customs (2000) 2 SCC 486.

Announcement

The Institute's Convocation and the National Students' Convention will be held on Friday, the 22nd March 2013, at Science City Auditorium, Kolkata. This is for the information of all concerned.

The New Service Tax: Service Calls Abound

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It is said that time is of the essence in every endeavour. Indeed, 'time and tide wait for no man'. As the axiom goes, 'a stitch in time saves nine'. The present season is full of heart-warming festivals in our country making us forget our daily woes for a while. The main monsoon is behind us. Soon the Revenue Department will start consultations and preparations in connection with the Budget to be presented on 28th February 2013. The hardy annual of Budget is at once a carnival and karma in our country. Now is the time to undertake a quick review of the problems and issues witnessed in the new-look Service tax that have bedeviled it since 1st July 2012. The fact that it is still early days in the new Service tax regime cannot take away from the reality that changes in Service Tax were introduced ahead of the curve and when the GST to which the New Service Tax conceptually belongs is still looming very distantly in the horizon. Despite the short tango of engagement with the new-fangled Service tax, the missteps in the new tax are far too transparent and very significant in terms of their impact. The wrinkles in the Service tax need to be ironed out and the tax linen brightened up. It got a bit dirty at the mill itself. In this Article we will look at some of the problems thrown up by the new Service tax and hope that the coming Budget will unveil suitable remedies for the maladies.

Government Vs Government

A major area of tax retreats in the New Service Tax is a broad range of tax concessions given to Government activities as well as to specified Services rendered to the Government. In this Article, our intention is not to question the wisdom of Tax withdrawal for the Government, though it would have been economically desirable and fiscally wise to have distinguished governmental non-merit services from merit services and to have confined the tax concessions to the latter alone. What we wish to point out is that a definition of '*Government*' surprisingly has been conspicuous by its absence in the new Service tax provisions. Even more surprising is the fact that though there is nothing in the new provisions to distinguish between the ***Union Government*** and the ***State Government*** as regards the tax concessions for government in general, the Education guide clearly tries to keep state government departments out of the tax exemption in areas of transactions and dealings with the central government departments. The Law utterly fails to throw light on the governmental status of various statutory bodies and statutory corporations.

A Look at the Concessions Granted to the Government

Section 66B containing the Negative List of Services provides for the following Services by the Government to be non-taxable:-

a. ***Services by Government or a local authority excluding the following services to the extent they are not covered elsewhere—***

i. *services of the Department of Posts by way of speed post, express parcel post, life insurance, and agency services provided to a person other than Government;*
ii. *services in relation to an aircraft or a vessel, inside or outside the precincts of a port or an airport;*
iii. *transport of goods or passengers; or*
iv. *support services, other than services covered under clauses (i) to (iii) above, provided to business entities;*

Services exempted under Notification 25/2012:-

Services provided to the Government, a local authority or a governmental authority by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alternation of –

a. civil structure or any other original works predominantly for use other than for commerce, industry, or any other business or profession.

b. a historical monument, archaeological site or remains of national importance, archaeological excavation, or antiquity specified under the Ancient Monuments and Archaeological Sites and Remains Act, 1958 (24 of 1958);
c. a structure predominantly for use as (i) an educational, (ii) a clinical, or (iii) an art or cultural establishment;
d. canal, dam or other irrigation works;
e. pipeline, conduit or plant for (i) water supply (ii) water treatment, or (iii) sewerage treatment or disposal; or
f. a residential complex predominantly meant for self-use or the use of their employees or other persons specified in the *Explanation I* to clause (44) of section 65B of the said Act;

The above provisions are in addition to a veritable range of exemptions and concessions applicable to various Services mentioned in the Negative List and in the Mega Exemption Notification. However, what stands out is the differentiation of Government, a local authority or a Governmental authority in the statutory exemption notification. While Governmental authority and local authority are defined, there is no definition of *'Government'* in the new tax regime. It is surprising that the Government is not defining itself. Is it because it is so unsure of its status and extent that it cannot say what it is? In the Guidance Note No.2 of its Education Guide, vide para 2.4.7, the Central Board of Excise and Customs has made an attempt to answer the question 'what is the meaning of *Government?*'

As seen from the Guidance Note, the definition of *Government* means the *President and the Officers subordinate to him*, and in the context of the State Government, it means the *Governor of the State and Officers subordinate to him*. By itself this attempted answer does not clarify much. When the CBEC says that the Central Government means the President and the Officers subordinate to him, do they mean only the Civil Service Officials working in the respective Central Government Departments or do they include Civil Service Officers posted as Corporate Executives and Directors in Central Government-owned or Central Government-controlled Companies? The same question can be asked of the definition of the *State Government* attempted in the Guidance Note. This definition of *Government* is narrow and ill-conceived. Article 12 of the Constitution of India defines *State* and that definition includes the Government of India and the Governments of the States as well as local and other authorities within the territory of India or under the control of the Government of India. The Apex Judiciary has classified many Governmental Agencies as coming within the scope of *State*. The List includes Corporations and Bodies answering the test of being an instrumentality or agency of Government. Some of the Organizations included are as follows:-

- Project and Equipment Corporation of India.
- Hindustan Steel Limited
- Indian Council of Agricultural Research
- Indian Statistical Institute
- Bharat Petroleum Corporation
- Indian Oil Corporation
- Coffee Board
- Steel Authority of India Limited
- Various State Electricity Boards.

Even though the delineation of the above Organizations as instrumentalities or Agencies of Government is in terms of the concept of protection of fundamental rights within the meaning of Article 12 of the Constitution, it cannot be much different in the case of Service Tax Law. In the absence of a statutory definition of *Government* in the Finance Act, 1994, the constitutional interpretation of instrumentality or agency of Government in the context of Article 12 of the Constitution, is bound to echo in the Service Tax Law. The unduly restrictive meaning of *Government* put out in the Education Guide fails against the meaning of *Government* in the constitutional interpretation of Article 12, which is the foremost provision in the Constitution as regards the definition of ***State***. We should not have different nebulous meanings of *State* and *Government* for different purposes.

The Guidance Note issued by CBEC vide para 2.4.10 further states that a statutory body or corporation or an authority created by the Parliament or a State Legislature is neither a Government nor a local authority. This construction of the Executive similarly fails against the test of instrumentality of State seen in the constitutional interpretation of Article 12. Disputes are bound to crop up in course of time regarding the meaning and scope of *Government* in the Service Tax Law. Therefore it is advisable for the Department to put in a clear cut definition of *Government* in the Service Tax Law, which is neither artificial nor new-fangled and reflects the spirit of constitutional interpretation of *State* and *Government* in the context of Article 12 of the Constitution.

Central Government Vs State Governments & State Government Vs State Goverment

The Guidance Note No.2 issued by the CBEC vide para 2.4.11 states quite anomalously that if a Service is provided by a Central Government Department to a State Government Department or vice versa, or by a State Government to another State Government, the same is taxable if such Service does not fall in the Negative List. This restriction defies logic and seems unfair in as much as the meaning of *Government* vide para 2.4.7 of the Guidance Note includes both the Central and the State Governments. The Guidance Note provision in this regard should be withdrawn at the earliest.

Export Of Services

The Export of Services Rules, 2005 has been rescinded and its replacement relegated to a short corner in the largely procedural Service Tax Rules vide Rule No.6A. The new rule has failed to extend the earlier concessions for Service exports in full measure. The change in the Rules *inter alia* requires that for an export of Service to be considered for exemption, the place of provision of Service should be in a non-taxable territory. What this practically means is that the Service being exported should be provided on foreign soil. However, the previous Export of Service Rules did not contain such a draconian restriction and the Department itself, vide its Circular No 111/5/2009-ST dated 24-2-2009, liberally accepted that in the context of Services falling under the erstwhile Rule 3 (1) (iii) of Export of Services Rules, 2005, it would be considered an Export of Service even if all the activities were performed in India, subject to the benefit of the Service accruing outside India. Numerous Services which enjoyed the liberality of the earlier Rule may now be affected by the restrictive new provision. This aspect requires expeditious amelioration by the government.

Coice of Classification in Works Contract Services

The new Service tax Law, while retaining the works contract services covered by the previous Rules, has expanded its scope and included certain works contracts such as repair and maintenance, etc. The construction activity involving residential or commercial or industrial construction is listed among the eligible Works Contract Services. The Service Tax Valuation Rules provide for the manner of arriving at the assessable value of various Works Contract Services including those relating to the construction of buildings. The tax value in these cases is put at 60% of the total amount charged for the Works Contract. As against this, Notification No.26/2012 vide S.No.12 allows an abatement of 75% of total value comprising the value of land and the value of construction, thus prescribing a different method of valuation. The Notification describes the method of valuation as follows:-

Sl. No.	Description of taxable service	Percentage of (value taxable)	Conditions
12.	Construction of a complex, building, civil structure or a part thereof, intended for a sale to a buyer, wholly or partly except where entire consideration is received after issuance of completion certificate by the competent authority.	25	(i) CENVAT credit on inputs used for providing the taxable service has not been taken under the provisions of the CENVAT Credit Rules, 2004. (ii) The value of land is included in the amount charged from the service receiver.

Thus, there are two competing conduits of valuation for the Construction Industry. From the statutory provisions, it is not clear as to the status of either formula in terms of choice for the tax payer. Tax payers would particularly like to know whether they can switch from one channel to another channel, depending upon commercial benefit, from year to year or contract to contract.

Service Tax on the Statutory Provision of Private Justice

We refer to the Service tax on Arbitral Tribunals which does not appear to be a sound proposition legally speaking, particularly in the context of the Education Guide issued by the CBEC admitting that activity for taxability requires ***contractual reciprocity***. In the context of Arbitral Tribunals, the charge of fees by the Arbitral Tribunal to the parties before it does not arise from any contractual reciprocity. There are indeed cases where the parties to the contract would have made an appointment of their respective Arbitrators only, whereas the Presiding Arbitrator would be later chosen by the Arbitrators or by the Court as the case may be, without involving any contractual understanding with the parties to the dispute. Only the provision for and the appointment of Arbitrators would have arisen from the contract. Further, the Arbitral Tribunal is almost a Court and the Awards are enforced by Courts. The functioning of the Arbitral Tribunal is statutorily established and regulated by the Arbitration and Conciliation Act, 1996 passed by the Parliament. In such circumstances, the Service Tax on Arbitral Tribunal amounts to a tax on a quasi-judicial forum.

Indirect Introduction of Taxability by Means of Exemption Notification

Service tax on Fees taken in a Court or Tribunal

The Finance Act 1994, as amended, provides for exemption to fees taken in a Court or Tribunal, which presupposes that there is a contractual reciprocity between the Court/

Tribunal and the fee paying litigant. This is an indirect attempt bring the Judiciary under Service Tax. Can the department withdraw the exemption to the court fees and tax the fees? The Judiciary is a part of *State* and justicing is a part of sovereign function of the State and may not be brought to tax.

Service Tax on the Transfer of a Going Concern as a Whole or as an Independent Part Thereof

The exemption from service tax provided to the transfer of a going concern as a whole or an independent part thereof is similarly questionable. Sale of shares and mergers & acquisitions amounting to transfer of a going concern will now attract service tax, though exempted for the time being. The transfer of a going concern is by no means an identifiable service, let alone a taxable service.

Conclusion

The changes in the Service Tax Law appear to have been introduced well ahead of the curve and without waiting for a consensus on the Goods and Services Tax. Despite a short time of a few months, many of the changes have confounded tax payers and tax experts alike. Many of the provisions contained in the new-look Service Tax bristle with complexity and doubtful legitimacy to say the least. There are many provisions which leave the tax payers confused as to choice and scope. Therefore the government will be well advised to consult all the stakeholders and aim at straightening the wrinkles in the law instead of devising new schemes to further increase the tax burden and ever more load the Law with undue and unwelcome complexity. To start with, the Education guide as an executive interpretation of the new service tax requires to be re-visited to a substantial extent.

Corrigendum

The article titled "An insight into Ethical Governance: A Framework for Nurturing Morality and Values" which appeared on page no 1170 of October 2012 (Vol 47 No 10) issue was co-authored by Ms. Sweety Sadhhukhan, M.Com, M.Phil, NET (JRF), SET, Faculty of Management Science, Dept. of Commerce, Sivanath Sastri College with Shri Anandaraj Saha, M.Com, M.Phil, NET, Lecturer, Dept. of Commerce, Sivanath Sastri College, Kolkata. The name of Ms. Sweety Sadhhukhan had been inadvertently missed out. The Editor sincerely regrets for such omission.

Defence PSUs–The Need to Rationalize The Functioning

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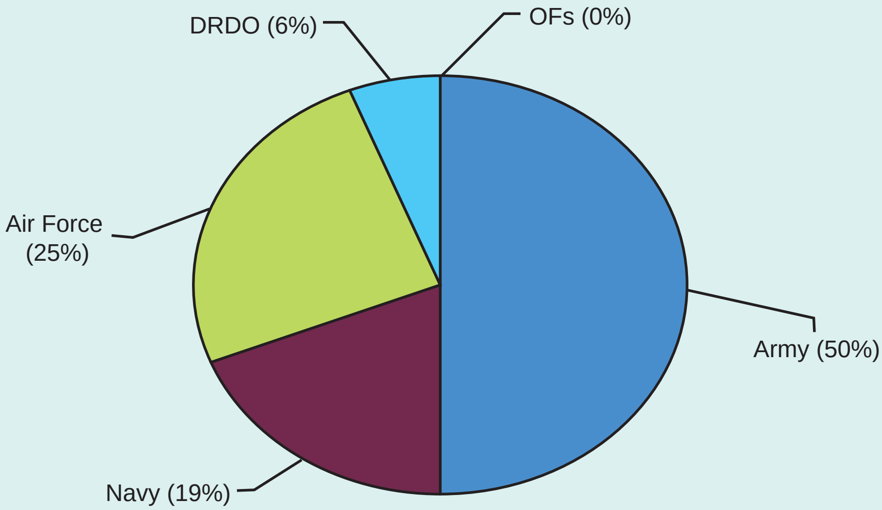
At a time when "efficiency and productivity" are taking over most of the performance evaluation yardsticks and words in corporate India, still there are segments which are hiding themselves under the umbrella of "National Security" without competitively justifying the costs and manner of functioning.

The Union Budget 2012–13, presented to the Parliament on March 16, 2012 hiked the defence outlays to Rs. 1,93,407.29 crore. The funds allocated to defence forces are spent on procurement of arms and ammunition, operational costs like payment of salaries to personnel, maintenance of vehicles, etc. A large chunk of the money allocated flows indirectly to various defence PSUs towards the procurement of equipments by armed forces particularly Airforce, Navy and Army. So when such huge amounts are indirectly flown to Defence PSUs, it is highly critical to evaluate the functioning of the defence PSUs. Even if we exclude the funds dedicated for the modernization of armed forces where the substantial amount flows out of the country, the amount directed towards domestic Defence PSUs is still significant.

Share of Defence Services in Defence Budget 2012–13



It is very important to have tight internal and external security systems in place in a country like India which has bordering countries like Pakistan, Bangladesh and China. Compounding with the external scenario, the internal complex socio-cultural atmosphere is making it a difficult task for the Government to manage and finance the complex funding requirements and social security obligations of the country.

List of major Defence PSUs in India

S.No	Company Name	Incorporated Year
1	BEL Optoelectronic Devices Ltd.	1990
2	BEML Ltd.	1964
3	Bharat Dynamics Ltd.	1970
4	Bharat Electronics Ltd.	1954
5	Garden Reach Shipbuilders & Engineers Ltd.	1960
6	Goa Shipyard Ltd.	1967
7	Hindustan Aeronautics Ltd.	1964
8	Mazagon Dock Ltd.	1934

Although security cannot be compromised, a realistic and thorough in depth analysis needs to be done in to the functioning of various defence public sector undertakings which are involved in the manufacturing, procurement, supply and maintenance of critical armed and non armed equipments to Indian defence forces like Airforce, Navy and Army.

Due to the complex social and political tensions in different parts of the country, there is a greater need for inclusive growth. To achieve this goal the government has to allocate more resources for infrastructure development, health and education, etc. However this is not possible in the current economic scenario unless government take a complete relook at the major spending areas and one such being the defence public sectors.

It is very relevant that whatever the costs that the government incurring in these manufacturing sectors has the cost visibility and financially these projects are feasible. In view of the recent remarks by General VK Singh on the costing and bribes related to Tetra vehicles there is a deeper need to look in to the functioning, profitability and the larger impact of these organizations on the fiscal deficit of the country and real strength of the nation's defence.

For Example, if we look at the "TEJAS –India's Light combat Aircraft", we can understand to a large extent the cost considerations are overlooked by many folds. Although it is a undisputable point that every Indian feels proud of new technological advancements at home, that does not mean we need to spent multi folds of the price at which we can upfront procure the equipments from elsewhere. The LCA project began in 1983 (the name Tejas only came later), with a preliminary allocation of Rs 560 crore for 'feasibility studies and project definition'. By February 2011 a whopping amount of Rs 6,051 crore has been spent on Tejas project although the scope of work has drastically changed from initial perception of idea and concept. Earlier there were wide spread reports on the cost overrun about Tejas which the defence forces and concerned agencies, from time to time rejected. However what need to be looked in to the demand for the LCAs in the country and current cost of the project and technology levels of the current LCAs- whether with the current project cost that has been already spent, whether we should have procured more number and more advanced versions of the LCAs from outside the country with Technology transfer agreements with technology up gradation, etc. If the answer is "Yes" then obviously there is no point to justify the LCAs produced locally.

The Finance Ministers of the country irrespective of which party they belong, are very punctual in taxing the salaried class of the country and it is a naked reality in India that it is only the salaries class who are paying Income taxes without any evasion either due to compulsion or due to lack of alternatives to avoid as the TDS is deducted at source by the employer. So the Government has a larger responsibility to optimally utilize the resources so collected with a more robust and efficient processes and products without any compromise on quality and costs. Although various other players like corporate also paying taxes, the more affected always is the salaries class.

Let us look in to few steps that the government can carry in order to stream line the operations across multi level and multi locality present PSUs of the country catering to the defence forces.

1 Systematic Review of the System

Neither the Government nor the Defence PSU's has any moral right to divert the tax payer's money towards any inefficiency in the Defence PSU's. The government should evaluate whether expenses incurred in a public sector is on par with other corporate or not on suitable comparable basis. Although few of the PSU's and their supporting wings disagree on this sort comparison, at the end of the day the money paid to feed them is earned very hard by people elsewhere. so the common citizens and tax payers too have the right to know whether what the taxes they are paid to government are genuinely and efficiently used elsewhere in the nation building or not.

Due to the multiple pay revisions and commissions enacted by the Governments / respective PSU's there is either very small gap or no gap between the remuneration of private sector employees and public sector employees these days. Moreover the PSU employees either Executives or Non Executives enjoy a bunch of perquisites which cannot be compared with private sector even today.

So when the compensation and perks are either equal or at times higher than the private sector employees, there is no reason why the public sector defence employees should result in to lesser productivity compared to private sector employees.

For Example if we look at the Employee (Executives and Non Executives) strength at one of the Bangalore based Defence PSU's Bangalore complex's F&A function, there are more than 100 persons dedicated towards the function. Considering the said organization is functioning on ERP system and considering their current turnover of Bangalore complex, there may be many questions similar to below that need to be answered in order to judge the efficiency and effectiveness of the function;

1. What are the productivity levels of Defence PSU employees in other countries compared to Private sector employees in those countries?
2. Is the Defence PSU's employee productivity in India is on par with other countries or not?
3. What are the cultural and social reasons which compel the productivity of employees in India to be different from the rest of the globe? Do these reasons apply only to defence PSU employees or all other employees too in the country?
4. Is the ratio of employees in a similarly comparable organization with similar turnover working on similar systems like ERP is same in the referred PSU or not? If not what are the realistic reasons that are contributing to such a scenario?

Once the macro level questions raised above are answered, then one can get in to organization specific micro level reasons to understand correlation between the productivity and employee cost.

Since the most defence PSU's in India works on cost plus model, it is very relevant from national perspective whether the cost itself is rationally arrived with efficient use of resources or the cost arrived by factoring people centric and process centric inefficiencies in to it. If the cost is not reflecting the efficient use of resources then government need to make the alternative arrangements so the resources of the country are well distributed compensating the efficient and effective thereby improving the fiscal performance of the country at macro level.

Apart from Labour cost, the other critical cost that has to be subjected to detailed analysis is Material cost. If not all, most of the defence PSUs in India are producing and supplying equipments to the defence forces of the country. In most cases the technology is either imported under Transfer of technology (TOT) agreements with running royalty payments or at times bought upfront from foreign countries. In very few cases the technology is developed domestically by Defence Research and Development Organization (DRDO) and other establishments engaged in the area and controlled by Government.

2 Comparative Costing Analysis

Similar to the methods used to benchmark the transfer pricing, the government need to evaluate what will be the price of similar defence equipment in another country and what is the price at which it is currently procuring from local defence PSUs. If the price paid to china made / Japan made Radar is 1/10th of what was made locally and if the technology of the equipment is not difficult to transfer to India, then there is no reason why the government should depend up on local PSUs. In an era where the transfer of technology is seamlessly happening across the globe cutting across geographical boundaries and not withstanding defence and non defence sectors, the Government of India should logically evaluate the possibility of procuring these equipments wherever possible from external sources limiting the domestic players to key competitive self reliance and strategic areas. Even in areas where the local defence PSUs claims that they need to supply the equipments from national security perspective, the Government should set a clear time bound goals of cost improvement and cost competitiveness.

3 Removing Entry Barriers

Even today after 20 years of following Liberalization economic policies, still large chunk of the defence supply sector in India is still under the monopoly of the government / Defence PSUs which are indirectly controlled by the Government of India. So government needs to evaluate the possibility of allowing the private players with proper process in place regarding their functioning in defece sector. Once the private players are allowed, both the private and PSUs should have the equal opportunity to supply with quality and price being the uncompromising criterias. If the particular Defence PSU is not able to compete with other private sector supplier to defence, then it should be allowed to have natural death rather than pumping artificial financial oxygen by the government wasting the tax payer's money.

It is not too long we have seen in case of Indian Telephone Industries (ITI) and Bharat Sanchar Nigam Limited (BSNL), how the entry of private and competitive forces changes the quality of the services and products being offered to the customers. In both the cases of ITI and BSNL, we have seen how the cost plus models protected by the Governments crumbles when the inefficiencies are not adequately identified and rectified in a open market.

4 Inventory Check

Year on year the armed forces are procuring the equipments from Defence PSUs. However there has been wide spread allegations that so procured equipments are not maintained properly and there is no up to date inventory check. If by any reason if the war broke out with enemy countries, then identifying which item available where may be a million dollar question and there by pushing the armed forces again to place further supply order. So critical analysis of the current stock levels of various equipments and their functional levels need to be evaluated. There is no point in keep on procuring the items and then dumping them in to Agra CDA area every year.

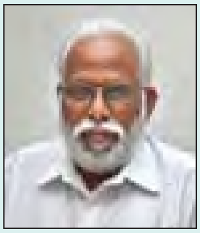
Advantages of allowing private players in to the defence PSU segment:

- Whoever is efficient and effective either private or PSUs will survive and there by contributing to national growth in a positive way.
- The fiscal deficit will not grow due to wrong funding of any inefficient process and systems.
- In the long run this translates in to better work culture and thereby improves the margins and satisfaction levels among the suppliers and consumers.
- The funds saved through improvements of cost or procurement of equipments at low cost and better quality avenues, the government can divert the funds to infrastructure growth and development of the country.
- In most PSUs in India if not all, the employees have been segregated as Executives and Non-Executives. Unfortunately this over a period of time grown with deeper roots and developed in to a new method of division of society at work places. Unfortunately without realizing that the pride of work comes with the abilities to deliver and the proven track record to deliver against expected benchmark expectations, so called executives creating this bad work culture there by spoiling the relations at work place. So allowing the private players over a period of time change the field and expose the people who are trying to take the prides in mere designations without displaying adequate productivity.
- Recently we have seen the role of BEML ltd in the "Tetra vehicle scam" which the Central Bureau of Investigation (CBI) is currently investigating. So any such safeguards voluntarily developed by these PSUs under the shadow of National security will also come to light when a deeper review of functioning and financial feasibility analysis are undertaken periodically by a independent agency like Comptroller and Auditor General of India(CAG).

However most of the organizations and various stake holders in those organizations operating in the field arguing against the privatization, quoting the below reasons;

1. **Job Security:** In Today's economy, every person who has the ability to perform has the opportunity to survive in one place or the other. If the person has no abilities to deliver obviously has no right to talk about the right on job security. Although the provision for differently abled /disabled persons should be made with private sectors, the properly abled persons asking for job protection irrespective of performance merely will not economically feasible.
2. **Exploitation:** In traditional days where the opportunities are less due to the only presence of public sectors in the country. However as we moved on with Liberalization, Privatization and Globalization (LPGs) polices post he New Industrial policy of 1991, the opportunities are widened in the country with the entry of both domestic and international players in to the country. So no organization can attract and retain the competent work force in the long run by resorting to policies which results in to the exploitation of man power.

Considering the various scenarios and arguments in favour and against the privatization and other strategic options, certainly the time has come for the government to look in the realistic and effective ways of procuring the cost effective and qualitative products without compromising on national security. People leading such organization need to understand that the profitability figure mentioned in the annual financial reports has a true value only when such profits earned in a competitive environment and not in a protected market. Even if the market is protected, the costs of the equipment supplied should always be comparable to a similar product sold elsewhere under open market conditions with similar features otherwise the fiscal deficit year on year goes on increasing with unproductive spent in these areas by the government and nothing will be identified as long as the mask of national security is not removed.



Knowledge Management In Banks

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Introduction

Reserve Bank of India in its report on Trend and Progress of Banking in India: 2010-11 has stated that while technological advancement in Information Technology have led to discernible improvement in the efficiency of Banking services, banks have not gained in terms of efficiency **'partly'** because of lack of Business Process Re-engineering and the challenge is to leverage technology optimally to balance growth, efficiency and risk management objectives. Here I consider **'partly'** as a significantly meaningful word, which ignited my mind to look for the way forward and find a comprehensive solution to improve the efficiency of the Public Sector Banks and help them reach higher levels in the value chain. The developments in last two decades, viz., globalization, consolidation, deregulation and diversification of the Indian Banking System have been greatly responsible for the business of banking becoming increasingly complex and riskier. These factors have been posing tough challenge to the managers of the Public Sector Banks thus creating an urgent need for various initiatives like Risk Management, Liquidity Management, Asset-Liability-Maturity Management, Capital Management, Credit & NPA Management, Technology Management and Skill & Knowledge Management. The process of Globalization has been gradual in the Indian Financial System, which predominantly is led by the Banking Institutions. The check posts and speed barriers created by Trade Unions and Left Wing Political Parties are attributed with the gradualization of the process of Globalization. But for the resistance created by these organisations, the level of penetration and integration of world economies would have been more deeper and seamless, which would have lead to higher levels of financial stress for the Banking System, especially in the post financial crisis era. The initiative of Financial Inclusion has added further challenge to the Banks more particularly the Public Sector Banks. These Banks are not only the commercial and profit making institutions but are also construed as the vehicles of social & economic transformation in a country having a very complex demographic mix.

RBI has been playing an important role in guiding the banks and creating a robust institutional framework to make the banking systems in Indian financially strong which can be seen from the fact that Public Sector Banks have remained well-capitalized despite phenomenal growth in their Loan Portfolio. The enhanced Basel-II norms are complied with while we are on our way forward to embrace Basel-III norms. Innovation on technology front has revolutionized the product development and also the new systems & processes leading to faster delivery of products and services to the customers and economizing on the cost of processes. But it is important for us to understand that the computers cannot question or re-interpret their programmed logic and pre-coded assumptions and hence Human Resources bestowed with these capabilities assume a significant role to manage not only the processes but the entire technology application in the banks. The Human Resources should be such to have the capabilities to handle and manage today's business and be possessing a long term vision to be future ready. It is easy to acquire human resources with given talent but also to make them future-ready is quite a complex and ongoing process. It brings into focus the need for Knowledge Management on a continuous basis in the Banks.

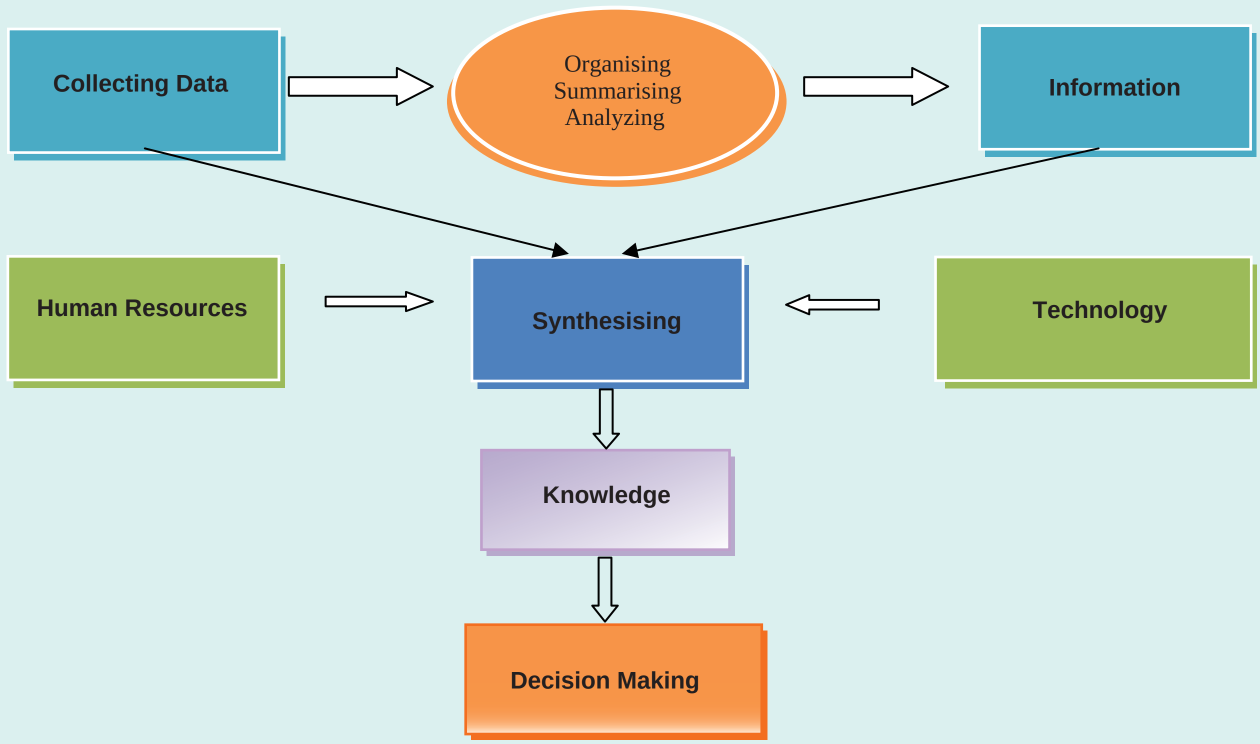
Knowledge Management

Do the Public Sector Banks in India have the system of Knowledge Management in place? There is a big question mark. But a study of Public Sector Banks revealed that an informal structure of Knowledge Management existed in these banks in the form of Training Institutions, Human Resources Development Department and some banks even have Archives whereby documenting the journey of the institutional growth, important past contributions, reaching out to certain important segments, core competence etc. Some banks even had documentaries about the growth history and success stories of individual and team performances and occasionally showed such documentaries to inspite the present pool of Human Resources. In today's context, it can be called as a **"Push Strategy"** whereby the banks encode the knowledge into a shared knowledge repository. On the other hand, the **"Pull Strategy"** of Knowledge Management revolves around seeking knowledge from an Expert.

With this background, it would be appropriate to discuss Knowledge Management in the banks in a wider perspective.

Before arriving at a definition of Knowledge Management, we must try to understand as to what is knowledge and in what way it is different from information. At the outset it would suffice to say that the knowledge and information are not identical. While the information in regarded as atomic & static, the knowledge is considered associative, rich, multi-layered, multi-faceted, contextual and dynamic. Information is not knowledge unless someone uses it. Thus the information is having a potential of getting converted into knowledge. A bank can recruit talented and knowledgeable people but unless their knowledge is used for the betterment of the organisation, it is not worth it. A natural corollary of this discussion is that Knowledge Management refers to effectively utilizing the collective knowledge of all the people in the organisation for Best Performance outcomes and enhanced value proposition.

There were no systematic efforts in the Public Sector Banks to invest some resources in Knowledge Management till 2005-06. When the Government of India set up a Knowledge Commission of India in 2005 under the chairmanship of Sam Pitroda, the country was awakened to the idea of Knowledge Management in a formal & structural manner. The Knowledge Commission of India being a national body was to focus on the strategical framework to enhance the human capabilities through the process of making the educational system more relevant and realistic. It accordingly submitted its reports on an annual basis to the Government of India and those reports encompassed the Technical Education, Vocational Education, Professional Education and Training and so on. The Knowledge Commission invited criticism from different quarters for its opposing view on the Government's move on the reservation in Educational Institutions of Excellence in the country. Although the terms of the Knowledge Commission were extended by 6 months, it eventually was wound up in 2009. But consequently, different organisations including banks developed awareness about the significance of Knowledge Management. It is in this manner the information came to be recognized as an Asset for the organisation. The banks also started treating data base, documents, policies, procedures, employee expertise, etc., as an important Asset. From a commercial standpoint, every asset needs to be managed to get commercial value for the organisation. The following flow chart would help us in understanding the issue better:



This flow chart reveals 4 stages of converting data into knowledge.

STAGE – I: Collecting the data.
STAGE – II: Organizing, Summarizing and Analyzing the data to convert the same into information.
STAGE – III: Synthesizing the information by blending it with Human & Technology variables to convert the information into knowledge.
STAGE – IV: Use of knowledge by Managers at different levels of hierarchy to take decisions. The decisions so made would be better in quality and content.

Defining Knowledge Management

It means to capture, retain, refine and re-use the knowledge by fitting all the pieces of information together and convey the same in an effective manner to help take such informed decisions in the organisations. Such informed decisions would help improve the quality of products & services in the banks. It can therefore be inferred that the Knowledge Management involves—

a. Capturing, planning, organizing, inter-connecting and providing access to the intellectual capital of the organisation through the use of technology and process.
b. Directing and supervising such assets like knowledge, people, processes and technology which are integral part of Knowledge Management.
c. Sharing of Individual Human Intellectual Capital with others in the organisations to enhance the organisation's overall capabilities.
d. Positive application of knowledge which is essential for effective Knowledge Management.

Effectively sharing information vertically & horizontally in the organisation would result in enhancing the efficiency of Human Resources in the banks. Consequently, it will provide a competitive advantage to the banks and help them face the competition with ease. To take the best possible advantage of the intellectual capital in banks, we need to leverage our Information Technology Infrastructure and IT enabled tools vis-à-vis our Human Resources as it is vital in any service industry. It can therefore be said that the Knowledge Management is a strategic HRM tool for better productivity and organizational effectiveness.

The role of Human Resources in banks assumes greater significance in the process of Knowledge Management for the simple reason that simple technology can also generate high performance when it is used by smart minds of motivated and committed people. The smart minds possess huge potential to outperform even under adverse business conditions. It can be explained with the help of a live example given below—

CUSTOMER: Good Morning Manager, I am a Non Resident customer of your Bank having huge FCNR deposits.
MANAGER: Good Morning Madam, what can I do to help you ?
CUSTOMER: Please close my two FCNR deposits and give me a counter draft in US Dollars in favour of a local branch of Standard Chartered Bank which is offering 1% extra interest.
MANAGER: Madam, I will do that but let me tell you that Stanchart cannot offer a cup of tea from my canteen when you visit them.
CUSTOMER: I am touched by your gesture. I do not want 1% extra interest. Please renew my deposits.

There were cheers on both the faces without involving any technological intervention. The smart mind outperformed!

It is therefore suggested that while focusing on technological processes, the banks must not lose sight of creating smart minds through the process of documenting and sharing the success stories on a perpetual basis, of course, duly factoring it for contemporary relevance.

In view of the foregoing discussion, we can attempt a realistic and comprehensive definition of "Knowledge Management" as under:

"Knowledge Management is a process to identify, capture, structure, organize, analyze value, share and leverage an organisation's intellectual assets collectively to enhance the performance outcome and competitiveness of the individuals, teams and eventually of the enterprise".

It must be borne in mind that the whole process of Knowledge Management needs to be contextualized and synergized to be more effective. In an environmental perspective, Knowledge Management refers to the critical issues of organisational adaptations, survival and competence in the face of radical and discontinuous environmental changes. Information Technology plays a vital role in implementation of the process of Knowledge Management. There is a greater need to transform Knowledge Management from a theoretical concept to a programmatic and thoughtful application in the banks to help them meet the greater opportunities and challenges.

Implementation Strategies for banks

The banking institutions are service organisations which are predominantly driven by their Human Resources, technology, processes, innovation and strategic collaborations across products, functions and business units. It thus calls for creating a huge talent pool, which the banks need to upskill and re-skill on a continuous and sustainable basis. The Human Resources should be encouraged to achieve breakthrough innovations leading to enhanced performance outcomes through the resultant competitive advantage and upscale the enterprise value proposition. The main strategies to achieve this would include—

i. Common understanding of the meaning and definition of Knowledge Management by all concerned in the bank.
ii. Acceptance of the process of Knowledge Management across hierarchy in the bank.
iii. Willingness on the part of employees to be subjected to the process of Knowledge Management.
iv. Effective use of technology and information.
v. An objective and robust system to evaluate the efficacy and effectiveness of Knowledge Management on a continuous basis.
vi. Sustained innovation and cross functional synergies.

We need to have a healthy blend of skill and wisdom for the success and growth of our banking institutions, more particularly, in Public Sector. The present position in Public Sector banks possesses a huge challenge in the form of a wide generation gap from the point of view of the age profile of the employees of the bank. It has challenged and threatened the homogeneity of the people working in the Public Sector banks. With these constraints, the banks need to enhance the key initiatives for success of Knowledge Management in Public sector banks. Some of such initiatives are discussed below:

(a) Information Technology Infrastructure

Most of the have been buying the IT capabilities from the companies which do not have domain knowledge of the business of banking. Hence the software developed for the banks is primarily an encrypted version of the manual systems and procedures. It is periodically upgraded with a view to enhancing the efficiency in transaction processing. There is a visible gap between the improved versions of technology and the skill levels of the user at front-end and also at back-end. There is need to create compatibility between the technology and its users for the success of the programme. The reduced dependence on external agencies for technology upgradation and connectivity will help enhance the level of success of the Knowledge Management in the banks.

(b) Skill Sharing

There are many ways of sharing the knowledge and skill in the organisation. Some of them are mentioned hereunder -

1. Mentoring
2. Grooming
3. Sharing of success stories
4. Creating Role Models
5. Trainings
6. Circulars/Manuals
7. Webcasts/Video-conferencing

It would be worthwhile to discuss these variables from a banking perspective.

Mentoring

Mentoring refers to a situation whereby an experienced and successful business leader assumes responsibility of transmitting not only the knowledge and skill possessed by him to the mentee, but also guides him about newer aspects of business leadership in an emerging environment. It thus becomes a transmission of the skills and wisdom to the younger generation to ensure the continuity of the business culture, ethos and values. A better understanding of the organisational culture, history, values and ethos has a significant impact on the sustainability of the organisation. The Public Sector banks have largely discontinued the practice of Mentoring. In view of the large recruitment of younger generation of Human Resources in all the Public Sector Banks to meet the challenge posed by growing attrition in the form of retirement, resignations, terminations on one hand and phenomenal growth of business & expansion of the network of branches on the other, the mentoring assumes a more significant place in handling the issues relating to the organisational culture in Public Sector Banks.

Grooming

Grooming and **Mentoring** are often confused to be one and the same thing despite being significantly different from each other. In an ordinary sense, grooming is related and referred to preparing a person for an office or an occasion. Thus sharing of job knowledge at work place with a junior employee is called grooming. It helps a junior level functionary to develop the capability of shouldering higher responsibilities in his department. It thus helps in succession planning at various levels of organisational hierarchy. Grooming to be successful in banks would essentially need a large number of able and willing seniors prepared to go beyond the call of duty to not only perform the tasks allotted to them but also ensure that the people working under them are also given a gradual exposure to the higher level of jobs to help them become future ready. The large generation gap between **the mentor** and **the mentee** and the **groomer** and the **gromee** may also call for introduction of newer concept like "**Reverse Mentoring**". The advancement and innovation of technology in banks have rendered many senior employees bereft of the skills required to handle new technology, whereas the new recruits pre-posses the said technology-skills in an adequate measure. Under such situations, the new recruits could be asked to share their knowledge and skills with their senior colleagues. This process would thus be a "**Reverse**

Mentoring". It would also be equally effective in enhancing the level of departmental efficiency performance outcomes and employer value proposition. Such measures will help the Banks to gain competitive advantage in the emerging environment in the banking space.

Sharing of success stories

The practice of sharing success stories provides a different and newer insight even into the ordinary issues. It also acts as an inspirational tool for many in the organisation. It is very important for those involved in this process to carefully select good success stories which could really create an inspirational impact amongst the members of the larger group. It would be equally important to select a target group which will have the proximate role functions relatable to the role functions of the employee whose success story is intended to be shared. It can be illustrated with the help of a real example given below—

An individual was maintaining a Savings Bank account at a branch of a Public Sector Bank at Lucknow. He approached the Branch Manager with a request for a Home Loan. The Branch Manager gave him an application form alongwith a check-list of documents/ formalities required to consider sanction of a Home Loan. The loan amount fell under the discretionary powers of the Regional Manager. The account holder completed the required formalities and submitted his loan proposal at the branch. The Branch Manager processed the application on the same day and finding the application in order, prepared his appraisal note with his recommendations to Regional Office and requested them to examine/scrutinize the acceptability of the proposal. Finding the proposal in order, Regional Office accorded sanction of Home Loan in a matter of couple of hours. The Branch Manager carried the sanction letter personally and advised the party to come and complete the formalities to facilitate disbursement of the Home Loan. The party was unbelievably surprised joyfully. He came to the branch to complete the formalities. Impressed with such a wonderful attention given by the Bank, he wanted to help the branch and opened two Savings Bank accounts for two of the projects of the Government which were under his control. The branch opened the SB accounts readily and within two weeks, these two accounts had a balance of more than Rs.55 crores, which was more than double of the then existing business of the branch. So easily getting such huge but low cost funds had added not only to the business growth of the branch but also helped the branch to earn substantial profit due to availability of low cost resources.

If such a success story is shared and replicated successfully in different branches at different places, it would go a long way to enhance the level of performance outcomes and help the branch to have a competitive advantage. It is one of the ways to enhance the enterprise value proposition. Every bank will have many more such success stories, which if shared in right quarters would certainly inspire the people to attain higher goals without much efforts. Those who practice such customer service models are easily the 'Best Bankers'.

Creating Role Models

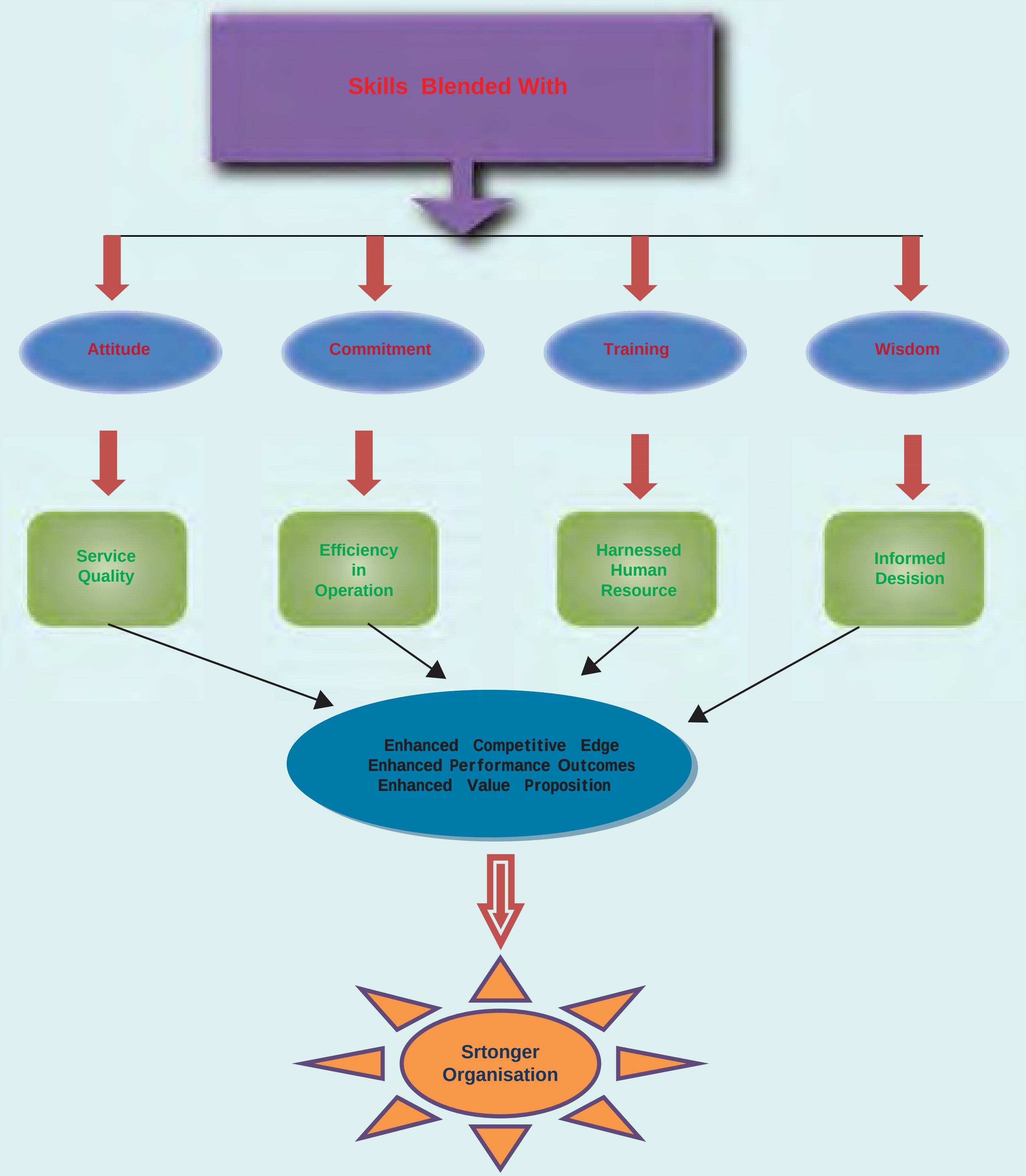
Every organisation can boast of having some outstanding performers. Individual performances do count for the growth of the organisation. The team spirit within the organisation like a Bank will lead to synergy effect whereby the collective performance of the team would invariably be more than the sum total of individual performances by each one of them without being part of the team. Even in the team, the role play by different members can be easily distinguished as 'GOOD', 'BETTER' and 'THE BEST'. Apart from inherent and required skills of the team players, it is possible to see the distinguished leaders, who apparently are admired by others in the team for their special qualities like transparency, values, ethics, honesty, integrity, leadership traits etc. Such persons gradually attain the status of **'Role Model'** in their team and also in the entire organisation. In a service industry like banks, the traits and valuable attributes mentioned in the earlier sentence have a significantly greater importance. The younger generation and others who are in the lower hierarchy start treating such outstanding performers as their 'Role Models' and try to tread the similar trajectory. Those who can do it successfully on a sustained basis will themselves become the 'Role Models' for another generation which would follow them. This process needs to be followed consciously and continuously in the banks to be institutionalized. It would certainly give an added edge to the banks which succeed in institutionalizing such valuable practices of Role Modeling in a banking institution.

Trainings

Training system occupies a pivotal role in the banking institutions in our country. It is considered responsible for the skill levels of the people in the banks. Last two decades have been witnessing the growth of globalization slowly but steadily. Yesterday's things have become obsolete today in the spheres of technology, products, services, systems & procedures and so on. Changes in buyer demografhics, preferences, innovations, customer attitudes, life styles and growing use of social networking portals have created the need for new ideas, which had necessitated emergence of knowledge workers. Even if the banks recruit people with pre-possessed knowledge to meet the current requirements, they will be left behind in the competitive race, if they do not further learn, unlearn and relearn. To make this process a success, the banks would need a highly progressive training culture. The hitherto practiced training models need to undergo changes to best leverage the teaching technology and available kits.

The focus of training has to shift to managing the change, uncertainties, complexities, strategic information etc. Another important area of focus for the training system should be the attitudinal changes of the Human Resources of the banks. Appropriate skills blended with positive attitude can improve the quality of front-end customer service and hence help enhance the image of the banks. In the area of Knowledge Management, I consider skill-blending as an important aspect, which need to be emphasized in the training programmes to meet the emerging challenges. There are four important variables which if appropriately blended with skill can produce higher performance outcomes. The skills blended with attitude, commitment, training and wisdom would lead to high quality customer service, efficiency in operations, harnessed Human Resources and more informed decision at the different levels of hierarchy in the banks.

It can be better depicted with the help of the following diagram:



Cross-functional trainings need to assume larger role as a part of Knowledge Management in the banks. There are high degrees of inter-linkages in different functional areas of the vast banking business. It is therefore important for the functional specialists to understand broadly the role and functioning of different cross-functional Teams and better appreciation for each other's roles. It can be made possible by imparting cross-functional trainings. The introduction of cross-functional trainings in the banks can deliver the following advantages:

i. Business would gain security.
ii. It would ensure continuity of service.
iii. Developing mutual respect for other functional areas.
iv. Understand and appreciate each employee's contributions.
v. Great morale booster.
vi. Rounded growth for Human Resources becomes feasible.
vii. Creation of an enormous asset in the form of motivated Human Resources Pool.

Circulars and Manuals

The systems and procedures are documented in the Manuals while the circulars serve the purpose of updation and modification of coded procedures. The circulars are also used to create awareness about new products and policies. The organisations having a culture of sharing the contents of the circulars with all concerned are invariably the well informed organisations. In banking institutions, the circulars play an important role in creating awareness amongst the people. The advent of Information Technology has made the use of circulars very simple while has also enhanced its effectiveness as thousands of people in the banks can simultaneously open the system and can familiarize themselves with the contents of the circulars.

Webcasts/Video-conferencing

Information Technology revolution has greatly enhanced the access of Top Executives to the people in different locations in the banks. It has become an easy and effective medium of communicating the policy objectives. An effective use of webcasts and Video-conferencing is highly cost-effective. The banks can use these mediums to cut on travel cost, save time and also have cross interaction. The knowledge sharing has been made easy by webcasts and video-conferencing.

The way ahead

A Human Resource Pool which is well trained in people, process and technology management can leverage strategic opportunities and challenges with equal ease. To create a workable Knowledge Management Infrastructure in banks, there is need to identify—

- Knowledge Managers supported by
  i. Knowledge Coordinators
  ii. Knowledge Engineers
  iii. Knowledge Architects
  iv. Knowledge Analysts
  v. Knowledge Leaders
  vi. Information Officers
- Knowledge and its source – internal & external.
- Capturing techniques for required knowledge synthesizing process to leverage knowledge.
- Need for innovation: Technology, Process and Products.

Those who can develop capability of figuring out next best thing and prepare themselves in advance in terms of skilled Human Resources and appropriate technology platforms only can ride the next wave of healthy and sustainable growth in emerging banking space. The basic requirement to attain such levels would be to identify such talents which have the capability of extracting '**Knowledge gems**' from the '**Ocean of Information**'.

Success Proposition:

For Knowledge Management to be successful in the banks, the following factors will be vital –

- Documenting the captured knowledge.
- Understanding the definition of knowledge.
- Effective delegation.
- Nurturing people with rounded growth.
- Averting indispensability by grooming second line leadership pipelines.
- Making content submission mandatory & rewarding.
- Making the knowledge sharing contextual.
- Converting learning and training into an organisational culture with perpetuality.
- Enhancing the stock of trained trainers.

These critical factors among others will play a catalystic role in growth of Knowledge Management in banks. The business leaders should demonstrate courage and intuitiveness to invest in Knowledge Management with a long term commitment to enhance stake-holders' value. Knowledge Management has got great potential to become a success in Public Sector Banks in India.

Performance Improvement–Need For Continuous Improvement

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Abstract

Only constant thing in any business is change. As a business goes through different phases of change, it thrives for better performance. Improving business performance is not a onetime exercise, it is a continuous process. This article, through a case study, highlights how a nascent organization forms through performance improvement initiative of a Trans Global aviation industry and leads to growth a fairly successful independent organization; its mitigation of growth challenges and subsequent global economic crisis leading to its retrospection of its performance norms. Through continued focus on improving its performance and identifying better processes to perform and deliver its business objectives, this organization grows to become stronger entity; reinvents itself through challenging its own performance level and moving to higher level of performance.

The article also highlights through live example how performance challenges are identified and appropriate/applicable solutions are aligned to address specific challenges; leading to multi-dimensional performance improvements. We observe that improvements were achieved through initial restructuring initiative to hiving it off as an independent entity to multiple phases of process improvements. Of course there were many other operational strategic initiative that we have not covered in the article, since the focus was more on process performance initiative.

Introduction

Globalisation of business has driven industries to continuously innovate and redefine their businesses to remain profitable and demonstrate strong performances to their stakeholders. This not only happens through developing right strategies, but also through adopting continuous performance improvement measures. While manufacturing industry has opportunities to improve cost through better utilization of assets, alternate improved production process, better supply chain, services industries options are more limited. In this article, we will look at one service industry in particular and how it evolved through strategic initiatives as well as adopting a continuous performance improvement framework.

Organisation

A leading global airline company, with a fleet strength of more than 200 and in business for more than 75 years, was battling the continued cost escalation and pressure on margin. It not only took few strong strategic steps, but also explored opportunities to improve its operation cost. It focussed on improving support services cost and set up Shared Service Centres (SSC) to manage back office operations. In the initial years, this initiative led to sizeable savings in operating cost and improved & better fiscal discipline. However, it realised that consolidating multiple SSCs into a single SSC would provide it with better cost performance through scale of operation. It took a strategic decision to structure this organisation differently and the SSC was made a subsidiary. This allowed it to define new organisation's objective and mission focussed on providing back office operation (BPO) services to the airline, with an option to extend the services to other airlines. This strategic initiative allowed it to convert one cost centre to a profit centre.

In late 1990s, the BPO organisation realised that with strength of more than 1500 staff, its operation centre should explore alternate locations to cut down operating cost. It decided to set up off-shore facility. Its success was not limited to the area of back office operation for support processes only, but extended to offer many value added information analysis to the airlines that led to increased revenue and profitability. Subsequently the airline decided to "sell" the subsidiary, with committed tie up on being a service receiver for a given period.

Margin Challenges

Over years the BPO organisation grew its portfolio of services from Travel and Leisure to Banking and Financial Services, Insurance, Transportation, Manufacturing, Utilities, Healthcare, Consumer Goods, Retail and Professional Services. It set up delivery centres (with more than 20 physical locations) across the globe, with presence in five continents, went through IPO. With staff strength of more than 20,000, a global client base of more than 200 and with annual revenue of more than \$300 Million, the global financial industry turmoil hit the company hard. With depleting revenue and largely committed cost structure, its priority moved to relook on strategic initiatives, including improving operational cost.

A major cost element for BPO organisations are people related cost—direct salary cost, office space, transportation cost, employee welfare cost, infrastructure cost etc. Although BPO runs in multiple shifts, effective utilisation of infrastructure does not get utilised three times due to business constraints. We can safely take utilisation at 1.6 for the organisation, although we have seen the same to go up to 1.7 or 1.8 in some BPO organisations. As the organisation prices its services, it has to consider not only the cost elements, but also competitive market forces. Secondly, service contracts are multiyear contracts and market volatility plays a major role in profitability. All these factors lead to pressure on sustainable margin.

Sample Case

As a service provider in the BPO space, this organisation has multiple clients. The nature of BPO services also vary. For some clients, they carry out only back office processes that do not require any regular interactions with either the client or client's end client. Whereas for some clients, they receive or make calls to the end client and on the basis of the interactions, they complete a process. In both cases, a process completion demands carrying out many sub-processes and each sub-process may have multiple steps or actions.

We are going to look at one such process to elaborate how process performances can be improved to achieve a better business performance. Before we get into the specific process details, it will be useful to share the process of identifying candidate processes. Choice of right candidate process is very important—a wrong choice can derail any initiative. Selection process also has to be focussed and short. If one spends long duration of time and energy (and associated cost) in identification process itself, it does not help the cause. Project sponsor and other stakeholders would typically lose interest and initial momentum gets lost. Hence, experienced resources need to be involved in process selection.

We went through a half day briefing on key business units and its performance parameters. This process of "getting to know the business" gave us key inputs on narrowing down our choice to couple of business units only. Once, we narrowed our choices, we went through an hour of presentation / discussion with respective business units to get an overview of their key challenges and its associated service areas / clients. By the end of the day (after having spent 3 hours with three business units and a couple of hours on internal discussions), we were ready with our choice of candidate processes. Candidate processes were chosen on following key parameters—

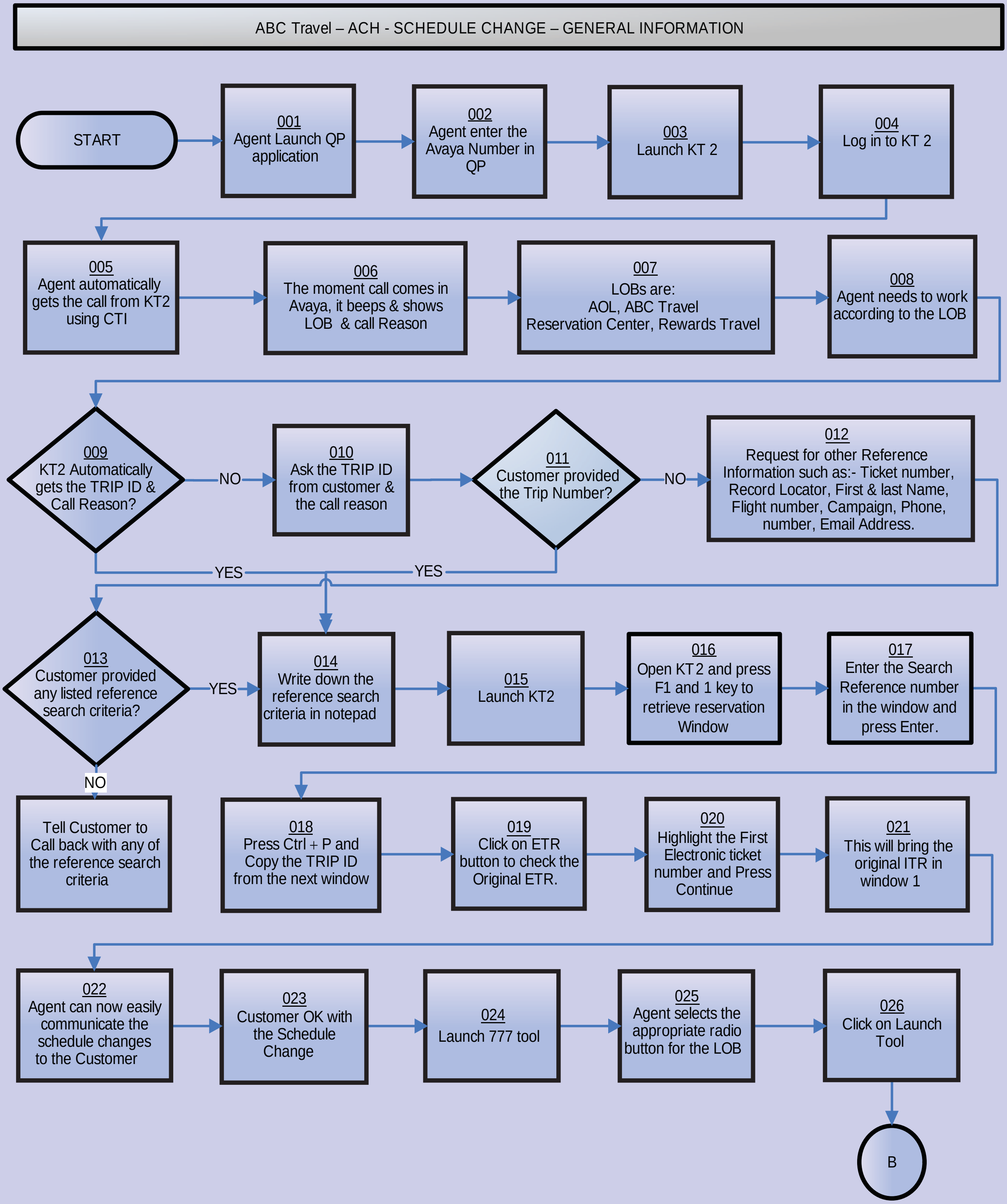
1. Nature of the process—is it significantly voice or has a good mix of non-voice steps?
2. How many applications are being used?
3. What is the level of automation?
4. How many agents are working on the process?
5. How deep is the client relationship, in terms of revenue, number of years of relationship etc.?
6. What is the level of application level integration?
7. What platforms are being used for the applications?

Our next step was to present our choices to respective business units and also provide them with our rationale. Final choice of process is not always based on objective criteria. It is definitely supported by initial objective evaluations, but finally business has to take a decision on choosing the candidate process based on how it is likely to impact their specific client and their future potential stronger relationship.

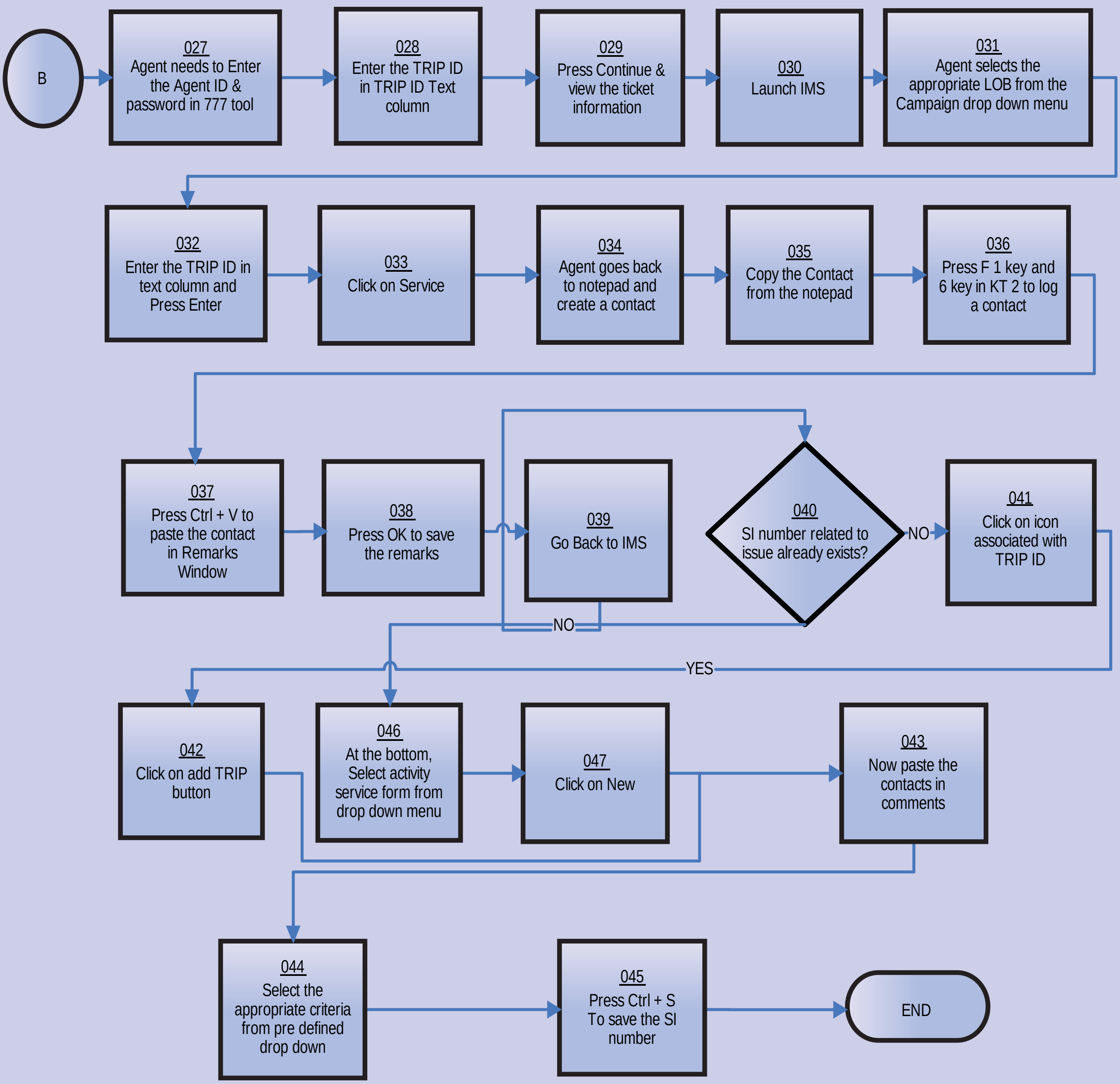
The process, we finally identified as the candidate process, (the process flow is depicted in diagram 1.1 and 1.2) is for Air Car Hotel Booking (Schedule Change) for a large multinational travel company. Although the flow diagram captures all steps that are carried out by an agent (the person we receives a call from the passenger or a person who wants to make changes to an existing booking for Air, Car and Hotel. When a caller calls the listed number, the caller gets directed to an IVR (Interactive Voice Response) that guides the call to the appropriate agent.

An agent starts her day through signing into her system and launching appropriate applications that links her to a workstation (steps 1 through 4). When a call comes to her and she picks it up (steps 5 & 6), she already has basic information about the call like reason for the call as well as Line of Business (LOB—the business has multiple LOBs and they are AOL, ABC Travel, Reservation Centre, Rewards Travel). Based on the LOB, she would have to choose appropriate actions. Based on the information provided by the caller and request, she would need to carry out appropriate changes, confirm the changes with the caller, record information on the system and complete the process through appropriate closure process (steps 7 through 45).

1.1: Flow Diagram of Sample Process—Part 1



1.2: Flow Diagram of Sample Process—Part 2



A look at this process flow gives us key information—

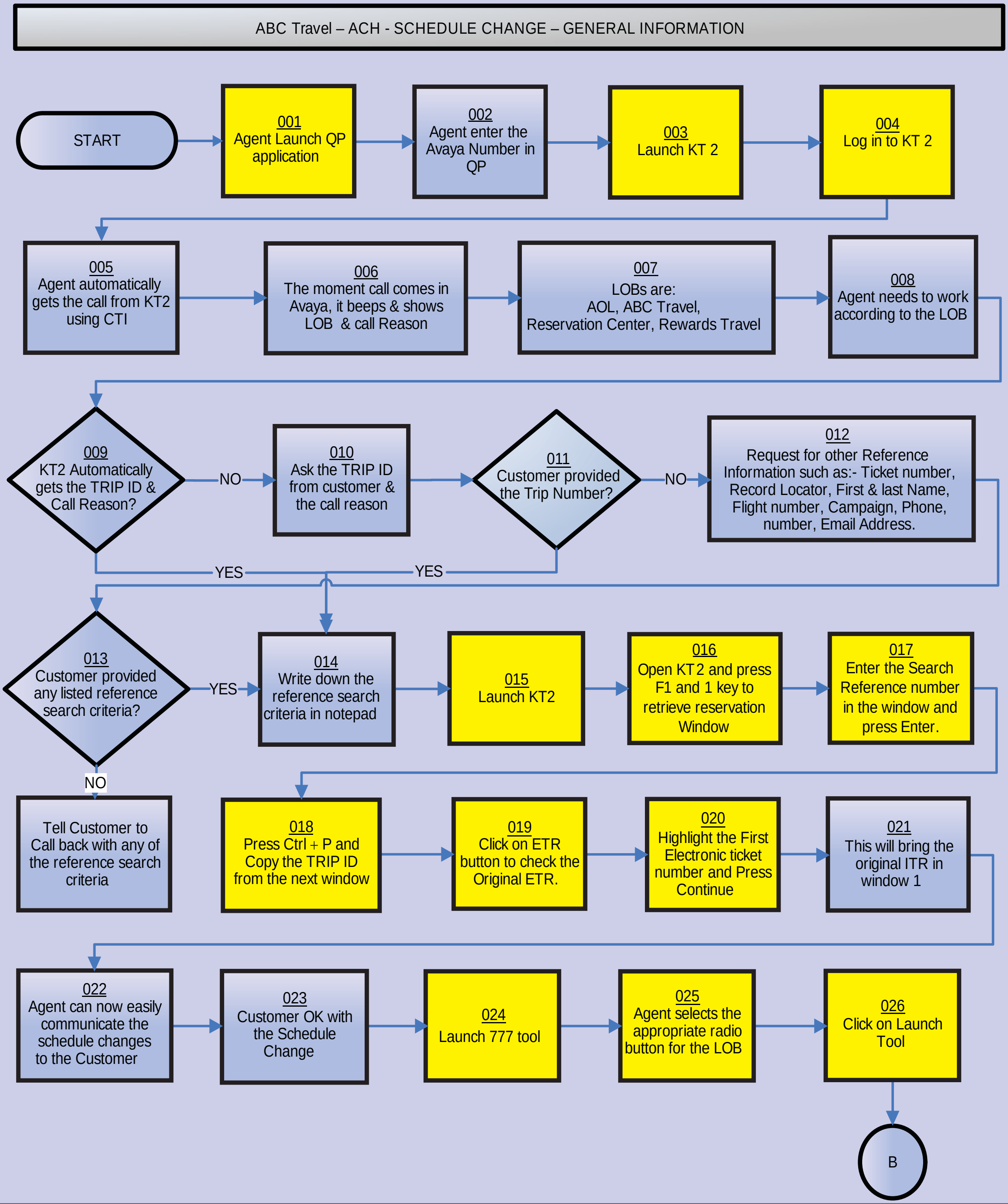
1. Every call leads to starting few applications.
2. She has to use multiple applications (KT2, 777, IMS, Notepad, MS Excel etc.) while on the call.
3. Some of the applications are even launched multiple times.
4. Same data is to be entered multiple times.
5. She has to switch from one application window to another many times.

What do we learn from these? We learn that there are non-value added activities that, if can be avoided, can lead to savings in time and effort. Let us look at some numbers, with few assumptions. If an agent takes 6 calls an hour and 70% of her time is actually spent with the caller and the balance time is spent on the system to move or process information, we have 18 minutes per hour being spent on systems. A reduction of 40% of 18 minutes would mean a saving of overall 12%. Thus average duration of a call will come down from 10 minutes to 8.8 minutes, leading to additional 0.8 calls per hour. This is direct benefit. Indirect benefits would include more satisfied callers, leading to better business and higher revenue.

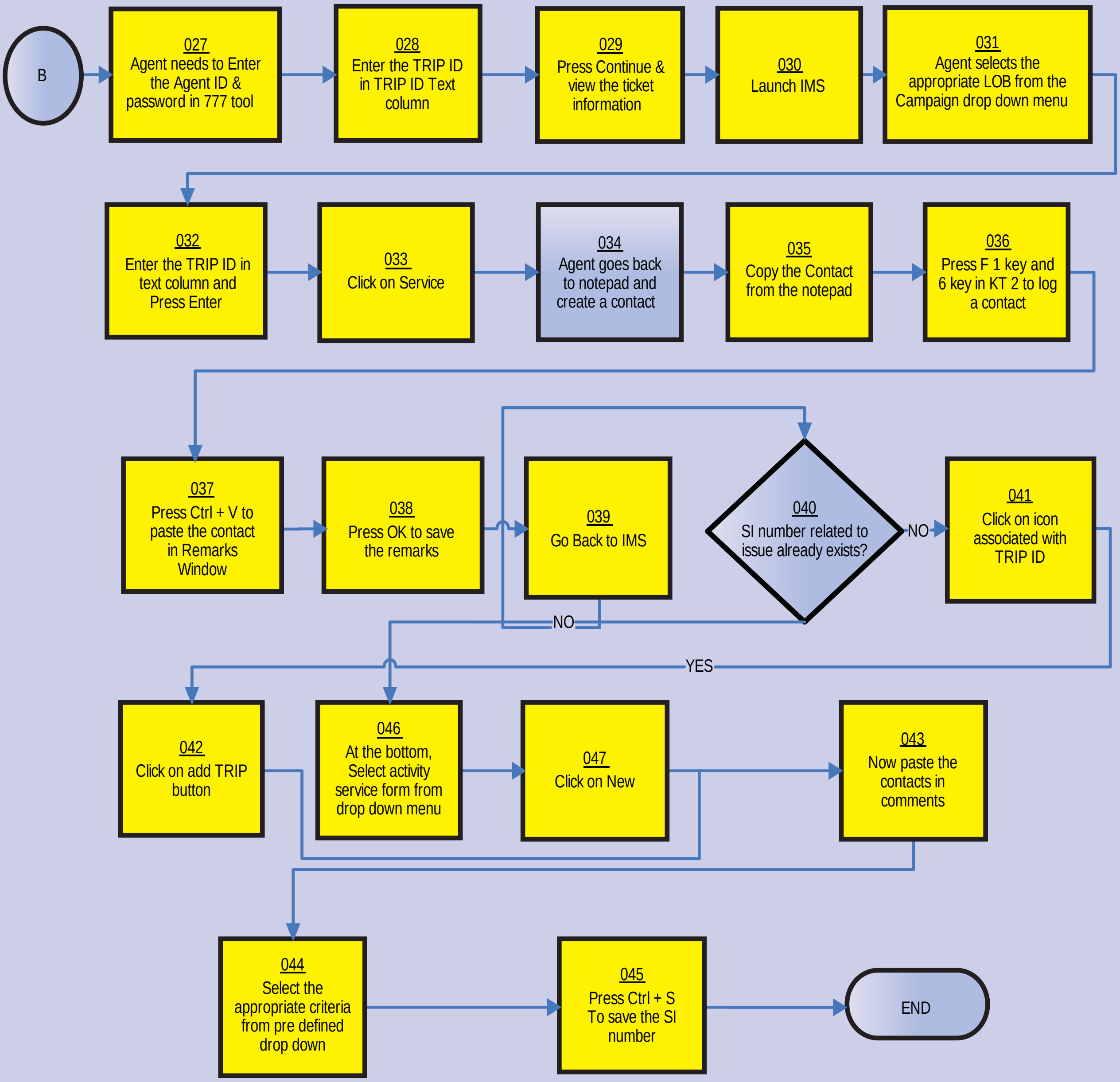
In this case, we actually achieved a reduction in average call handling time by 22%. When we look at average revenue per hour in dollar terms, with the revenue pegged at $18 / hour per agent, this translates into additional revenue of $3.96 / hour per agent. The case in point had 800 agents for the process. The numbers come to—

No. of Agents	800
No. of hours in a month	176
Additional Revenue	$557,568 / month

2.1: Flow Diagram of Sample Process with automated activities marked—Part 1



2.2: Flow Diagram of Sample Process with automated activities marked—Part 2



Of course, in order to achieve this we need to look at the cost of implementing such changes. The suggested changes can be carried out through appropriate change in the user processes, so that information once captured is automatically pushed into all the relevant applications. Secondly, if we can automate possible user processes, we can not only speed up the process, but also avoid avoidable errors. From information technology point, a part of this can be achieved through proper application level integration. Balance would normally demand application level changes. Both would require significant time and evolve large spends to achieve the objective. As requirements evolve with changing business scenario, application level integration turns out to be achievable only up to a point. Ownership of the applications was also a challenge. As a BPO service provider, most of the applications are not owned by the service provider and cannot be modified. So, even though the route was expensive, it was not an option.

The diagram 2.1 and 2.2 depict what all sub-processes or activities were automated. All of them have been coloured yellow. It shows that in terms of number, most of them are getting automated. There are, of course, few other additional advantages.

To understand the additional advantages, we would also need to know a typical day for an agent. As the shift starts, she has to "log in" to her computer through her "user id" and "password". She will also have to start the process, as depicted in diagram 1.1 and whenever she leaves her station, she has to "log off" from her system. In a typical day, this log-in log-off process and initial applications launching happens at least four times (as you start the shift, 1st tea-break, meal break, 2nd tea-break), if not more. Secondly, if the system remains idle for more than a given time period, it automatically logs off. That also demands additional log-in. The automation process can also avoid such lengthy processes and provide automatic launching of applications, as she logs in to the computer. Thus she does not have to launch initial applications, every time she logs in. Here, although there will be time savings, but it also facilitates better work satisfaction for the agent, as she is avoiding non-value added processes.

Conclusion

Any performance improvement initiative ought to have an impact on cost of goods / services in relation to revenue. While we observe in the above case, we focussed on improving delivery cycle time, leading to opportunity to earn more revenue, it also improved cost of service delivery. In a service industry, cost of attrition is very high. It not only leads to increase in cost of recruitment, it also contributes to higher cost of training, loss of productivity and a domino effect on employee morale. It has been observed that "boredom" on the job is a contributor to attrition and removal or automation of "non value added" processes can help in optimizing "boredom" factor, along with contributing to better margins. The process of performance improvement is a continuous process and has to be revisited again and again. Fresh pairs of eyes and ears are important factors to identify opportunities for improvement, along with ROI for such investments on performance improvements.

Letters to Editor

Dear Sir,

It is with great sense of satisfaction and happiness that I am writing this letter to you. First of all, I congratulate you and your entire team of "The Management Accountant" for doing a commendable job in the last few months particularly with reference to the quality, contents and the overall get-up of the Journal "The Management Accountant" which is the Official Organ of the Institute of Cost Accountants of India. It gives a great sense of satisfaction that our suggestions are being looked into and implemented by the Institute particularly many areas relating to the quality and content of the journal. In my earlier communication to you, I had given several suggestions for consideration by the Institute relating to the Journal. It is seen that several of them have already been considered and implemented by the Institute. I would like to mention a few of them:

1. The pages and the printing are now in colour, which has given a total new look to the Journal.
2. The price has now been increased to Rs 60 which is quite reasonable and was necessary.
3. Many relevant articles are now being published.
4. The overall quality of the Journal has improved significantly during the last few months for which you also personally deserve much appreciation.

   In spite of this, there is no scope of complacency and a lot more is to be done. My earlier suggestions which I hope are being definitely considered to be implemented in future are once again stated below:

   a.) Interview with Members Occupying High positions in Government, private, and other sectors are to be regularly published in "The Management Accountant".
   b.) Financial Cross Word & finance Quiz should be included.
   c.) There should be articles on Work Life balance, Stress Management, Communication Skills, Information Technology Tools for Members ,Yoga, & Health Tips , Motivational Thoughts, etc in every issue.
   d.) More publicity should be give to the Benevolent Fund of the Institute. All Members should be included in the Scheme.
   e.) There should be more seminars, conferences, conventions on relevant /current topics, which will enhance the co-ordination & communication amongst the Members of this Institute and also along with our sister professional Institutes.
   f.) The Management Accountant should reach the Members by 10th of a Month.

The overall communication level and interaction of the Institute with its Members has improved significantly during the last one year and it is expected that through you and the Journal department, a lot of unfinished agenda will be addressed.

Yours sincerely

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■ Letters may be edited for brevity

Reforms in The Indian Primary Market: Some Reflections

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It is appearing that the Indian IPO market is drying up as retail investors interest seems to be waning. Now, IPO's are far from their heydays. Fund raised by the Indian Companies is down to a trickle. The amount of fund raised by Indian Companies through this route has been declining since 2008 (except (2010).

According to the Global IPO trends 2011, published by Ernst and Young, India stood at 4th place in raising of capital, sharing 3.7% of global IPOs. While, Chinese companies were raised substantial amount of capital sharing around 47% of global capital raised through IPOs.

The amount of capital raised by Chinese Companies during 2008-10, increased by 250%, but, in our country the increase was very negligible. It implies that Indian capital market has been losing its sheen in the post-crisis financial world and China is increasingly becoming popular with respect to attracting foreign capital.

The primary markets across the globe have lost investors confidence and the experts opine that the aggressive pricing of IPO's contributed for loss in momentum in the primary market. The Indian primary market has fared badly in terms of returns with most trading well below their issue price. In fact, 3/4th of all issues made in the last six years are trading below their issue price.

Several factors, like linking remuneration of investment bankers to the issue price, fluctuations in the secondary markets, deterioration in macro-economic factors, failure to take forward the reforms, frauds, price manipulation, scams, high interest rate offered by banks, etc, have been contributing for the loss of investors confidence, particularly small investors in the primary market.

Growth required investment and investment requires savings. India has experienced a growth rate of around 10% during 2003 – 07 and this was possible due to high investment from all the three primary sources – household savings, corporate profits and foreign fund flows. India has seen a significant investment boom when investment on gross capital formation increased sharply from 22% of GDP to almost 38% of GDP.

Domestic savings have declined from 38% of GDP in financial year 2008 to 32% of GDP in financial year 2011. From the close analysis of the saving trend of the last 10 years, it appears that the household savings as a % of GDP remained more or less same. But, the more productive component of the household saving – financial savings, have dropped to 1990 levels of 7.8% of GDP from 12.2 % of GDP in 2010. It implies that India has to depend more on the overseas flows to fund its capital needs.

A study conducted by National Council of Applied Economic Research on household savings has revealed that out of India's 227 million households just 24.5 million households invest in equity, debt, mutual funds and derivatives. About 40% of households said that they lacked sufficient information that markets were not transparent. Majority of the respondents felt that equity was unsafe. It is evident from the fact that only 5% of households savings are in shares and debentures.

Fund raised through IPO route is down to a trickle. After tapering off in the adverse market conditions during 2008 and 2009, IPO's made a came back in 2010. However, since 2010, IPOs have been declining. Since, January of this year, around 14 companies tapped this market and of which only 12 companies raised a small amount of Rs. 1,302 cr. (Exhibit 2) and other two companies had to withdraw due to poor response.

It appears that IPO market is drying up and retail investor interest in offers also seems to be fading. Keeping in mind that much more need to be done for the development of a healthy and broad based equity market and to revitalize the mutual fund industry, SEBI, in its board meeting held on 16th Aug., 2012, took several important decisions. Here,

Exhibit 1: **How households shifted their savings:**

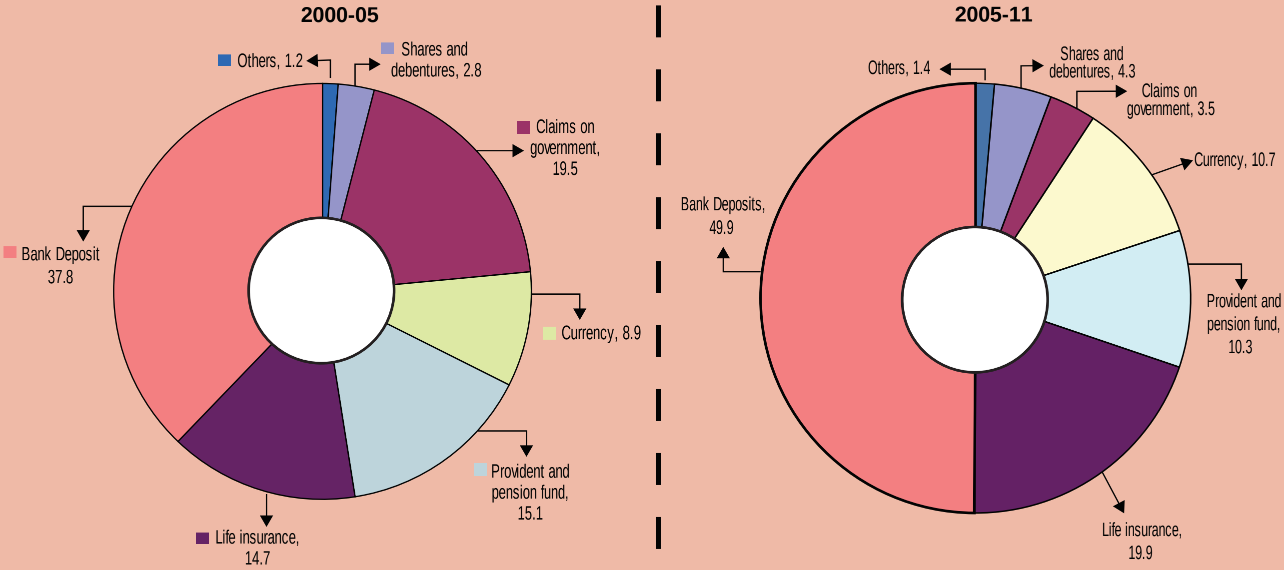

Exhibit 2: IPO Report – Public Issues in Last Few Years:

Years	No. of Issues	Amount Raised (Rs. In Cr.)	Issues Succeeded	Issues Failed
2007	108	33,946.22	104	4
2008	39	18,339.92	36	3
2009	22	19,306.58	21	1
2010	66	36,362.18	64	2
2011	40	6,043.57	37	3
2012*	14	1,3.02.45	12	2

** Up to 31st Aug., 2012*

in this post, we briefly touch upon only some of the key proposals and also the issues that some of them may pose.

Primary Market Reforms

These reforms may enhance the participation by small/retail investors, helps the corporate entities in raising the capital, boost the investors confidence.

Enhancement of retail/small investor participation:

In this connection, the regulator has taken several measures and key steps are:

E-IPO:

As of now, a retail investor while applying for IPO, has two options – submitting application along with the cheques and other one is submitting bid through the Application Supported by Blocked Amount (ASBA) mode.

In case of ASBA, retail investors will have to approach any of the designated branches of the self-supported syndicate bank, a bank registered with SEBI to provide this facility and submit the bid either in electronic mode or physical mode. Under this mode, the investor money will not leave his account and simply the banker will block his customer account until the allotment of share is made. After the allotment of share, the banker will remit the amount equivalent to application money to the issuer and the balance amount will be unblocked. This facility offers several benefits to both the investors and issuers.

Investor will continue to earn interest on his amount so blocked. Besides, he need not wait for the refund of money from the company. It reduces the pressure on the part of the company with regard to refund of amount.

It was introduced in 2008 and SEBI made it mandatory for non-retail investors (2011) and HNI. So far, this facility has been used in over 90 public issues and 37 right issues. In these issues, this facility has been opted for an average in 18.42% of the total applications. It is worth to mention here that the submission of bid through this mode is now hovering at around 25% which was just less then 1% when it was introduced.

Now, the regulator has provided one more way-E-IPO for submitting bid. Under this new mechanism, the investor has to approach stock broker and submit the application either through electronic or physical mode. Broker will then punch their application on the system.

At present, companies are making IPO's through merchant bankers/syndicate members. With this facility, the retail participation may get enhanced as investors can submit bid through any registered brokers. Currently, only 5% of the total brokers are appointed as sub-syndicate members.

This facility will be a cost-saving one as it will save paper, printing and other cost involved in processing application form. In fact, as of now, about Rs. 100-200 is spent by an issuer in processing each application form. Submitting application through online is a less time consuming one and helps the companies to list its shares within stipulated time (12 days from the closure of subscription). As we know that, in May 2010, the SEBI has reduced the timeline for listing of shares to 12 days from the earlier 22 days.

Implementing e-IPO calls for amendments of the Companies Act dispensing with the requirement of an investor to "agree in writing" since no application form submission is envisaged as the allotment will be in demat account.

Minimum Allotment:

Regulators would like to modify the share allotment procedure to ensure that every retail investor will get allotment, irrespective of his application size, subject to availability of shares. It has also decided to enhance the minimum application size from the current Rs. 5,000–7,000 to Rs. 10,000–15,000. It would assure that small investors are not sidelined by the big investors, helps to improve the liquidity of stocks and it will ensure the more equitable distribution of shares. In fact, on 25th Oct., 2010 SEBI has increased the application limit for retail investors to Rs. 2,00,000 from the earlier Rs. 1,00,000.

But, it is unclear how allotment procedure can be modified to ensure that every small investor will get minimum bid lot. It is also not clear how applications from retail investors that are not at the cut-off price are to be considered for allotment.

Declaration of Price Bands:

The share issuing companies, now, have to announce price band of the issue at-least five working days before the issue opens as against the existing norms of 2 working days. This proposal provides more time to the investor to evaluate the offer and take an informed decisions.

The price band is the price range within which the company will offer shares through IPO route. Under the extant regulation, the difference between the lower and upper of price band should not be more than 20%. In other words, the upper limit should not be more than 120% of the floor/lower price.

Withdrawal of Application by Non-Retail Investors (NRI):

This class of investors, henceforth, cannot withdraw or lower their bid size at any stage of the public issue. However, they are allowed to enhance their bid size.

It is expected, henceforth, application from this class of investor will come only in literally minutes before the closure of the issue, leaving no time to the market for any assessment about the view of the NRI on IPO. Therefore, it would be better if IPO remain open for subscription for a day longer for retail investors as it helps them to have view of the NRI on the IPO.

Measures to Facilitate Capital Raising by Issuers:

In order to help the corporate entities in

Achieving a minimum public shareholding requirements:-

Rule 19A of SCRR says that for a continues listing, the minimum public shareholding should be 10% in case of Public Sector undertaking and 25% in case of other companies.

Prior to Sept., 1993, Rule 19(2)(b) of the SCRR required a minimum public offer of 60% of the issued capital of a company for getting listed on stock exchange (SE). With a view to encourage more and more companies to list their securities on SE and broaden the market, the government reduced this minimum shareholding limit.

Recently, apart from the existing three routes - Institutional Private Placement (IPP), Offer for Sales (OFS), and Follow on-Public Offer (FPO), SEBI has provided two more routes – Right Issues and Bonus Issues, to achieve this limit. There are around 181 Companies (apart from 12 PSUs), where the promoters holding is more than 75% (Exhibit 3a and 3b). The SEBI has stipulated that these companies have to meet this requirement by 4th June, 2013 (for PSUs, it is Aug., 2013).

By the end of June 2013, these private companies have to offer roughly 27,000 cr. and PSU need to sell shares worth Rs. 11,000 cr.

It is observed that the average fund raising in the last 5 years on the Indian stock exchanges was Rs. 30,000 cr. p.a. This was less then the 38,000 cr. required to comply with norms.

CII has asked the market regulators to extend the deadline to 2015. Also all three the options – IPPs, OFS and FPOs have their limitations and as such, it would be desirable to allow other routes like – QIPs.

In case of right issues, the company will offer securities to the existing shareholders on the basis of their holding and promoters by not opting to take up his/her right can bring down their stake to 75%. But, in case of bonus issue, it would

Exhibit 3a: **List of PSUs – who needs to meet "Minimum Public Shareholding Norms"**

Sl. No.	Co. Name	Total of Promoter and Group	Market Capitalisation (BSE)	% Stake that needs to be reduced	Value of stocks that needs to be diluted (in Rs. Cr.)
1	Hind. Copper	99.59	24,560	9.59	2,355
2	MMTC	99.33	77,600	9.33	7,240
3	HMT	98.88	3,011	8.88	267
4	F A C T	98.56	1,961	8.56	168
5	Natl. Fertilizers	97.64	3,451	7.64	264
6	Scooters India	95.38	139	5.38	7
7	Neyveli Lignite	93.56	13,766	3.56	490
8	Andrew Yule & Co	93.30	631	3.30	21
9	ITI	92.98	671	2.98	20
10	R C F	92.50	3,078	2.50	77
11	St Bk of Mysore	92.33	2,343	2.33	55
12	S T C	91.02	1,508	1.02	15
					10,980

Exhibit 3b: **List of select Private sector companies – who needs to meet "Minimum Public Shareholding Norms"**

Sl. No.	Co. Name	Total of Promoter and Group	Market Capitalisation (BSE)	% Stake that needs to be reduced	Value of stocks that needs to be diluted (in Rs. Cr.)
1	Bombay Rayon	93.15	3,250	18.15	590
2	Shantivijay Jew.	93.10	28	18.10	5
3	Astrazeneca Phar	90.00	5,144	15.00	772
4	Fres. Kabi Onco.	90.00	2,157	15.00	324
5	Puravankar Proj.	89.96	1,443	14.96	216
6	Best Eastern Hot	89.60	44	14.60	6
7	Khoday India	89.54	186	14.54	27
8	BOC India	89.48	4,003	14.48	580
9	Suashish Diamond	89.43	220	14.43	32
10	Omaxe	89.15	2,653	14.15	375
11	Marathon Nextgen	89.14	286	14.14	40
12	Alfa Laval (I)	88.77	7,055	13.77	972
13	Gillette India	88.76	7,846	13.76	1,080
14	M R P L	88.58	10,656	13.58	1,447
15	Elantas Beck	88.56	1,671	13.56	227

be interesting to see how this idea is implemented as section 205 of the Companies Act allow companies to make bonus issues but does not seem to allow latitude for being selective.

In fact, a dispersed shareholding structure is required for the sustenance of a continuous market for listed securities to provide liquidity to the investors and discover fair prices. Beside, the larger the shareholder base, the less is the scope for price manipulation.

Contribution by Promoters:

As per Regulation 32 of the SEBI Regulation 2009 (ICDR), the promoters of the company have to contribute in the public issue to the tune of 20% of the post issue capital and such contribution shall be locked in for a period of 3 years.

In many instances, it was realized that the promoters were unable to meet this requirement by themselves. Now, SEBI has provided a relief to them as now these promoters can take help of SEBI registered Alternative Investment Funds (AIF) in meeting such requirement subject to a maximum of 10%. It would be better to clarify whether these AIF shall be treated as promoters for all other purpose of the offer documents and whether for their investment the lock in period will apply.

Halving of average market capitalization for fast track issues:

As per Regulation 10 of ICDR, a company which would like to raise capital through this route should have a market capitalization of Rs. 5,000 cr., regulator has amended this regulation and brought it down to Rs. 3,000 cr. It may encourage more companies to use this route and raise capital. This route was introduced by SEBI in 2007 to enable a listed company to have access to further capital.

Pricing norms for QIPs modified:

With a view to encourage the companies to raise the fund through QIP route, SEBI has allowed the companies to give (allow) a discount of 5% to the price calculated as per the ICDR.

This may act as an incentive to the Qualified Institutional Buyers as well as private equity investors and could kick start the otherwise slowed down institutional placement process.

Re-filling of the Prospectus not required:

The increase in flexibility to the issuers to change the amount to be raised by up to 20% (earlier ceiling was 10%) from the declared amount in the prospectus is a welcome measure.

Now, the issuing companies can enhance/reduce in the size of issue without re-filling of offer document with the SEBI provided such change is not more than 20% of original amount proposed to be **raised.**

Additional Disclosure:

To bring Indian disclosure norms on par with 20F filing prescribed by the SEC, and provide updated information to the investors, SEBI has asked all listed companies to file a comprehensive annual disclosure statement, apart from existing requirements with it.

This measure will go a long way in ensuring transparency and disclosure by Indian companies.

Cap on General Corporate purpose:

While the extant regulation did not put any cap on the deployment of issue proceeds under General Corporate purpose and now the regulator has placed a 25% cap on this item, which may bring more transparency in capital rising.

Some Key Reforms for MF Industry

Indian mutual fund industry comprises around 44 players and of this around 24 are in the red. SEBI also took several measures to re-energies the mutual fund industry. Some of key measures are:

- **Fungibility of Total Expenses Ratio (TER):** SEBI's extant regulation allows the mutual fund to charge up to 2.5% on the net asset managed by it as expenses for a year. This is the total money available in the hands of fund houses to meet all costs – fund manager fees, brokerage and transaction costs on securities, selling and operating expenses, distributors commission, legal fees, etc.

  The extant regulation does not permit the fund houses to spend the amount as they desires. Of this, they have to set aside 1.25% towards investment management fees. The new regime will take away this sub limit and allow to spend the amount collected as they wishes and it opens up many interesting possibility both for investors and fund houses.
- **Improvement of Geographical Reach of MF:** To enhance investment penetration, the fund houses have been allowed to charge extra 30 bps, if such houses collect funds from cities/towns beyond 15 cities. However, the fund houses can enjoy this right only when they are able to collect of either 30% of gross new inflows or 15% of the average asset under management of the scheme from beyond top 15 cities. If actual collected amount is smaller one, then proportionate amount will be allowed as additional TER.

  As per the data released by AMFI, as of June 2012, the top 15 cities contributed around 86.95% of the total asset under management (AUM) of the industry. The AUM of the industry as of Aug., 2012 was Rs. 7.5 lakh cr.

  Now, the fund houses can levy and collect the service tax from the investors, which may come about 14 bps (12.6 % on the fund management fees). Besides, the fund houses are entitled to levy additional 20 bps for such investors who withdraw their money within a year of making their first investment. However, this amount should be added to the scheme unlike earlier one, where the fund houses used to either transfer into the fund house treasury or passed on to the distributors.

  With these changes, the TER may go up to 3% for investors belonging to other cities and 2.70% for 15 cities. In other words, the cost of buying MF will get increased. Transaction cost in most of countries is just 25-27 basis points.
- **Enhanced Participation:** with a view to encourage small farmers and traders who doesn't have either PAN card or bank account, the SEBI allowed to these persons to participate in mutual fund schemes by way

Exhibit 4: Illustrates the overall cost incurred by an investor for executing a trade for Rs. 1,00,000.

Value of Trade Rs. 1,00,000			
Particulars		% of Total Cost	% of Traded Value
Average Brokerage (at the rate of 10 bps)	100	37%	0.10%
Service Tax on Brokerage	10.3	4%	0.01%
Stamp Duty	10	4%	0.01%
SEBI Turnover Fee	0.2	0%	0%
Exchange Transaction Charges (at highest slab based rate)	3.25	1%	0.00%
Securities Transaction Tax (STT)	125	46%	0.13%
DP Charges	20	8%	0.02%
Total	268.75	100%	0.27%

of cash transactions to the extent of Rs. 20,000 subject to the compliance of the provisions of prevention of money laundering Act, 2002.

- **Direct investment:** In order to promote direct investment, the regulator decided to have a separate plan for direct investment, with a lower expenses ratio. Distributors have raised voice against this proposal on the plea that it will have a adverse impact on their income. It would be more beneficial to a savvy investor.

  For the purpose of avoiding differential treatment in the same scheme to different classes of investors, regulator has decided that all new investors will be subjected to single expense structure under a single plan.
- **Enhanced Disclosure:** In order to bring Indian disclosure on par with best global one, the regulator has mandated to all AMCs to provide monthly portfolio disclosure on their website, also publish half yearly financial statements on their websites and an advertisement in this regard be published in the national and one regional news paper.

Conclusion:

Undoubtedly, SEBI has done a lot to enhance the retail participation in the capital market. However, there are several areas where action need to be initiated and key of such area are reduction in the transaction tax, withdrawal of stamp duty, providing safety net to the small/retail investors, making available demat account at free/nominal costs, etc.

Indian market has among the highest transaction cost globally on equity transaction. The transaction cost encompasses brokerage, exchange transaction charges, depository charges, SEBI turnover fees, STT, stamp duty and service tax on brokerage. The transaction costs have two component charges payable to brokers and exchange for their services and other charges are statutory and regulatory in nature.

India levies both the STT as well as stamp duty. Globally, imposing STT or stamp duties on cash based equity transaction is common but imposing STT on derivative transaction is uncommon. Out of the total cost, about 55% constitutes various statutory levies and STT alone constitutes for 46% of the total statutory taxes. This is extremely higher when compared to the global market (Exhibit 4).

According to IMF paper, globally speaking the total cost of trading is in the range of 9 basis points to 30 bps of the traded value. However, in India, with 27 bps, the trading costs are at the higher end of the range after China and Hong Kong. Reduction of these taxes can be done with a little loss to the exchaquer, since the growth in volumes by this move can compensate for the reduction in revenues.

In India, the cost of maintaining the demat account for investor is very high. The brokerage houses will levy anywhere between Rs. 300 to 500 as Annual Maintenance Charges (AMC) regardless of the value of the securities in the account. Considering this higher cost, the SEBI has issued a circular, which came into effect from 1st Oct., 2012, stating that all DPs should reduce maintenance charges on the Basic Service Demat Account (BSDA). The new charges are quite low.

The value of securities in the BSDA should not exceed Rs. 2,00,000, otherwise it attract normal maintenance charges. The AMC would be zero where the value of securities in the account are up to 50,000 and anything above Rs. 50,000 and up to Rs. 2 lakh would attract AMC of Rs. 100. The BSDA value would be determined everyday according to the daily closely price of securities or daily closing NAV.

Across the globe, genuine investors have been losing the money invested by them due to one or other kind of frauds – price manipulations, IPO scam, vanishing companies, etc.

About 100 companies were ultimately identified as vanishing companies which dubiously raised funds of about Rs. 800 cr. through public offering during 1993-95 and investor lost their money for no reason and limited punitive action taken by the Government against such companies and their director has not avoided recurrence of such events.

Small investors became victim of the massive IPO scam of 2005-06 related to over 20 companies. Thousands of fictitious applications financed by over 80 financers resulted in allotment being made against such applications resulted either nil or partial allotments to genuine investors.

A committee headed by Justice Wadhwa (2007) has recommended that genuine investors who were the loser's be compensated out of the proceeds disgorged from the offenders and no dispersal seems to have made.

We hope that, the regulator will look at other measures like providing fiscal incentives, introducing safety net for retail participants, providing investors education on massive scale, strict enforcement of law relating to insider trading, strictly imposing all the norms and regulations of corporate governance, etc, which will helps in building the investors confidence. Regulator should remember that cases of insider trading and price manipulation should not be solved through the consent order. Retail investors are ready to accept market related risk only when they feel that they are receiving a fair deal and SEBI has to create a conducive environment for this.

References:

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The **54th National Convention—2013** of the Institute will be held during January 18-19, 2013 at Gujarat University Convention and Exhibition Center, Ahmedabad, Gujarat

Advisory from the Institute

Members of the Institute are once again advised not to charge fee less than the suggested minimum Professional fees, as approved by the Council at its 268th Meeting held on 10th May 2012. The same is given below for the information of the members:

Suggested Minimum Professional Fees as Approved by the Council at its 268th Meeting held on May 10, 2011

1. Fees for Cost Audit related assignments:

Turnover in Rs. Crores	Fees for Cost Audit	Fees for Cost Records/Compliance
Below 5	20,000	
5 – 10	40,000	
10 – 20	50,000	
20 – 50	75,000	25,000
50 – 75	1,00,000	35,000
75 – 100	1,25,000	50,000
100 – 150	1,75,000	75,000
150 – 250	2,50,000	1,00,000
250 – 500	4,00,000	1,50,000
500 – 750	5,00,000	2,00,000
750 – 1000	6,00,000	2,50,000
1000 – 2500	7,50,000	3,50,000
2500 – 5000	8,50,000	4,50,000
5000 – 20000	10,00,000	5,00,000
20000 and above	Negotiable	Negotiable

1. Costing Assignments:

1.1 Monthly Retainership	:	Rs. 10,000 – 15,000 for the first visit and Rs. 2,500 – 5,000 for each subsequent visit of around two hours during the month.
1.2 Casual Visit	:	Rs. 5,000 – 10,000 per day (Partner having less than 10 years of practice)
	:	Rs. 10,000 – 25,000 per day (Partner having more than 10 years of practice)
1.3 Chamber Consultation	:	Rs. 2,500 per hour at the minimum.
1.4 Certificate Work	:	(a) Minimum Rs. 2500 per certificate – for Small Scale Units. (b) Minimum Rs. 5000 for others. (c) For certification involving in-depth scrutiny and study Rs. 2000 per hour of work involved.

2. Designing Systems of Cost and Management Accounting (Minimum Fees)

	(Rs.)
(a) Upto Turnover of Rs. 2 Crores	50,000
(b) Rs. 2 Crores to Rs. 10 Crores	1,00,000
(c) Rs. 10 Crores to Rs. 100 Crores	2,50,000
(d) Above Rs. 100 Crores	5,00,000

3. Finance Applications and Feasibility Reports:

Scrutiny of technical and market feasibility reports, preparing financial feasibility reports and drawing projection of profitability, financial position, capital plan and cash flow – Based on Project Cost.

4. Charges for providing services of juniors:

Cost Accountant	(Qualified Assistant)	Rs. 1,000 per hour
Cost Assistant	(Intermediate)	Rs. 750 per hour
Cost Assistant	(Trainee)	Rs. 500 per hour

For all assignments, Service Tax and other applicable Taxes, Travelling and out-of-pocket expenses will be charged extra.

Guidance Note on Cost Accounting Standard on Administrative Overheads (CAS-11)

The Council of the Institute of Cost Accountants of India has issued the Cost Accounting Standard - 11 (CAS-11) on Administrative Overheads which lays down a set of principles and methods of classification, measurement and assignment of Administrative Overheads for determination of the cost of product or service and the presentation and disclosure in the cost statements. The Cost Accounting Standards have been set in bold italic type and reference number of the standard has been retained.

The Guidance Note deals with principles and methods as provided in the CAS-11 and practical aspects in connection with the determination of Administrative Overheads for a product or service.In the preparation of cost statement and its attestation, Administrative Overheads shouldbe determined with reference to CAS-11.

The Companies (Cost Accounting Records) Rules, 2011 provide that every company, including a foreign company defined under section 591 of the Companies Act, 1956 which is engaged in production, processing, manufacturing or mining activities have to maintain cost accounting records in accordance with the Generally Accepted Cost Accounting Principles (GACAP) and Cost Accounting Standards issued by the Institute, to the extent these are found to be relevant and applicable. The above Rules further provide that these will be applicable to companies wherein:

a. aggregate value of net worth as on the last date of the immediately preceding financial year exceeds five crores of rupees; or
b. the aggregate value of the turnover made by the company from sale or supply of all products or activities during the immediately preceding financial year exceeds twenty crores of rupees; or
c. the company's equity or debt securities are listed or are in the process of listing on any stock exchange whether in India or outside India.

The Companies (Cost Audit Report) Rules 2011 cast a duty on a Cost Auditor appointed under Section 233B of the Companies Act, 1956 to certify inter alia that books and records maintained by the company are in conformity with the Cost Accounting Standards issued by the Institute to the extent these are found to be relevant and applicable.

Chapter 1 Introduction

Administrative Overheads have been defined by the CAS-11 as the cost of all activities relating to general management and administration of an entity. These costs generally represent amounts incurred at Head office / Corporate office relating to administration and policy matters of the company.

Administrative Overheads are the cost of all activities relating to general management and administration of an entity**.** These are the total costs of formulating the policy, directing the organisation and controlling the operations of an entity.

Administrative Overheadsexclude production overheads, marketing overheads and finance cost. Production overheads includeadministration cost relating to production, factory, works or manufacturing. Such costs are in the nature of administrative support to functions connected with the production e.g. Purchase, factory accounts, factory administration etc.

Administrative cost on the other hand represent costs incurred in connection with the management of affairs of the entity such as Policy making, Finance, Human resources and the like.

For example:

Indirect materials - printing and stationery; office supplies;

Indirect employee costs - Salaries of administrative directors, secretaries, accounts department and so on;

Indirect expenses - rent rates and taxes, insurance, legal charges, audit fee and the like. These include the costs of the concerned departments as well as the Head Office and other administration costs as detailed below:

A. Administrative Overheads generallyinclude the expenses of following departments:

- General Administration
- Human Relations
- Finance and Accounts
- Cost Accounts
- Internal Audit
- Secretarial

- Law and Taxation
- Information Technology Department
- Security

Administrative costs include all executive, organizational, and clerical costs associated with general management of an organization rather than with manufacturing, marketing, or selling. For examples administrative costs include executive compensation, secretarial salaries, general accounting, public relations, and similar costs involved in the overall, general administration of the organization as a whole.

Other Administrative Expenses:
Printing and stationery
Travelling & Local Conveyance
Membership fee
Computer maintenance expenses
Vehicle maintenance expenses and the like.
A detailed list of other administrative expenses is at annexure 1

B. Corporate Office Expenses:

Board of Directors:

- Directors' sitting fees, remuneration and commission;
- Directors' travelling expenses;
- Meeting and other board expenses.

Other Management Expenses:

1. Administration - Salaries and fringe benefits of general and administrative personnel (corporate office staff). For example salaries ofmanagers, and other employees in the administrative functions of the company. Rent, rates and taxes, travelling and other administrative expenses;
2. Cost information should be collected and analyzed systematically and consistently, whether for a routine information system, or for a specific application and / or purpose.In the preparation of cost statement and its attestation, if required, Administrative Overheads relating to a product / service should be determined with reference to CAS-11.

Chapter 2 Definitions

4.1 **Abnormal cost:** ***An unusual or atypical cost whose occurrence is usually irregular and unexpected and / or due to some abnormal situation of the production or operation.***

4.2 **Absorption of overheads:** ***Absorption of overheads is charging of overheads to Cost Objects by means of appropriate absorption rate.***

4.3 **Administrative Overheads:** ***Cost of all activities relating to general management and administration of an organisation.***

4.4 **Cost Object:*****This includes a product, service, cost centre, activity, sub-activity, project, contract, customer or distribution channel or any other unit in relation to which costs are ascertained.***

4.5 ***Finance Costs: Costs incurred by an enterprise in connection with the borrowing of funds.***

4.6 **Imputed Costs:** ***Hypothetical or notional costs, not involving cash outlay, computed for any purpose.***

4.7 **Normal capacity:** ***Normal Capacity is the production achieved or achievable on an average over a number of periods or seasons under normal circumstances taking into account the loss of capacity resulting from planned maintenance.***

4.8 **Overheads:** ***Overheads comprise of indirect materials, indirect employee costs and indirect expenses which are not directly identifiable or allocable to a cost object.***

Chapter 3 Principles of Measurement

5.1 ***Administrative*** **overheads**shall ***be the aggregate of cost of resources consumed in activities relating to general management and administration of an organisation.***

Administrative Overheads is the cost of all activities relating to general management and administration of an organisation. It is represented by cost of shared services, infrastructure cost and general management cost. Resources consumed are in terms of employee costs, utilities, office supplies, legal expenses and outside services. The measurement of these resources consumed is to be determined in terms of relevant cost accounting standards.

CAS-6 lays down the principles with regard to the valuation of receipts of material. Therefore receipt of indirect materials should be valued at purchase price including duties and taxes, freight inwards, insurance and other expenditure directly attributable to procurement (net of trade discounts, rebates, taxes and duties refundable or to be credited by the taxing authorities) that can be quantified with reasonable accuracy at the time of acquisition.
The consumption of indirect material is to be valued at issue rate adopted i.e. First in First out, Last in First out, Weighted Average. Suchbasis should be followed consistently.

Indirect employee cost is to be measured in terms of CAS-7 (Employee cost). Employee cost relating to administrative staff should be the gross pay and allowances payable. It should take into account the employee's salary including all allowances and other benefits, such as Employer's contribution to EPF, FPS, ESIS, Holiday Pay, Gratuity Payable, Bonus and so on. Remuneration paid to Officers, Managers and Executive Directors of an entity - engaged in administrativefunction should cover fixed salary, PF contribution, leave, superannuation and severance payment, other benefits, and the like. It should also include any amount paid as commission based on percentage of profit. Other benefits include free furnished accommodation, house rent allowance, leave travel concession, reimbursement of medical expenses for self and family. Personal accident insurance, fully maintained company's car with driver, gardener, watchmen and the like. These should form part of employee cost. Remuneration paid to non-executive directors should be treated as Administrative Overheads.

Utilities consumed by administrative cost centres are to be collected and measured in accordance withprinciples laid down by CAS-8. Repair and maintenance cost should be measured in accordance with principles laid down by CAS -12.

5.2 ***In case of leased assets, if the lease is an operating lease, the entire rentals should be included in the administrative overheads. If the lease is a financial lease, the finance cost portion should be segregated and treated as part of finance costs.***

A lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.Leases are of two types viz Finance lease and Operating lease. A finance lease is a lease that transfers substantially all the risks and rewards incident to ownership of an asset. Whereas an operating lease is a lease other than a finance lease. The basic concept of lease accounting is that operating lease is merely rental, whereas financial is a disguised purchases.

Lease Rentals in respect of assets taken on 'Operating Lease' for administrative activities should be included under Administrative Overheads. Payments under an operating lease will be recognised by the lessee as an expense over the lease term. Lease rentals for assets acquired under Financial Lease should be segregated between the cost component of asset and interest component by applying an implicit rate of return. Interest component should form part of the Finance Cost and should not be included under Administrative Overheads.

5.3 ***The cost of software (developed in house, purchased, licensed or customised), including up-gradation cost shall be amortised over its estimated useful life.***

Software may be either developed in house, purchased, licensed or customised. Where software is included in the purchase price of hardware (For example operating system software) and the cost of the software cannot be easily calculated, the software should be capitalized and amortized as part of hardware. In case of licensed soft ware, if one-off licensing fee is paid during the period in order to use the software which has acquired service potential or future economic benefits relating to that software, such cost of license fee should be capitalized as part of the software and amortised over its useful life. In case licensing fee is not a one-off (For example a yearly licensing fee which covers maintenance and upgrades automatically provided by the vendor) service potential or future economic benefits obtained will normally expire when the next payment is due and should not be capitalized and charged during the period.In house developed software as soon as it is put to use, it should be capitalized and amortized over its useful life.

5.4 ***The cost of administrative services procured from outside shall be determined at invoice or agreed price including duties and taxes, and other expenditure directly attributable thereto net of discounts (other than cash discount), taxes and duties refundable or to be credited.***

Various types of services related to administration may be procured from outside, such as legal consultancy, management consultancy, internal audit, and so on. In such cases determination of cost of administrative services procured from outside shouldbe as per agreed price / invoice. It should include duties and taxes and other expenditure. These are to be net of any discount, rebate, taxes and duties refundable, if any.

5.5 ***Any Subsidy / Grant / Incentive or any amount of similar nature received / receivable with respect to any Administrative overheadsshall be reduced for ascertainment of the cost of the cost object to which such amounts are related.***

Subsidy and grant received / receivable should be recognized on a systematic basis. These should be matched with the related cost for which these are intended to compensate over the period.

For example:

Subsidy may be receivable for any social service, such as crèche, schooling, community centre and the like. Subsidy receivable for this purpose may be reduced from the cost of such services, while ascertainment of the cost of the administrative overheads.

5.6 Administrative overheads shall not include any abnormal administrative cost.

Abnormal cost has been defined under paragraph 4.1 of CAS - 11. The rationale of exclusion is that inclusion of such items in the cost will make the cost not comparable with a normal situation. Such an aberration is avoided to understand the cost in a better perspective for any purpose. For determining the abnormal cost following two conditions should be satisfied:

a. Costs were never envisaged; and
b. They are not likely to recur during an accounting period.

For example:

- Abnormal administrative cost resulting from natural calamity (flood, earthquake, and the like).
- Sudden breakdown/ loss due to major fire accident.

It should not form part of part of the administrative overheads and should be dealt with in the costing profit and loss account.

5.7 Fines, penalties, damages and similar levies paid to statutory authorities or other third parties should not form part of the administrative overheads.

Fines, Penalties, damages and the like are levied by the statutory authorities for non-compliance with statutory requirements or delays. These are abnormal cost and should not form part of Administrative Overheads.

For example:

- Penalty for delay in depositing Provident Fund contribution with the Provident Fund Authorities.
- Penalties for non-payment of statutory dues / noncompliance with legal requirement for example not filing certain statutory returns in time.

5.8 Credits / recoveries relating to the administrative overheads including those rendered without any consideration, material and quantifiable, shall be deducted to arrive at the net administrative overheads.

If any administrative services are provided to other activity / unit without any consideration, the cost of the same, if material and quantifiable, should be determined. It should be adjusted
against the Administrative Overhead.

For example management consultancy services are provided to other unit, the cost of the same has to be adjusted against the administrative overheads

5.9 Any change in the cost accounting principles applied for the measurement of the administrative overheads should be made only if it is required by law or for compliance with the requirements of a cost accounting standard or a change would result in a more appropriate preparation or presentation of cost statements of an organisation.

Resources consumed in the administrative overheads are indirect material, indirect employees cost, utilities and other similar items. These are represented in the form of shared services, infrastructure cost and general management cost. Principles applied for measurement of these resources are to be as per relevant cost accounting standard and are to be followed consistently. However, change in principle of measurement of Administrative Overheads should be applied if it is required by law or for compliance with the requirements of a cost accounting standard or a change would result in a more appropriate preparation or presentation of cost statements of an entity.

For example profit sharing bonus paid to employees was not earlier treated as employee cost. But as per the CAS - 7, profit sharing bonus now forms part of employee cost. It is to be measured as per requirement of Bonus Act and CAS - 7. If there is any change in computation of bonus, its measurement has to comply with required changes.

Chapter 4 Assignment of Cost

6.1 While assigning administrative overheads, traceability to a cost object in an economically feasible manner shall be the guiding principle.

Once administrative overheads have been accumulated and measured, these are to be assigned to a cost object. Cost Object is a logical sub-unit for collection of cost. Cost Object may be classified in different ways like function-wise and nature-wise. Thus cost object may be any customer, product service, contract, project, activity or other work unit for which a separate cost measurement is desired.

For assigning the administrative overheads, traceability is a key element. Tracing administrative overheads to cost objects can occur:

1. Direct tracing;
2. Driver tracing; and
3. Allocation.

Direct tracing is the process of identifying and assigning cost that is specifically or physically associated with cost object. For example, tracing cost of stationery consumed in the accounts department to a cost object i.e. accounts department. Drivers tracing may be through cost activities viz. units manufactured, hours worked, number of batches in production, number of orders processed, number of departments, and so on.

The method of direct cost tracing usually relies on the observation, counting, and/or recording of the consumption of resource units, such as staff hours or days that are spent on or assignment, or gallons of fuel consumed in a transport trip. Direct tracing also applies to specific resources that are dedicated to particular outputs.

Direct cost tracing often minimizes distortion and ensures accuracy in cost assignments. It shall be applied only to items that account for a substantial portion of the cost of an output and only when it is economically feasible. For example, it is usually unnecessary to trace the cost of office supplies (pens, papers, computer disks, etc.) to various activities or outputs.

The tracing of such costs directly usually outweighs the benefit of the increased accuracy in assigning the resources. It is often not possible to physically observe the exact amount of resources consumed by a cost object, especially in case of administrative overhead, being an indirect cost. In case of indirect cost there is no relationship between the cost and cost object and tracing is not economically feasible.

The following steps are to be followed when tracing the administrative cost:

1. Identify the activities that cause the administrative costs,
2. Measure the cost of those activities; and
3. Assign the cost of the activities to those products and customers.

Various items of administration overheads are first collected according to nature of expenditure. These are arranged according to department or function. This is the method of primary distribution. The expenses which are capable of being identified with a specific department are directly assigned. The expenses which cannot be assigned directly to specific departments are assigned on suitable basis. Examples of direct identifying with department or functions are:

General Office	
Secretariat	
Finance and Accounts	
Human Resources	
Legal	
Following are the bases used to assignment of administrative expenses:	
Expenses	Bases
Office rent, rates and taxes	Floor area
Depreciation of office building	Floor area
Legal expenses	Number of cases handled / time basis for consultancy
Salaries and allowances	Number of employees

In brief assigning administrativecosts shall be conducted on a reasonable and consistent basis. Directly tracing costs might be a preferred approach when economically feasible. Assigning costs on a cause-and-effect basis shall be considered for costs that cannot be directly traced to outputs. This issue therefore requires a judgment taking into account facts and circumstances of each case.

6.2 *Assignment of administrative overheads to the cost objects shall be based on either of the following two principles;*

1 Cause and Effect - Cause is the process or operation or activity and effect is the incurrence of cost.
2 Benefits received – overheads are to be apportioned to the various cost objects in proportion to the benefits received by them.

A cost is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship.Assigning of costs shall be conducted on a reasonable and consistent basis. Testing reasonableness shall take into account the purpose of the cost information and the economic feasibility of collecting and assigning it. Following criterion shall be considered:

Assigning costs on a cause-and-effect basis shall be considered for costs that cannot be directly traced to outputs.

*For example:*A computer technology department provides technical support to other departments of an organization. The costs of the department may be assigned to other departments on a cause-and effect basis through two steps. In the first step, the costs are assigned to the activities of the department, such as hardware installation and maintenance, software design and installation, or programming adjustments. In the second step, the costs of these activities are further assigned to other departments based on their usage of the technical services.

Assigning Cost - Benefit received:

Standard provides for assigning of Administrative Overheads to the various cost objects in proportion to the benefits received by them. Benefits received when measurable and traceable, provide guidance for assignment. The beneficiaries of the output of the cost pool shall be identified and costs allocated in proportion to the benefits received. Benefits received shall be interpreted as meaning the receiving of services or goods by the activity represented by the cost objectives to which the costs are being assigned.

For example: A corporate wide advertising programme promotes the general image of corporation rather than as individual product. The costs of such programme may be allocated on the basis of division sales in the belief that divisions with higher sales levels are more likely to benefit than divisions with lower sales levels.

Chapter 5 Presentation

7.1 *Administrative overheads shall be presented as a separate cost head in the cost statement.*

7.2 Element wise details of the administrative overheads based on materiality shall be presented.

Administrative overheads are required to be presenteds a separate head in the cost statement. Element wise details of administrative overheads are to be indicated in the cost statement if these are material. What is considered material or immaterial depends on the facts of each case. The materiality of a particular cost is important in classifying costs. The less significant a cost, the less likely will it need to be traced to a cost object. An example as to how administrative overheads can be reflected in a cost statement is given in Annexure I.

Chapter 6 Disclosures

8.1 The cost statements shall disclose the following:

- The basis of assignment of administrative overheads to the cost objects.

  Disclosure is to ensure the consistency and compliance of requirement of Cost Accounting standards. Disclosure is to be made relating to the basis of assignment of administrative overheads adopted to cost objects / units in the cost statement or by way of foot note.

  Any imputed cost included as a part of administrative overheads.

  Imputed cost does not form part of the cost as it does not involve any cash outlay. However, if any imputed cost has been included in the administrative overheads, the same shall be disclosed.

  For example: Rent of Rs. Two Lakh for owned office building has been included in Administrative Overhead.

- Administrative overheads incurred in foreign exchange.

  Payment made in foreign exchange for Administrative Overhead relating to import of any office equipment / consultancy / foreign travelling shall be disclosed in the cost statement.

- Cost of administrative activities received from or supplied to related parties.

  If any administrative service has been procured from or supplied to related parties (as defined under The Companies Act, 1956), its relationship, nature of transaction viz. quantity, rate, other terms / conditions of procurement are to be disclosed. The objective of disclosure is to ascertain that the transaction is at arm's length and on purely commercial terms.

  For example:

  Related party → A B C Ltd

Nature of relationship → We and our subsidiaries own 51 percent of their Equity.
Nature of transactions: Hiring of office premises.

Office premises measuring 15000 sqft has been hired from ABC Ltd @ Rs 1500 per sq ft. The rate is a market prevailing rate for such premises and transaction is at arm's length. Related party disclosure is to be made.

- Any Subsidy / Grant / Incentive or any amount of similar nature received / receivable reduced from administrative overheads.
  Any subsidy / grant / incentive or any amount of similar nature received or receivable relating to Administrative Overheads is to be reduced from the Administrative overheads.
  For example for setting up school in township / adopting any social activity, subsidy/grant received is to be disclosed.

- ***Credits / recoveries relating to the administrative overheads.***
  If any credit or recovery considered while determining the administrative overheads the same shall be disclosed.
  For Example: certain administrative services were provided during the year to an associate/Group entity~~sister~~ unit, a sum of Rs 15 lakh received has been credited to the Administrative Overheads.

- Any abnormal portion of the administrative overheads.
  Abnormal portion of administrative overhead in the cost of cost object is to be excluded as the same has not contributed to the cost object. Disclosure is to be made.
  For example: During the year there was fire resulting in loss of office equipment and furniture fixtures of Rs 9 lakh. The same has been excluded from the administrative overheads.

- Penalties and damages excluded from the administrative overheads.
  Penalties and damages paid are not an item of cost as these are levied for non compliance with regulatory / contractual requirements. These are to be excluded from cost and disclosure made.

8.2. *Disclosures shall be made only where material, significant and quantifiable.*

Level of materiality and significance has not been stated in the standard. Materiality is to be judged in terms of quantity and nature of material and in particular context of its omission. A piece of information is material, if its non disclosure could influence the decision of a user.

Material and significance of any information will be different from situation to situation. If material, the same is to be disclosed.

8.3. Disclosures shall be made in the body of the Cost Statement or as a foot note or as a separate schedule.

Disclosure in the body of cost statement will depend on nature and materiality of Administrative Overheads. If it forms material part of the Administrative Overhead and can be identified with a cost object the same shall be disclosed in the cost statement otherwise, disclosures may be made either in the body of the Cost Statement or by way of foot note.

8.4. Any change in the cost accounting principles and methods applied for the measurement and assignment of the administrative overheads during the period covered by the cost statement which has a material effect on the administrative overheads shall be disclosed. Where the effect of such change is not ascertainable wholly or partly the fact shall be indicated.

Cost Accounting principles, and methods applied for the measurement and assignment of Administrative Overheads are to be applied consistently between one period to other and uniformly applied for different elements of Administrative Overheads. If any change is made in these principles and methods which results in material effect on the cost of product, the same shall be disclosed in the cost statement. In case the impact of change in principles and methods of cost accounting is not ascertainable, the fact is to be disclosed by a note to the cost statements.

For example Head Office (General Management) expenses were being assigned to various units on the basis of Turnover. During the current year the assignment of general management expenses have been assigned on a composite ratio which takes into account turnover, capital employed, gross profit, employee cost of units. Previous year's figure is not on comparable basis.

Annexure I

List of other administrative expenses:

i. General Charges;
ii. Casual labour;

iii. Licence fees;
iv. Insurance expenses;
v. Training expenses;
vi. Printing of the Annual Report;
vii. Telephone;
viii. Bank charges;
ix. Printing and stationery;
x. Vehicle maintenance expenses;
xi. Travelling and local conveyance for staff;
xii. Water charges;
xiii. Electricity charges;
xiv. Subscription and membership fee;
xv. Books and periodicals;
xvi. Inspection fees;
xvii. Computer maintenance expenses;
xviii. Gas charges;
xix. Cleaning and plant watering;
xx. Advertisement (related to recruitment);
xxi. Stipend and trainee expenses;
xxii. Gifts and presents;
xxiii. Depreciation and repair & maintenance of administrative fixed assets(machines and furniture located in HO; and
xxiv. Other miscellaneous expenses, such asReception; Company party to celebrate functions.

Annexure II

DISCLOSURE OF ELEMENTS OF ADMINISTRATIVE OVERHEADS

COST STATEMENT OF PRODUCT For the period/year ending Production						
S.No.	Item	Unit	Quantity	Rate	Amount	Cost per unit
1.	Material cost					
1(a)	Indigenous – Purchased Self manufactured					
1(b)	Imported					
2.	Other materials/chemicals					
3.	Total Material cost					
4.	Utilities – power, Power Steam Water etc					
5.	Employee cost					
6.	Direct expenses: Royalty Others(specify)					
7	Production Overhead					
	Adjt for opening/closing WIP					
8	Cost of Production					
9	ADMINISTRATIVE OVERHEADS Employees cost Repairs and Maintenance Depreciation Others Total					

TO BE PUBLISHED IN THE GAZETTED OF INDIA EXTRAORDINARY
(PART-I, SECTION-I)
GOVERNMENT OF INDIA
MINISTRY OF COMMERCE AND INDUSTRY
DEPARTMENT OF COMMERCE
PUBLIC NOTICE No. 22(RE-2012)/2009-14
NEW DELHI THE 11TH October, 2012

Subject:- Certification of various documents by Cost Accountants under Handbook of Procedure Vol.I andAppendices under Foreign Trade Policy.

In exercise of powers conferred under Para 2.4 of the Foreign Trade Policy, 2009-14, the DirectorGeneral of Foreign Trade hereby makes the following amendments in the Handbook of Procedure Vol.Iand Appendices 2009-2014 in public interest:

1. Wherever the term "Chartered Accountant" appears, it would deem to mean and include"Cost Accountant" also. Similarly, wherever the term "FCA" has been used in respect of aChartered Accountant, it would deem to mean and include the term "FCMA" in respect of aCost Accountant.
2. The words "CA Number" shall be substituted to read as "Membership Number".
3. The words "Cost and Works Accountant" shall be substituted to read as "Cost Accountant".

Effect of this Public Notice:- Under the EXIM Policy and Procedure, wherever certification by aChartered Accountant was required, the exporters would be able to get certification done by a CostAccountant also.

Sd/-
(AnupK.Pujari)
Director General of Foreign Trade
E-mail: dgft@nic.in
(F.No.01/94/180/468-Appendices/AM12/PC 4)

Cost Accounting Standards Board

REQUEST FOR COMMENTS

Cost Accounting Standards Board, the standard –setting body of the Institute, has approved the release of Exposure Draft of Guidance Note on Cost Accounting Standard on Administrative Overheads (CAS-11). The proposed exposure draft of Guidance Note may be modified in the light of comments received before being issued in final form.

Please submit your views/ comments/ suggestions on the Guidance Note on CAS -11 preferably by email, latest by 24thNovember, 2012.

Comments should be addressed to :

The Secretary,
Cost Accounting Standards Board
The Institute of Cost Accountants of India
3rd Floor, CMA Bhawan
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New Delhi- 110 003
Email id responses should be sent to :casb@icwai.org

Copies of this draft Cost Accounting Standard may be downloaded from the CASB Website at http://www.casbicwai.org

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA
(STATUTORY BODY UNDER AN ACT OF PARLIAMENT)
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Ref.No.Ex/12/2012 October 9, 2012

ANNOUNCEMENT

On 3rd October 2012 the Election Commission of India had notified the schedule of Gujarat State Assembly Elections, 2012.

The notification had stated that there will be 2 (Two) phases of Assembly Elections for Gujarat State Assembly Election 2012. For the first phase, the date of polling will be 13.12.2012 (Thursday) and the 2nd phase polling will be held on 17.12.2012 (Monday).

In view of the above, the Institute has rescheduled its December 2012 examination for Gujarat State only as per following :

Examination Centre	Original date of Examination	Revised date of Examination	Intermediate 9.30 A.M. to 12.30 P.M.	Final 2.00 P.M. to 5.00 P.M.	Foundation 2.00 P.M. to 5.00 P.M.
Surat Centre Code - 117	13.12.2012	23.12.2012	Applied Direct Taxation	Indirect & Direct Tax Management	NIL
Vapi Centre Code - 129	13.12.2012	23.12.2012	Applied Direct Taxation	Indirect & Direct Tax Management	NIL
Adipur-Kachchh Centre Code - 134	17.12.2012	23.12.2012	Applied Indirect Taxation	Business Valuation Management	Business Mathematics & Statistics Fundamentals
Ahmedabad Centre Code - 101, 132	17.12.2012	23.12.2012	Applied Indirect Taxation	Business Valuation Management	Business Mathematics & Statistics Fundamentals
Baroda Centre Code - 103	17.12.2012	23.12.2012	Applied Indirect Taxation	Business Valuation Management	Business Mathematics & Statistics Fundamentals

Scheduled date and Subject of Examination except above two days as per Time Table and Programme – December 2012 of above centres in Gujarat will remain unchanged.

The Examination Time Table and Programme – December 2012 for all other Centres in India and Overseas will remain unchanged.

A. Das
Director (Examination)

FOR THE ATTENTION OF MEMBERS IN FULL-TIME EMPLOYMENT

The Central Government vide the following notifications, has allowed cost accountants in full time employment,in addition to certification by members in full-time practice, to certify the Compliance Report to be filed with the Central Government in compliance with the following rules, namely:-

a) The Companies (Cost Accounting Records) Rules, 2011 notified vide GSR429(E), dated the 3rd June, 2011;
b) The Cost Accounting Records (Telecommunication Industry) Rules, 2011 notifiedvide GSR 869(E), dated the 7th December, 2011;
c) The Cost Accounting Records (Petroleum Industry) Rules, 2011 notified vide GSR870(E), dated the 7th December, 2011;
d) The Cost Accounting Records (Electricity Industry) Rules, 2011 notified vide GSR871(E), dated the 7th December, 2011;
e) The Cost Accounting Records (Sugar Industry) Rules, 2011 notified vide GSR872(E), dated the 7th December, 2011;
f) The Cost Accounting Records (Fertilizer Industry) Rules, 2011 notified vide GSR873(E), dated the 7th December, 2011;
g) The Cost Accounting Records (Pharmaceutical Industry) Rules, 2011 notified videGSR 874(E), dated the 7th December, 2011.

The Compliance Report would be required to be filed in XBRL mode and the member in employment would be required to affix his digital signature to the e-Form for filing of the report.

It may be noted that the status of the member would be checked by the MCA at the time of filing against the database of the Institute.

In case of members in full-time employment who would be certifying the Compliance Report of the company where they are employed, their attention is drawn to the above requirement and hereby advised to provide the Institute with full particulars of their employment, designation, employer's name with address and membership status for updating in the database of the Institute. In case there is mismatch of the member's status of employment as recorded in the database of the Institute, the validation of the Compliance Report may fail while being uploaded to the MCA Website.

The details are to be sent by signed hard copy to the Membership Department of the The Institute of Cost Accountants of India, 12, Sudder Street, Kolkata – 700 016. Scanned copy of the same may also be sent by e-mail to: membership.pradipta@icwai.org.

All members in employment are hereby requested to send their employment details to the Institute positively by **November 30, 2012**.

General Circular No: 33/2012

No. HQ/MCA/Digitized/ARBS/2009-Pt2
Government of India
Ministry of Corporate Affairs

5th Floor, "A" Wing, Shastri Bhawan,
Dr. R.P. Road, New Delhi - 110001
Dated: 16.10.2012

To

The President
Institute of Chartered Accountants of India, Institute of Company Secretaries of India and Institute of Cost Accountants of India

Subject: Quality of XBRL filing certified by Professional members.

Sir,

You are aware that XBRL filing of financial statements by a select class of companies for FY 2010-11 was mandated vide Ministry of Corporate Affairs Notification GSR No: 748(E) dated 05.10.2011. The e-forms were duly certified by CA/CS/CWA professionals for their completeness and correctness in representation with respect to audited financial statement of the company.

2. A random scrutiny of XBRL filing of financial statements by few companies to MCA for FY 2010-11 reveals significant variations in disclosures in published results and the XBRL filings due to 'incorrect' mapping of disclosures. It has been observed that few disclosures were 'mapped/tagged' with incorrect accounting concept despite availability of appropriate element in taxonomy. It has also been observed that provisions of "Block Text tagging" and/or "Footnote" have been inappropriately used to report disclosures, like subsidiary details, related party transactions, Director's Report, etc., even when appropriate elements were available in the taxonomy for such disclosures. Few instances of "incorrect" tagging of XBRL documents are provided at Annexure-I.

3. Such filing are inaccurate and do not adequately represent true and fair view of the state of affairs of the company as per Section 211 of the Companies Act, 1956. Such XBRL filings, apart from being misleading, also dilute the effectiveness of XBRL for stakeholders' usage relating to the companies. It is unfortunate that professionals have certified the authenticity of such incorrect data, for which they are liable to be penalized. Such lapses defeat the very purpose of introducing XBRL filings which are meant to elicit more detailed and refined information as to the affairs of companies. Please note that XBRL filings are being minutely scrutinized to see if similar mistakes also appear in a larger sample.

4. It is bounden duty of Institutes to direct its members to take necessary steps to improve the quality of XBRL filing for FY 2011-12 to be undertaken by its members. The Institute may conduct further trainings, issue guidelines, etc so that such quality related issues are appropriately resolved.

5. This may be accorded high priority.

Yours faithfully,

(Pankaj Srivastava)
Director

Encl: As above

Annexure-I

GENERAL XBRL FILING ERRORS

Errors	Observation
Cash Flow Statement not tagged	The Cash Flow Statement for FY 2010-11 is available in the Audited Financial Statements (PDF file). However, the same has not been tagged in XBRL financial statements filed at MCA portal.
Information of all subsidiaries not provided in XBRL financial statements	Information about one Subsidiary has been tagged in XBRL financial statements whereas the Company had nine Subsidiaries.
Information of all related party transactions not provided in XBRL financial statements	Related Party Disclosures have not been tagged in XBRL financial statement.
Parenthetical (additional disclosures) information not tagged in XBRL financial statements	Aggregate Market Value of Investments not provided by way of footnote. Additional information on Issued, Subscribed & Paid up Share Capital not explained by way of footnote.
Footnotes not tagged in XBRL financial statements.	Footnotes on Share Capital, Secured Loan, Reserve and Surplus, unsecured loan-Fixed deposits, Investments, Fixed Assets, Security deposit, etc have not been tagged. Footnote on "Investments" has not been given.
Different presentation in pdf and XBRL filings	The Annual Report presented before the shareholders the figures were presented in Rs Thousands whereas in the XBRL documents the figures were provided in Rs. Lakhs.
Incorrect usage of Footnote	Director's Report provided by way of footnote whereas separate tags are available for tagging of Directors' Report. Similarly, for Auditors' Report, Significant Accounting policies, Unsecured Loan, Current Liabilities, etc Footnote has been incorrectly used.

INCORRECT USAGE OF TAGS

A. When appropriate taxonomy element is available

Line Item	Tag Used (label)	Correct Tag (label)
Secured Cash Credit from Banks	Term Loan	Working Capital Loans Banks Secured
Investment in Quoted Equity Shares	Unutilized Money	Equity Securities Long Term Quoted
Bad debts written off	Other Provisions Created	Bad debts Advances written off
Investment (joint Venture)	Equity securities long-term unquoted non-trade	Investment joint ventures
Power and fuel expenses	Electricity expenses	Cost power fuel
Advertising and Brand marketing	Travelling conveyance	Advertising and promotional expenses
Travelling and conveyance	Legal professional charges	Travelling conveyance
Purchase/sale of Fixed Assets	Purchase other Assets, Proceed disposal other assets	Purchase tangible fixed Assets, Proceeds sale disposal tangible fixed assets

B. Incorrect tagging/ inaccurate disclosures

Line Item	Tag Used	Correct Tag	Remarks
Stock Differential-(Decrease)/ Increase	Not tagged separately	Increase decrease inventories	Clubbed with 'Other expenditure'.
Salaries, Wages & Bonus	Tagged as zero	Amount is 92,539,039	It is a mandatory tag. Clubbed with 'Other expenditure'.
Power, Fuel, Water & Gas	Tagged as zero	Amount is 248,737,864	Clubbed with 'Other expenditure'.

Manufacturing Cost	Tagged as zero		Clubbed with 'Other expenditure'. It is a manufacturing company.
RAW MATERIALS CONSUMED Opening Stock	Not tagged	Stock of Raw Materials, Opening Balance	Given as part of footnote to 'Raw Materials Consumed'
RAW MATERIALS CONSUMED Add: Purchases	Not tagged	Purchase raw materials during year	
RAW MATERIALS CONSUMED Less: Closing Stock	Not tagged	Stock of Raw Materials, Closing Balance	
Deferred Tax Liability (Net)	Net Deferred Tax Assets	Deferred Tax Liability	Tagged with negative sign.
Deferred tax liabilities(Net)	Deferred tax liability depreciation	Deferred tax asset other, Deferred tax asset VRS payment, Deferred tax asset provision for doubtful debts, etc	Disaggregated disclosures all consolidated into 'Deferred tax liability depreciation'

Regions & Chapters News

WIRC

Aurangabad Chapter of Cost Accountants (ACCA)

A full day seminar on eXtensible Business Reporting Language (XBRL) was organized by ACCA on 14th September, 2012 at Hotel Vits, Aurangabad.

CMA Sanjay Mundade Director—Commercial & CFO of SKODA Auto I. (P) Ltd was the Chief Guest. Senior members CMA A.G,Dalwadi & CMA M.A.Dalwadi of Ahmedabad shared their knowledge on basic concept of XBRL and its importance in view of the recent notifications of Ministry of Corporate Affairs, Govt of India. The e-filing of all annual returns of all companies through XBRL has been mandatory by MCA.

CMA R.S. Deshmukh Chairman, ACCA and CMA P. P.Mohani Chairman, PD Committee of the Chapter welcomed the guest, speakers and the audience.

The programme started with Ganesh Vandana after which CMA R.S.Deshmukh, briefly narrated the theme of the programme. CMA A.R.Joshi introduced the guest and speakers to the audience while CMA S.R. Pimple concluded the seminar with thought provoking remarks. CMA Amit Devdhe proposed vote of Thanks.

The seminar received an overwhelming response from the industry participants, practicing professionals and students.

Indore-Dewas Chapter of Cost Accountants (IDCCA)

A workshop was organized by IDCCA on 16th September 2012 at Hotel Surya, Indore on Emotional Intelligence. CMA P.D. Modh, Chairman, Oral Coaching Centre of Ahmedabad Chapter was the resource person for the workshop. CMA Modh discussed about the importance of EQ i.e. Emotional Quotient and explained its points of distinction with IQ i.e. Intelligence Quotient. He explained that various types of emotions like hate, anger, love, joy, sorrow jealousy etc. can be managed intelligently with the help of conscious approach. He emphasized that IQ may be helpful in initial part of career but to reach at heights, EQ plays very important role.

CMA (Dr.) Niranjan Shastri, Chairman, IDCCA welcomed all the delegates sitting on the dais and off the dais. CMA Vijay P. Joshi, Ex-Chairman, WIRC felicitated newly elected chairman of WIRC, CMA Shrenik Shah. In the felicitation ceremony, CMA Shrenik Shah felicitated passed out students of Foundation, Intermediate and Final. The program was attended and appreciated by delegates who included faculty members, members and students of our Institute. The program was covered by local media and almost all leading newspapers gave a good coverage to the event.

SIRC

In order to update and enhance the skill and knowledge of members, practitioners and the executives who are engaged in conducting audit under Tamil Nadu VAT, SIRC organized a Seminar on 'TN VAT – Audit' on 28th September, 2012 at its premises. Around 60 delegates have attended the Seminar. CMA S. Ramachandran, Chairman, Members in Practice Committee welcomed the delegates. CMA P. Raju Iyer, Vice-Chairman, SIRC introduced the speakers and also highlighted the significance of audit under Tamil Nadu VAT and requested the members to make use of the opportunity provided to the Cost and Management Accountants by Govt. of Tamil Nadu. On this occasion, Shri M.R.

Sivaraman, I.A.S., Former Revenue Secretary, Govt. of India rendered special address. There were four Technical Sessions which were handled by Shri P. Ravindran, eminent Advocate & Consultant – Indirect Taxes, Chennai and Shri K.K. Sekar, DGM – Indirect Taxes, Ashok Leyland Ltd., Chennai. Technical Session I & II dealt with 'Legal Aspect of TN VAT Audit with updated amendments'. During the Interaction Session, the resource Persons clarified the queries raised by the participants and the audience.

CMA P. Raju Iyer, Vice Chairman, SIRC proposed vote of thanks.

The third centralized Campus Placement programme was organized by SIRC on 5th October, 2012 at Hotel Vestin Park, Chennai. Around 150 candidates participated in this Job fair. SEBI, ITC Limited, Tata Consultancy Services, Larsen & Tubro Ltd and Lucas—TVS Ltd. took part in the 'Job Mela' and selected candidates. Earlier, an orientation programme comprising 'Interview Techniques', 'Group Discussion' & 'Mock Interview' were conducted for the candidates who participated in the campus placement in order to enhance their skills to face the interview.

EIRC

EIRC organized a workshop on "Performance Appraisal Report" on 5th October 2012 at EIRC Premises. CMA Chitra Agarwal, Chairman, MDP Committee welcomed the members. CMA T.C.A. Srinivasa Prasad Council Member was the key speaker who very lucidly gave a presentation covering every aspects of Form III. The session was very interactive and there was overwhelming response from members who participated in the workshop.

EIRC organized a Workshop on CARR & CAR on 15th September 2012 at EIRC Premises. CMA Ashok Mukherjee Chairman, EIRC welcomed the members. CMA (Dr) Sanjiban Bandyopadhyaya, Council Member and CMA Somnath Mukherjee, Ex-CCM of the Institute were the speakers. Dr. Bandyopadhyaya explained in detial the relevance and inportance of various circulars issued by Ministry of Corporate Affairs. CMA Somnath Mukherjee addressed the members on different issues of Cost Audit and Performance Appraisal Report. The programme was very interactive and lively.

NIRC

NIRC of the Institute organized a Seminar on "XBRL Concept – Cost Audit & Compliance Report" on 28th

September 2012 at Scope Auditorium, Scope Complex, New Delhi. CMA Vijender Sharma, Chairman of NIRC coordinated the Seminar and welcomed CMA B.B. Goyal, Advisor (Cost), Govt. of India and the Key note Speaker Shri Vijay Sahni, Director, Webtel. Also present were Shri Nimesh, Consultant, TC&MCA, Shri Ankit of Webtel and other members. CMA B.B. Goyal, Advisor (Cost), MCA, was the Chief Guest of the seminar who inaugurated the Seminar by lighting the lamp CMA B.B. Goyal explained the key points of Cost Audit & Compliance Report in XBRL format. Shri Vijay Sahn, Director, Webtel gave a power point presentation and presented a demo for filing of XBRL form. All the queries raised by the participants were well replied to by the eminent speakers.

NIRC of ICAI organized a mock Interview on 7th October2012, at CMA Bhawan, New Delhi for the benefit of final passed out students of June 2012. CMA Vijender Sharma, Chairman, NIRC welcomed the Chief Guest CMA Subhash Agarwal, Director Finance, CCI. Shri J.K. Teotia, Addl Secretary, SFIO,was the Guest of Honour and Mr. L. Gurumurthy, Director, Tranning & Placement of the Institute was the special Invitee. The students benefitted a lot from the programme.

Advanced Certificate Courses by the Directorate of Advanced Studies

The Directorate of Advanced Studies of the Institute announces the following three advanced certificate courses :

- Course on Business Valuation and Corporate Restructuring;
- Course on Treasury and Financial Risk Management; and
- Course on Enterprise Performance Management and Appraisal System

These courses will be delivered at the proficiency level to develop expert knowledge. The objective is to bridge the gap between the capabilities needed by the industry and regulators and capabilities available in the market. On successful completion, participants will develop capabilities to deliver professional services in respective areas. The courses will be open to members of the Institute of Cost Accountants of India and others who have relevant experience.

On successful completion of a course, the participant will be awarded a certificate.

The information relating to the eligibility criteria, course fee, course duration, course contents and other pertinent details for each of these courses is available on the Institute's website.

The first batch for the Course on Enterprise Performance Management and Appraisal System is already running at Hyderabad. The second batch of the course alongwith the other two courses are scheduled to commence in January' 2013.

Registrations and nominations are invited for all the three courses and the last date for registration is **December 3, 2012**.

Ask for a brochure by mailing to: advstudies@icwai.org, advstudies.kimi@icwai.org

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA
(statutory body under an Act of Parliament)

MANAGEMENT DEVELOPMENT PROGRAMMES 2012-13

DURATION	TOPIC	VENUE	FEE (RS.) NON-RESIDENTIAL	FEE (RS.) [illegible]
	NOVEMBER, 2012			
20-23	Basic Financial Skills for Non Finance Executives and Engineers	Mysore		35000*
29 Nov. – Dec 8	International Programme on 'Strategic Financial Management'	Singapore, Kualalumpur & Bangkok	-	250000*
	DECEMBER, 2012			
11-14	Recent Trends in Financial Management	Amritsar		35000*
18-21	Contracts and their Management	Shirdi	-	35000*
18-21	Emerging Issues in Direct and Indirect Taxation	Shirdi	-	35000*
26-30	Certificate Course on IFRS and Converged Indian Accounting Standards	Mumbai	25000*	-
	JANUARY, 2013			
02-04	Costing for Engineers	Chennai	15000*	40000*
08-12	Recent Trends in Corporate Reporting including IFRS and Revised Schedule VI	Hyderabad	-	35000*
08-12	Advance Tax, TDS and Tax Planning	Hyderabad	-	35000*
	FEBRUARY, 2013			
19-22	Risk Based Internal Audit for Effective Management Control	Puri	-	35000*
19-22	Emerging Issues in Management of Taxation	Puri	-	35000*

Note :- *Plus 12.36% Service Tax.

For Non-Residential Programmes: - Fee includes course fee, course material, lunch, tea/coffee etc.

For Residential Programmes - Fee includes course fee, course material, accommodation on Single Room basis, all meals and visits. The charges for accompanying spouse would be Rs. 1000/- (Rupees one thousand only) towards accommodation, all meals and visits for all the three days excluding International programmes.

CEP Credit Hours - (For 1 Day Prog. - 4 Hours) (For 2 Days Prpg. - 6 Hours) (For 3 Days & more Prog.- 10 Hours)

For Kind information:

For outstation programmes the participants are requested to get the confirmation from the Institute before proceeding to the venue. If any participant reaches the venue for the postponed/cancelled programmes without getting the confirmation from the Institute, the Institute will not be held responsible for the same. The cancellation/postponement of the programmes, if any, will be intimated to only those organizations whose nominations have been received by the Institute on time.

For residential programmes normally the first day check-in is at 12.00 noon and last day check-out is at 12.00noon

The Payment of the Fee is to be made by Cheque/DD in favour of 'The Institute of Cost Accountants of India' payable at New Delhi.

Details for ECS Payment: State Bank of India (60321), Andhra Association Building, 24-25 Institutional Area, Lodhi Road, New Delhi- 110003
Current A/c No. 30678464753 MICR Code : 110002493 IFCS Code : SBIN0060321

The Institute of Cost Accountants of India

(Statutory Body Under An Act of Parliament)

Examination Time Table & Programme — December 2012

Programme for Syllabus 2008

Day, Date & Time	Intermediate 09.30 A.M. to 12.30 P.M.	Final 02.00 P.M. to 05.00 P.M.	Foundation 02.00 P.M. to 05.00 P.M.
Monday 10 th December, 2012	Financial Accounting	Capital Market Analysis & Corporate Laws	
Tuesday 11 th December, 2012	____	Financial Management & International Finance	
Wednesday 12 th December, 2012	Commercial and Industrial Laws & Auditing	Management Accounting-Strategic Management	
Thursday 13 th December, 2012	Applied Direct Taxation	Indirect & Direct – Tax Management	
Friday 14th December, 2012	Cost & Management Accounting	Management Accounting – Enterprise Performance Management	Organisation and Management Fundamentals
Saturday 15 th December, 2012	____	Advanced Financial Accounting & Reporting	Accounting
Sunday 16 th December, 2012	Operation Management and Information Systems	Cost Audit & Operational Audit	Economics and Business Fundamentals
Monday 17 th December, 2012	Applied Indirect Taxation	Business Valuation Management	Business Mathematics and Statistics Fundamentals

Programme for Management Accountancy—December 2012 Examination

Monday 10th December, 2012 09.30 A.M. to 12.30 P.M.	Monday 10th December, 2012 02.00 P.M. to 05.00 P.M.	Tuesday 11th December, 2012 09.30 A.M. to 12.30 P.M.	Tuesday 11th December, 2012 02.00 P.M. to 05.00 P.M.	Wednesday 12th December, 2012 09.30 A.M. to 12.30 P.M.
Management Accountancy	Advance Management Techniques	Industrial Relations & Personnel Management	Marketing Organisation & Methods	Economic Planning & Development

Examination Fees

Groups (s)	Final Examination	Intermediate Examination	Foundation Course Examination	Management Accountancy Examination
One Group (Inland Centres) (Overseas Centres)	₹ 1250/- US $ 100	₹ 1000/- US $ 90	₹ 1000/- US $ 60	Per Group ₹ 2500/-
Two Groups (Inland Centres) (Overseas Centres)	₹ 2250/- US $ 100	₹ 1600/- US $ 90		

1. (a) Application Forms for Foundation Course, Intermediate and Final Examinations are available from Institute's Headquarters at 12, Sudder Street, Kolkata, Regional Councils and Chapters of the Institute on payment of ₹ 50/- per form. In case of overseas candidates, forms are available at Institute's Headquarters only on payment of US $ 10 per form.
   (b) Students can also download the Examination Form from ICAI Website at www.icwai.org.
   (c) Students can also submit the form online.
2. Last date for receipt of Examination Application Forms without late fees is 10th October, 2012 and with late fees of ₹ 300/- is 20th October, 2012.
3. Examination fees to be paid through Bank Demand Draft of requisite fees drawn in favour of "The Institute of Cost Accountants of India" and payable at Kolkata.
4. Students may submit their Examination Application Forms along with the fees at ICAI, 12 Sudder Street, Kolkata - 700016 or Regional Offices or Chapter Offices. Any query in this regard may be addressed to Examination Directorate at 12, Sudder Street, Kolkata - 700016.
5. Finance Act 2011, involving Assessment Year 2012-2013 will be applicable for the subjects Applied Direct Taxation (Intermediate), Applied Indirect Taxation (Intermediate) and Indirect & Direct - Tax Management (Final) for the purpose of December 2012 term of Examination under Revised Syllabus 2008.
6. Examination Centres: Adipur-Kachchh(Gujarat), Agartala, Ahmedabad, Akurdi, Allahabad, Asansol, Aurangabad, Bangalore, Baroda, Berhampur(Ganjam), Bhilai, Bhilwara, Bhopal, Bhubaneswar, Bilaspur, Bokaro, Calicut, Chandigarh, Chennai, Coimbatore, Cuttack, Dehradun, Delhi, Dhanbad, Durgapur, Ernakulam, Faridabad, Ghaziabad, Guwahati, Hardwar, Howrah, Hyderabad, Indore, Jaipur, Jabbalpur, Jalandhar, Jammu, Jamshedpur, Jodhpur, Kalyan, Kannur, Kanpur, Kolhapur, Kolkata, Kota, Kottayam, Lucknow, Ludhiana, Madurai, Mangalore, Mumbai, Mysore, Nagpur, Naihati, Nasik, Nellore, Neyveli, Noida, Panaji (Goa), Patiala, Patna, Pondicherry, Pune, Rajahmundry, Ranchi, Rourkela, Salem, Shillong, Solapur, Surat, Thrissur, Tiruchirapalli, Tirunelveli, Trivandrum, Udaipur, Vapi, Vashi, Vellore, Vijayawada, Vindhyanagar, Waltair and Overseas Centres at Bahrain, Dubai and Muscat.
7. A candidate who is completing all conditions will only be allowed to appear for examination.
8. Probable date of publication of result : Foundation—1st February, 2013 and Inter & Final - 21st February, 2013.

A. Das
Director (Examination)

11th Edition

Cost Congress 2012

Confederation of Indian Industry
Total Cost Management Division

International conference on **Total Cost Management**

6 & 7 December 2012 Hotel Hilton, Chennai

Theme:
Changing Business Model in Turbulent Times - Leveraging TCM

Objectives :

Evolve and standardize best practices of TCM across the sectors in the industry Provide a forum for sharing best practices by the industry and domain experts

Focus Areas:

- Steering through turbulent times
- Achieving excellence through business model
- Re-modelling supply chain in turbulent times
- Leveraging TCM for manufacturing excellence
- Re-modelling reporting framework
- Maturity Model case study presentations

Pre Event TCM Workshop

Target Audience

- Middle level functional heads of all departments
- CA / CMA / CS / MBA / ICAI Students

Date & Venue :
Date : 5 Dec 2012
Venue: Hotel Hilton, Chennai

Contact:

Mithun G
mithun.g@cii.in
+91 40 4418 5172

Date & Venue

Date : 6 & 7 December 2012
Venue : Hotel Hilton, Chennai

Master Speaker:
Mr. Charles Tilley
Chief Executive
CIMA

Speakers Confirmed
Mr Nilendu Sarkar
Vice President Supply Chain
Hindustan Unilever Limited

Ms Sonia Shrivastava
CSR Head South Asia
Intel

Knowledge Partner

CIMA | Chartered Institute of Management Accountants

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Lighting of the sacred lamp by CMA S.C. Mohanty, Vice President of the Institute at the joint conference of the Institute with ASSOCHAM at India Habitat Centre, New Delhi on 18.10.12. Also seen Prof K.V. Thomas, Hon'ble MoS (IC) for Consumer Affairs, Food & Public Distribution, Shri D.S. Rawat, Secretary General, ASSOCHAM (extreme right), Shri Sanjay Mitra, Head (Indirect Taxes), ITC Ltd

Release of 'Knowledge Study' on "Inter State Trade – Transforming India into Single Market" in the hands of Prof K.V. Thomas, Hon'ble MoS (IC) for Consumer Affairs, Food & Public Distribution. Also seen CMA S.C. Mohanty, Vice President of the Institute, Shri D.S. Rawat, Secretary General, ASSOCHAM and Shri P.K. Jain, Chairman, SME Council, ASSOCHAM

The Institute spreads its wings to small towns and rural areas hitherto unreached

Inauguration of CMA Support Centre at Pudukottai, Tamil Nadu on 13.10.12 by Shri V. Kuthik Thoandaiman, Hon'ble MLA of Pudukottai

Inauguration of CMA Support Centre at Pollachi, Tamil Nadu on 12.10.12 by Shri K. Sukumar, Hon'ble MP of Pollachi

Inauguration of CMA Support Centre at Puliamputti, Tamil Nadu on 12.10.12

Inauguration of CMA Support Centre at Nagapattinam on 15.10.12

Inauguration of CMA Support Centre at Mayiladurai on 15.10.12

Inauguration of CMA Support Centre at Pattukkottai on 13.10.12 by Shri N.R. Rangarajan, Hon'ble MLA of Pattukkottai

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Editor : Rajendra Bose