TOLL FREE 18003450092 / 1800110910

Azadi Ka Amrit Mahotsav

November - 2022 Issue

CMA Student E - Bulletin

FINAL

The Institute of Cost Accountants of India

Statutory Body under an Act of Parliament

www.icmai.in

CONTENTS

I. Knowledge Update ... 1

II. Corporate Laws & Compliance (CLC) ... 2

Composition of Board of Directors Under The Companies Act, 2013 ... 3

III. Strategic Financial Management (SFM) ... 8

Section C & Study Note 8: Security Analysis and Portfolio Management ... 9

IV. Strategic Cost Management Decision Making (SCMD) ... 13

Costco striving to provide Maximum Life Time Customer Value! ... 14

V. Direct Tax Laws and International Taxation (DTI) ... 20

Equalisation Levy ... 21

VI. Corporate Financial Reporting (CFR) ... 29

MCQ on Intangible Assets and Impairment of Assets ... 30

VII. Indirect Tax Laws & Practice (ITP) ... 33

Indirect Tax ... 34

VIII. Cost & Management Audit (CMAD) ... 39

Understanding Administrative Overheads (CAS – 11) ... 40

IX. Strategic Performance Management and Business Valuation (SPBV) ... 44

Valuation of Bonds And Mergers and Acquisitions ... 45

X. Examination Time Table ... 49

XI. Practical Advice ... 50

XII. Submissions ... 51

XIII. Message from Directorate of Studies ... 52

XIV. Few Snapshots ... 54

KNOWLEDGE
Update

In this section of e-bulletin we shall have a series of discussion on each of these chapters to provide a meaningful assistance to the students in preparing themselves for the examination at the short end and equip them with sufficient knowledge to deal with real life complications at the long end.

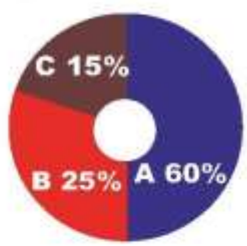
GROUP: 3, PART: 13

CORPORATE

LAWS & COMPLIANCE - (CLC)

Shri Subrata Kr. Roy
Company Secretary & Consultant
He can be reached at:
subrataoffice@rediffmail.com

Your Preparation Quick



Syllabus Structure
A Companies Act 60%
B Other Corporate Laws 25%
C Corporate Governance 15%

Learning Objectives:

Read the Study Material minutely.

- For details or if you don't understand Study Material or the section is important to identify the topic, then refer to Bare Act, otherwise reference to Bare Act is not necessary. For Company Law, book by Avtar Singh is recommended. For other laws Institute Study Material is sufficient.
- The words used in any of the texts as mentioned above should be understood by immediate reference to the Dictionary.
- The main points coming out in any of the provisions should be either underlined or written in separate copy which has to be repeated again and again.
- Theoretical knowledge should be adequate and clear before solving practical problems.
- Don't write wrong English. It changes the meaning and therefore answer may be wrong even when the student's conception is clear. Also don't make spelling mistakes.

Composition of Board of Directors Under The Companies Act, 2013

Board of directors is individual, and is defined as a person occupying the position of directory, by whatever name called. Director collective are called as board of director. Any persons who control the management of the company will be deemed as director, through his designation can be different.

Maximum no. of Directors – **in case of public limited company is 15. However, any company may increase number of directors, with the permission of central court. There is no maximum specified for private company.**

Minimum no. of Directors – 2 (in the case of private company)

- 3 (in the case of public company)

No. of directors above 15 requires approval by special resolution of shareholders.

One director to be resident individual.

At least one women director in case of listed company.

(Directors appointed by BIFR and Central Govt. shall not be counted for total number of directors.)

ROTATIONAL AND NON-ROTATIONAL DIRECTORS

At least 2/3rd shall be eligible to retire by rotation in every AGM.

Out of 2/3rd, 1/3rd must retire in every AGM.

(Directors appointed by CG, BIFR, FI/Banks shall not be taken in to account for calculating the number of rotational directors)

Listed companies shall have 50% of the Board's strength as independent director if the chairman is executive and 1/3rd if chairman is non-executive.

Tenure of non-rotational director or full time director shall not be for more than 5 yrs.

KMP- **Key managerial personnel in relation to a company means-**

(i) the Chief executive officer or the managing director or manager.
(ii) the company secretary
(iii) the whole-time director
(iv) the Chief financial officer
(v) such other officer as may be prescribed

NATURE OF COMPANY MANAGEMENT

Shareholders are the owners of the company. They can anytime decide to run themselves or may like persons to act on their behalf for management of the company and highest level of such inclusion of outside person is director, who will be member of the board of director.

Management powers to be exercised by:	Type of Powers	Reference
Shareholders	Powers not given/delegated to the Board of Directors.	Section 180 of the Companies Act, 2013 and Articles of Association of the company.
Board of Directors	All powers of decision making about the company unless reserved for the shareholders.	Section 179 of the Companies Act, 2013.

Chairman	Executive/ Non- Executive functions of the company. Chairing the Company meetings.	Section 104 of the Companies Act, 2013.
C.M.D	Exercises both Chairman and Managing Director's Power.	
Managing Director **-Should be of 21-70 years** **-is an undischarged insolvent** **-has not suspended payment to its creditors** **-has not been convicted of any offence for a period of more than 6 months.**	Has substantial powers of the management of the company. Works under the supervision and control of the Board of Directors.	Section 196 of the Companies Act, 2013.
Whole Time Director/Functional Director	Full time employee of the company. Looks after specified functions of the company.	

Type of Directors	Appointing Authority	Situation of appointment	Tenure of Office
First Directors	Articles of Association	At the time of registration	Upto first AGM
Normal Directors	Shareholders in Annual General Meeting.	Normal	To retire on the basis of seniority
Additional Directors	Board of Directors	In between two AGMs	Till the next AGM or the last date in which the AGM should have

			been held whichever is earlier.
Alternate Directors	Board Of Directors	When the original Director is out of India for more than 3 months	Till the return of the original Director.
Directors appointed by Central Government	Central Government	Inspection and Investigation Oppression and Mismanagement	As per order
Director appointed by B.I.F.R	B.I.F.R (Board of Industrial and Financial Reconstitution)		As per BIFR order.
Director appointed / nominated by Financial Institute/Government	Nominated by Financial Institute (Appointed by shareholders at AGM)	Company taken loan from the institution, equity investment in the company.	As per FI/ Bank
Independent directors (Section 149)	For all listed companies at AGM.	Paid up capital 10cr/turnover 100cr/outstanding loan 50cr.	5 consecutive terms but can be re-appointed by passing a special resolution.
Directors appointed by small shareholders.	Small shareholder who holds shares of nominal value of not	In AGM. Any listed company may or shall in case of notice by 1000 small shareholders (or 1/1oth of such category	Up to 3 years. Shall be rotational. Considered to be independent.

	more than twenty thousand rupees.	of shareholders having holding of face value of rs. 20000)	
Shadow Directors	Legally not a director.	Persons who control the affairs or control the majority of directors.	

Appointing Retiring Director

The nomination for appointment of a Director who retires in an AGM and is eligible for reappointment automatically comes up in the said meeting unless a resolution to the effect that he will not be appointed or someone else will be appointed in his place is moved.

Appointment of a person as a director for the first time.

Apart from the above provision Under Section 160 of the Companies Act, 2013 a person who is not a retiring director can also be eligible for appointment as a director of a company provided he deposits his candidature in writing, himself or through some other member of the company at least 14 days before the meeting along with a fee or ` 1 lakh which shall be refunded if the candidate gets minimum 25% of the votes casted.

Vacation of office of directors: (Section 167)

The office of a director shall become vacant if he is disqualified by an order of the court or Tribunal or by personal capacity.

GROUP: 3, PART: 14

STRATEGIC

FINANCIAL MANAGEMENT - (SFM)

Dr. Swapan Sarkar
Assistant Professor
Department of Commerce
University of Calcutta
He can be reached at:
swapansarkar22@gmail.com

Your Preparation Quick

Syllabus Structure

A Investment Decisions 25%
B Financial Markets and Institutions 20%
C Security Analysis and Portfolio Management 25%
D Financial Risk Management 30%

Learning Objectives:

After studying this section on Strategic Financial Management, you will be able to:

- understand the direct and indirect quotations
- know the European terms and American terms

Section C & Study Note 8: Security Analysis and Portfolio Management

- **Steps in Portfolio Management**

Portfolio management involves the following steps.

a) **Identification of objectives and constraints:** The primary step in portfolio management is to identify the objectives (income, capital appreciation, minimisation of risk etc.) and constraints of the investors (fund constraints or other technical difficulties such as not having a de-mat account etc.)

b) **Selection or Choice of the asset mix:** The next major step in portfolio management process is identifying different assets that can be included in portfolio in order to spread risk and minimize loss.

c) **Formulation of portfolio strategy:** The next step in the portfolio management process is formulation of an appropriate portfolio strategy. There are two choices for the formulation of portfolio strategy, namely, an active portfolio strategy; and a passive portfolio strategy. In case of an active portfolio strategy.

d) **Security analysis and selection:** In this step various individual securities or assets are analysed to explore their possible return and risk. The analysis should involve economic analysis, industry analysis and lastly company analysis (this process is known as *fundamental analysis*) for a long-term value investment objective or analysing the past trend in securities prices in stock market (known as technical analysis).

e) **Portfolio execution:** In this step actual investment is executed in the selected securities after all the necessary formalities. The amount of investment is decided based in the overall plan or objectives of the investor.

f) **Portfolio evaluation:** In this step, the investor or the financial planner evaluates the performance of the portfolio by various portfolio performance evaluation tools ranging from total return to risk adjusted returns, tracking error etc. and thereby identifies the requirement of any revision in the portfolio in order to better cope up with the economic scenario or to achieve the short and long term objectives.

g) **Portfolio revision:** This involves selling out an existing investment and investing the money realised in another channel or instruments. However, it may sometime also involve changing the mix of existing constituents in the portfolio already constructed.

- **Return and Risk**

While evaluating the performance of any portfolio, the two considerations that play the most important role are return and risk.

- **Concept of Return**

Return is the compensation an investor receives from any investment for the uncertainty involved in such investment and for the deferment of his current consumption. It is the principal reward from the investment. Return on any investment comprises of two components namely, income component and capital gain (or appreciation) component. While income component represents the periodic payouts of an investment (preferably in cash), capital appreciation component represents the increase in the value of the initial investment. Investments such as bank deposits offer only the income component while any market linked instruments (such as shares, bonds traded in the market and mutual funds) offer both return as well as capital appreciation. Thus, total return of a security is the sum of income component and capital appreciation.

- **Types of Return**

Return from an investment can be either Ex-post Return or Ex-ante Return.

I. Ex-post Return

Ex-post return, also called realized return, refers to the return that has been earned or realized. Thus, it is historical in nature.

The formula for calculating ex-post return is given by,

R_t = Regular return + capital appreciation = $\frac{D_t}{P_{t-1}} + \frac{P_t - P_{t-1}}{P_{t-1}}$

Where, D_t is the dividend received during the period t

P_t is the current price of the security

P_{t-1} is the price of the security at the beginning of the period t

While using the above formula, dividend is assumed to be received at the end of the holding period.

Ex-post return for a given period is also known as holding period return (HPR). The above formula is for Single Period Ex-Post Return.

Illustration 1

An investor bought 100 shares of X Ltd. on April 30, 2022 for Rs.8,000 per share. the company paid a dividend of Rs.300 on April 30, 2023. if the price of the stock on May 1, 2023, is Rs.8,500, then calculate the ex-post return for the one-year time horizon.

Solution:

Ex-post return is given by,

R_t = Regular return + capital appreciation = $\frac{D_t}{P_{t-1}} + \frac{P_t - P_{t-1}}{P_{t-1}}$

Where, D_t is the dividend received during the period t = Rs.300

P_t is the current price of the security = Rs.8,500

P_{t-1} is the price of the security at the beginning of the period t = Rs.8,000

So, $R_t = \frac{300}{8000} + \frac{8500-8000}{8000}$ = 0.10 i.e., 10%

For multi period investments, an investor can calculate either Total Return or Average Return. Average Return can be calculated using either simple average (arithmetic mean) or geometric average (geometric mean).

An 'n' year multi period total return or holding period return = $[(1+R_1)(1+R_2)\ldots(1+R_n)] - 1$.

Arithmetic Average Return $(\bar{R}) = \frac{\sum_{t=1}^{n} R_t}{n}$ where R_t = ex-post return for period t; n = no. of periods.

In case single period ex-post returns are negative, the Arithmetic Average Return produces somewhat misleading results. This is why Geometric Mean Return is preferred. It is calculated as follows:

Geometric Mean Return = $[(1+R_1)(1+R_2)\ldots(1+R_n)]^{1/n} - 1$.

It is also known as Compound Annual Rate of Return.

Consider the following example.

Illustration 2

The price movement and dividend per share of RIL is given below.

Financial Year	Price at the end (P_t) (Rs.)	Dividend Received (D_t) (Rs.)
2010-11	600	45
2011-12	650	30
2012-13	720	25
2013-14	760	40
2014-15	800	35
2015-16	850	45
2016-17	830	50
2017-18	870	55
2018-19	900	60

You are required to calculate, for the period 2011-12 to 2018-19:

a) Single period ex-post returns

b) Arithmetic average return

c) 8 year holding period return

d) Compound annual rate of return

Solution:

Single period ex-post return is given by,

$R_t = \frac{D_t}{P_{t-1}} + \frac{P_t - P_{t-1}}{P_{t-1}}$

Calculation for single period ex-post returns

Financial Year	P_t	D_t	$\frac{D_t}{P_{t-1}}$	$\frac{P_t - P_{t-1}}{P_{t-1}}$	R_t (%)
2010-11	600	45	-----	-----	------

2011-12	650	30	$\frac{30}{600}$	$\frac{50}{600}$	$\frac{80}{600} = 0.13$
2012-13	720	25	$\frac{25}{650}$	$\frac{70}{650}$	$\frac{95}{650} = 0.15$
2013-14	760	40	$\frac{40}{720}$	$\frac{40}{720}$	$\frac{80}{720} = 0.11$
2014-15	800	35	$\frac{35}{760}$	$\frac{40}{760}$	$\frac{75}{760} = 0.10$
2015-16	850	45	$\frac{45}{800}$	$\frac{50}{800}$	$\frac{95}{800} = 0.12$
2016-17	830	50	$\frac{50}{850}$	$\frac{-20}{850}$	$\frac{30}{850} = 0.04$
2017-18	870	55	$\frac{55}{830}$	$\frac{40}{830}$	$\frac{95}{830} = 0.11$
2018-19	900	60	$\frac{60}{870}$	$\frac{30}{870}$	$\frac{90}{870} = 0.10$
Total					0.86

Arithmetic Average Return ($\bar{R}$) = $\frac{\sum_{t=1}^{n} R_t}{n}$ = 0.86/8 = 0.10 = 10%.

8 year holding period return = $[(1+R_1)\ (1+R_2)\ldots..(1+R_n)] - 1$

= [(1+0.13)(1+0.15)(1+0.11)(1+0.10)(1+0.12)(1+0.04)(1+0.11)(1+0.10)] – 1 = 2.26 -1

= 126%

Compound annual rate of return = $(2.26)^{1/8} - 1$ = 1.107 – 1 = 0.107 = 10.7%.

Note: While calculating the return, appropriate adjustment has to be made for bonus and stock split declaration.

Note: <u>Annualized HPR</u>:

For holding period less than one year, annualized return can be calculated as follows:

Annualized HPR = $(1+ \text{HPR})^{365/52/12 \div \text{holding period}}$ -1

For example, if 3 month HPR is 6%, then Annualized HPR = $(1+0.06)^{12/3} - 1$ = 26%. This is also known as effective return.

Note: <u>Real Return</u>:

It is inflation adjusted return. It is calculated as follows:

Real Return = $\left(\frac{1+Nominal\ Return}{1+Inflation\ rate}\right) - 1$.

For example, if HPR is 12% with inflation rate 2%, then real return = $\frac{1+0.12}{1+0.02}$ -1= 9.8%.

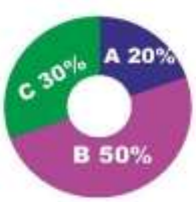
GROUP: 3, PART: 15

STRATEGIC

COST MANAGEMENT DECISION MAKING - (SCMD)

CMA(Dr.) Sreehri Chava
Cost & Management Consultant,
He can be reached at:
sreeharichava@yahoo.co.in

Your Preparation Quick



Syllabus Structure
A Cost Management **20%**
B Strategic Cost Management Tools and Techniques **50%**
C Strategic Cost Management - Application of Statistical Techniques in Business Decisions **30%**

Learning Objectives:

The Strategic cost management framework provides a clear plan of attack for addressing costs and decisions that affect them. It helps to get answers on:

- Is there a plan for strategic cost management
- Have the controlling functions for each significant cost in the organization been identified
- Are there resources devoted to finding or obtaining new approaches to breaking cost barriers
- Is cost modelling being used or is there an active effort to develop or buy cost modeling capability

Costco striving to provide Maximum Life Time Customer Value!

01.00: The Business

Costco Wholesale Corporation (Costco) is a membership warehouse club, dedicated to bringing its members the best possible prices on quality brand-name merchandise. Costco operates more than 800 locations worldwide and provides a wide selection of merchandise, plus the convenience of specialty departments and exclusive member services.

02.00: The History

The company's first location, opened by entrepreneur Sol Price in 1976 under the name Price Club, was in a converted airplane hangar on Morena Boulevard in San Diego, California, USA. Price introduced the world's first membership warehouse club, a place where efficient buying and operating practices gave members access to unmatched savings. Thus was initiated a ground-breaking retail concept.

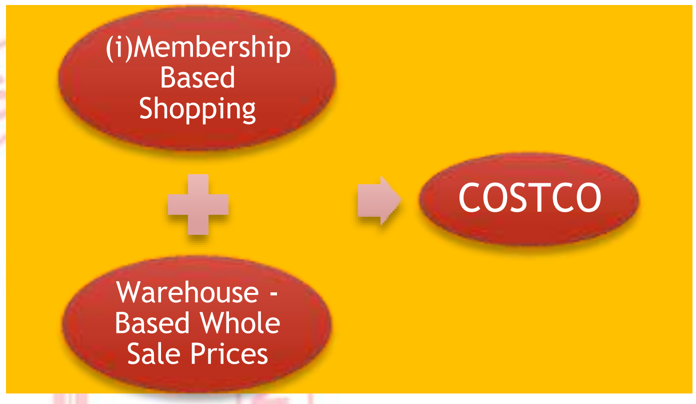
At first, Price Club was limited exclusively to business members, who could purchase a wide range of supplies and wholesale items. Jim Sinegal, the executive vice president of merchandising, distribution and marketing, was instrumental in fine-tuning the merchandise and marketing strategies, helping to turn Price Club into a success story that changed the face of retailing worldwide. Seven years later, Jim Sinegal channelled his expertise into co-founding Costco Wholesale with Jeff Brotman, and together they opened the first warehouse in Seattle, Washington in 1983. Eventually, Costco became the first company ever to grow from zero to $3 billion in sales in less than six years.

Over the next decade, both Price Club and Costco Wholesale continued to innovate and grow, and in 1993, the two mega-retailers merged, creating a gifted leadership team that soon made Costco the world's most successful warehouse club. At the time of merger in 1993, the combined company, operating under the name PriceCostco, had 206 locations generating $16 billion in annual sales. Since resuming the Costco name in 1997, the company has grown worldwide with total sales in fiscal year 2021 exceeding $192 billion.

03.00: The Business Model

In principle, the company is engaged in the operation of membership warehouses and focuses on offering merchandise to customers at wholesale prices. The unique proposition is 'Providing Life Time Value to Customers'. The key elements of the business model are twofold, viz.

(i) Membership Based Shopping, and
(ii) Warehouse Based Whole Sale Prices.



03.01: Membership Based Shopping: The primary component of the model is the membership-based shopping. It simply means that in order to shop at any Costco store, one needs to be a member. This membership attracts a fee. Also, membership fees can vary as the company operates a tier system.

There are two categories of membership offered by Costco. These are:

a. **Gold Star Membership**: This membership category, with an annual fee of $60 in US, is designed to cater to the needs of individual customers who specifically want to benefit from the high discount prices offered by the company.
b. **Business Membership:** This type of membership is designed for small and medium-sized businesses (SMBs). It is set up to help optimize the resale of Costco goods by these outlets. Outside SMBs, individuals who have a business license or evidence of business ownership are also eligible for this membership type.

In addition to this, the company also offers Executive Memberships. This allows customers to collect points and earn rewards as they perform certain activities or transactions with Costco. Unlike many other brands, Costco has been able to find a way around its membership requirement to create a barrier to entry. Because of this, it has been able to accrue nearly 119 million members as of August 2022. The membership fees generated, as a result, account for more than 2% of the company's annual income.

03.02: Warehouse Based Whole Sale Prices: The second feature is that, being conceived as a warehouse club, Costco sells its products in bulk from the warehouse itself. In general, Costco warehouses carry about 4,000 SKUs (stock keeping units) compared to the 30,000 found at most supermarkets. The selection is limited to nationally-branded private-label products, but comprising a wide range that can produce high sales volumes and rapid inventory turnover. Bulk of the purchases are direct from the manufacturer; Distribution is efficient; Handling of merchandise (with no frills) is minimum; and the warehouse facilities are on self-service mode. As a consequence, the entity achieves substantial cost savings in relation to storage, selling, general, and administration expenses. Reportedly, Costco has been able to prices its products at 14-15% markup, in comparison to over 20% markup by its competitors, above the costs. This, in turn, enables Costco to offer its merchandise comparatively at a much lower prices than its competitors.

04.00: Value Propositions

Costco, because of its unique business model, is perceived to possess strong value propositions. The value-added goods and services that it offers to its members hinges on four value elements. These are:

- Low Prices: As Costco operates a unique business model that focuses on offering wholesale prices for merchandise whereby members will almost always get lower prices when shopping at its warehouses. This makes Costco more attractive than conventional grocery stores and supermarkets;
- Zero Risk Membership: Another strong aspect of its value proposition is its risk-free membership offering. The fact that consumers are given the option of claiming a refund if unsatisfied with Costco's service is a major selling point. In addition to this, members can also turn in several goods in-store and request a refund, further contributing to higher customer confidence in the brand.
- Membership Reward Program: Costco's Executive Memberships reward scheme which allows customers to claim up to $750 annually in reward points has also been proven to have a strong positive effect on the brand's exposure.
- International Exposure: Costco's global reach and growing online sales channel means that members can always readily access the goods and services offered by the merchant.

05.00: Key Financials

Tabulated below are the key financials of Costco for the last six years. These figures have been taken from the annual reports of the company.

Key Financials of Costco

Serial	Particulars	52 Weeks Ended					
		28.08.2016	03.09.2017	02.09.2018	01.09.2019	30.08.2020	29.08.2021
I	**Financials in USD Millions**						
A	Revenue						

1	Net Sales	116073	126172	138434	149351	163220	192052
2	Membership Fees	2646	2853	3142	3352	3541	3877
3	Total	118719	129025	141576	152703	166761	195929
B	Operating Expenses						
1	Merchandise Cost	102901	111882	123152	132886	144939	170684
2	Selling, General & Administration	12068	12950	13876	14994	16332	18461
3	Preopening	78	82	68	86	55	76
4	Total	115047	124914	137096	147966	161326	189221
C	Operating Income	3672	4111	4480	4737	5435	6708
II	**Key Percentages**						
1	Operating Income to Revenue	3.09	3.19	3.16	3.10	3.26	3.42
2	Merchandise Cost to Net Sales	88.65	88.67	88.96	88.98	88.80	88.87
3	Selling, General & Administration to Net Sales	10.40	10.26	10.02	10.04	10.01	9.61
4	Membership Fees to Operating Income	72.06	69.40	70.13	70.76	65.15	57.80

The financials and the key percentages are self-explanatory. The Revenue of the company has gone up from USD1,18,719 million in 2016 to USD 1,95,929 millions by 2021; Percentage of Operating Income to Revenue reflects a consistence trend of over three percent; Percentage of Merchandise Cost to Net Sales has always been less than 89% revealing the fact that Costco pursues the policy of minimum markup pricing; Percentage of Selling, General & Administration to Net Sales hover around 10% highlighting the operating efficiencies; and the Percentage of Membership Fees to Operating Income comprises substantial quantum of operating income signifying the competitive advantage of membership bonding.

06.00: SWOT Analysis

In terms of SWOT (Strengths Weaknesses Opportunities and Threats) the posture of Costco may be summed up as follows:

06.01: Strengths

- Pricing: Costco offers to its member customers the lowest possible prices for all of the goods and services.

- Operating Structure: The business model allows for a high sales volume that is equally matched with rapid inventory turnover. As a result, Costco is almost always guaranteed large profits, even though they sell at lower prices;
- Operating Efficiency: The business model the company runs on affords it a higher degree of operating efficiency. Costco's higher operating efficiency is accomplished through variable cost minimization.

06.02: Weaknesses

- Limited Product Mix: Costco has a limited product mix compared to the wider and more extensive selection available from competitors like Walmart. This weakness prevents maximization of revenues from consumers who might not find what they are looking for at Costco warehouses/stores.
- Exclusivity to Members: Costco's business model creates exclusivity to members and prevents other shoppers from easily purchasing at its warehouses.
- Low profit margins: Because of Costco's generic strategy, the company has the weakness of low profit margins, which leaves little room for price adjustments.

06.03: Opportunities

- Expansion: There are readily available markets in developing Asian countries just waiting to be leveraged. Costco's online platform still has room for growth, and its services and products can be further extended into regions where it doesn't exist currently;
- Diversification: The company can diversify and expand the list of products and services it currently offers. This will increase its appeal to potential consumers who are in search of more variety, boost revenue, and put it on a level footing with some of its competition as well.

06.04: Threats

- Competition with Retail Stores: Costco Wholesale Corporation faces tough competition with retail firms like Walmart, especially Walmart's Sam's Club.
- Online Competition: In the online market, many small and medium-sized firms are now selling goods for low prices, thereby competing against Costco.

06.05: Assimilation

As a business, Costco Wholesale Corporation is highly viable, effective, and efficient. It remains one of the world's leading minimal expense pioneers, and everything — from its membership fees to bulk purchases — ensures a steady and growing stream of income for the brand. However, the threats against Costco are market-based. In the ultimate, the company should continue to focus on its on positive inventions and relegate the weaknesses and threats.

07.00: Quick Take

Costco's operating philosophy has been simple. Keep costs down and pass the savings on to the members thus providing Maximum Life Time Customer Value!

GROUP: 3, PART: 16

CA Vikash Mundra
He can be reached at:
vikash@taxpointindia.com

DIRECT TAX
LAWS AND INTERNATIONAL TAXATION - (DTI)

Your Preparation Quick

Syllabus Structure
A Advanced Direct Tax Laws **50%**
B International Taxation **30%**
C Case Study Analysis **20%**

Learning Objectives:

- To develop basic idea about the problem of International double taxation
- To get acquainted with the methods of reliefs
- To have acquaintance with the basic provisions of the provisions of the Indian Income-tax Act regarding reliefs for double taxation.

Equalisation Levy

ith the expansion of information and communication technology, the supply and procurement of digital goods and services have undergone exponential expansion everywhere, including India. The digital economy is growing at 10% per year, significantly faster than the global economy as a whole.

Currently in the digital domain, business may be conducted without regard to national boundaries and may dissolve the link between an income-producing activity and a specific location. From a certain perspective, business in digital domain doesn't seem to occur in any physical location but instead takes place in the nebulous world of "cyberspace." Persons carrying business in digital domain could be located anywhere in the world. Entrepreneurs across the world have been quick to evolve their business to take advantage of these changes. It has also made it possible for the businesses to conduct themselves in ways that did not exist earlier, and given rise to new business models that rely more on digital and telecommunication network, do not require physical presence, and derives substantial value from data collected and transmitted from such networks.

These new business models have created new tax challenges. The typical direct tax issues relating to e-commerce are the difficulties of characterizing the nature of payment and establishing a nexus or link between a taxable transaction, activity and a taxing jurisdiction, the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes. The digital business fundamentally challenges physical presence-based permanent establishment rules. If permanent establishment (PE) principles are to remain effective in the new economy, the fundamental PE components developed for the old economy i.e. place of business, location, and permanency must be reconciled with the new digital reality.

The Organization for Economic Cooperation and Development (OECD) has recommended, in Base Erosion and Profit Shifting (BEPS) project under Action Plan 1, several options to tackle the direct tax challenges which include modifying the existing Permanent Establishment (PE) rule to include that where an enterprise engaged in fully de-materialized digital activities would constitute a PE if it maintained a significant digital presence in another country's economy. It further recommended a virtual fixed place of business PE in the concept of PE i,e creation of a PE when the enterprise maintains a website on a server of another enterprise located in a jurisdiction and carries on business through that website. It also recommended to impose of a final withholding tax on certain payments for digital goods or services provided by a foreign e-commerce provider or imposition of a equalisation levy on consideration for certain digital transactions received by a non-resident from a resident or from a non-resident having permanent establishment in other contracting state.

Considering the potential of new digital economy and the rapidly evolving nature of business operations it is found essential to address the challenges in terms of taxation of such digital transactions as mentioned above. In order to address these challenges, Chapter VIII of the Finance Act, 2016[1], titled "Equalisation Levy", provides for an equalisation levy of 6 % of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment ('PE') in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India. Different provisions thereof are discussed below:

A. Charge of equilisation levy on specified services [Sec. 165]

Equalisation levy shall be payable @ 6% of the consideration for any specified service received or receivable by a person, being a non-resident from:

i. a person resident in India and carrying on business or profession; or
ii. a non-resident having a permanent establishment in India.

- Specified service means
  - a) **online advertisement**,
  - b) any provision for digital advertising space or any other facility or service for the purpose of online advertisement and
  - c) any other notified service – Sec. 164(i)
- Online means a facility or service or right or benefit or access that is obtained through the internet or any other form of digital or telecommunication network – Sec. 164(f)

Taxpoint

These provisions extend to the whole of India.

Exceptions

The equalisation levy shall not be charged, where:

[1] The equalization levy would come into effect from 01-06-2016 [Notification dated 27-05-2016]

a) the consideration received or receivable for specified services shall not include the consideration, which are taxable as royalty or fees for technical services in India, read with the agreement notified u/s 90 or 90A of the Income-Tax Act.
b) the non-resident providing the specified service has a permanent establishment in India and the specified service is effectively connected with such permanent establishment;
c) the aggregate amount of consideration for specified service received or receivable in a previous year from resident in India or from a non-resident having a permanent establishment in India, does not exceed ₹ 1,00,000; or
d) the payment for the specified service by the person resident in India, or the permanent establishment in India is not for the purposes of carrying out business or profession.

Collection and recovery of equalisation levy on specified services [Sec. 166]

Who is liable to deduct equalisation levy:

Every person, being a resident and carrying on business or profession or a non-resident having a permanent establishment in India (hereafter in this Chapter referred to as assessee) shall deduct the equalisation levy u/s 165 from the amount paid or payable to a non-resident in respect of the specified service

Rate of levy: 6%

Threshold limit: Such deduction shall be made if the aggregate amount of consideration for specified service in a previous year exceeds ₹ 1,00,000.

Time limit for depositing the levy to the credit of the Central Government: The equalisation levy so deducted during any calendar month shall be paid by every assessee to the credit of the Central Government by the 7th day of the month immediately following the said calendar month.

Consequences of failure to deduct equalisation levy: Any assessee who fails to deduct the levy shall be (even though not deducted) liable to pay the levy to the credit of the Central Government in accordance with the aforesaid provisions

B. Charge of equalisation levy on e-commerce supply of services [Sec. 165A]

Equalisation levy shall be charged @ 2% of the amount of consideration received or receivable by an e-commerce operator from e-commerce supply or services made or provided or facilitated by it—

a. to a person resident in India; or

b. to a non-resident in the specified circumstances; or

- "Specified circumstances" mean—
    i. sale of advertisement, which targets a customer, who is resident in India or a customer who accesses the advertisement though internet protocol address located in India; and
    ii. sale of data, collected from a person who is resident in India or from a person who uses internet protocol address located in India

c. to a person who buys such goods or services or both using internet protocol address located in India.

Taxpoint

☸ *Consideration received or receivable* from e-commerce supply or services shall include:

i. consideration for sale of goods irrespective of whether the e-commerce operator owns the goods, so, however, that it shall not include consideration for sale of such goods which are owned by a person resident in India or by a permanent establishment in India of a person non-resident in India, if sale of such goods is effectively connected with such permanent establishment.

ii. consideration for provision of services irrespective of whether service is provided or facilitated by the e-commerce operator, so, however, that it shall not include consideration for provision of services which are provided by a person resident in India or by permanent establishment in India of a person non-resident in India, if provision of such services is effectively connected with such permanent establishment.

☸ *e-commerce operator* means a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both;

☸ *e-commerce supply or services* means:

i. online sale of goods owned by the e-commerce operator; or
ii. online provision of services provided by the e-commerce operator; or
iii. online sale of goods or provision of services or both, facilitated by the e-commerce operator; or
iv. any combination of activities listed in clause (i), (ii) or clause (iii);

☛ *Online sale of goods* and *online provision of services* shall include one or more of the following online activities:

a. acceptance of offer for sale; or
b. placing of purchase order; or

c. acceptance of the purchase order; or
d. payment of consideration; or
e. supply of goods or provision of services, partly or wholly

Exceptions

The equalisation levy shall not be charged:

a. the consideration received or receivable for e-commerce supply or services shall not include the consideration, which are taxable as royalty or fees for technical services in India, read with the agreement notified u/s 90 or 90A of the Income-Tax Act.
b. where the e-commerce operator making or providing or facilitating e-commerce supply or services has a permanent establishment in India and such e-commerce supply or services is effectively connected with such permanent establishment;
c. where the equalisation levy is leviable u/s 165 [i.e. A supra]; or
d. sales, turnover or gross receipts, as the case may be, of the e-commerce operator from the e-commerce supply or services made or provided or facilitated is less than ₹ 2 crore during the previous year.

Collection and recovery of equalisation levy on e-commerce supply or services [Sec. 166A]

The equalisation levy u/s 165A shall be paid by every e-commerce operator to the credit of the Central Government quarterly as per following time schedule:

Date of ending of the quarter of financial	Due date of payment
30th June	7th July
30th September	7th October
31st December	7th January
31st March	31st March

Furnishing of Statement [Sec. 167]

- Every assessee or ecommerce operator shall, within 30th June immediately following the financial year, prepare and deliver to the Assessing Officer (or to any other authority or agency authorised by the Board), a statement in Form 1, verified in such manner and setting forth such particulars as may be prescribed, in respect of all specified services or e-commerce supply or services during such financial year.

- *Revised Statement*: An assessee or ecommerce operator who has not furnished the statement within aforesaid time or having furnished such statement, notices any omission or wrong particular therein, may furnish a statement or a revised statement, as the case may be, at any time before the expiry of 2 years from the end of the financial year in which the specified services or e-commerce supply or services was provided or facilitated.
- *Notice by the Assessing Officer*: Where any assessee or ecommerce operator fails to furnish the statement within 30th June immediately following the financial year, the Assessing Officer may serve a notice upon such assessee or ecommerce operator requiring him to furnish the statement in the prescribed form, verified in the prescribed manner and setting forth such particulars, within 30 days from the date of service of the notice.

Processing of Statement [Sec. 168]

Statement furnished u/s 167 shall be processed in the following manner:

a. the equalisation levy shall be computed after making the adjustment for any arithmetical error in the statement;

b. the interest, if any, shall be computed on the basis of sum deductible or payable as computed in the statement;

c. the sum payable by, or the amount of refund due to, the assessee shall be determined after adjustment of the interest against any amount paid u/s 166 or 166A or 170 and any amount paid otherwise by way of tax or interest;

d. an intimation shall be prepared or generated and sent to the assessee or ecommerce operator specifying the sum determined to be payable by, or the amount of refund due to, him; and

e. the amount of refund due to the assessee or ecommerce operator shall be granted to him.

Time limit

No intimation shall be **sent** after the expiry of 1 year from the end of the financial year in which the statement or revised statement is furnished.

Taxpoint

For the purposes of processing of statements, the Board may make a scheme for centralised processing of such statements to expeditiously determine the tax payable by, or the refund due to, the assessee or ecommerce operator.

Rectification of mistake [Sec. 169]

- With a view to rectifying any mistake apparent from the record, the Assessing Officer may amend any intimation issued u/s 168, within **1 year** from the end of the financial year in which the intimation sought to be amended was issued.
- The Assessing Officer may make an amendment to any intimation either *suo motu* or on any mistake brought to his notice by the assessee or ecommerce operator.
- An amendment to any intimation, which has the effect of increasing the liability of the assessee or ecommerce operator or reducing a refund, shall not be made unless the Assessing Officer has given notice to the assessee of his intention so to do and has given the assessee or ecommerce operator a reasonable opportunity of being heard.
- Where any such amendment to any intimation has the effect of enhancing the sum payable or reducing the refund already made, the Assessing Officer shall make an order specifying the sum payable by the assessee or ecommerce operator and the provisions of this Chapter shall apply accordingly.

Interest on Delayed payment of equalisation levy [Sec. 170]

Every assessee or ecommerce operator, who fails to credit adequate equalisation levy to the account of the Central Government within specified period, shall pay simple interest @ 1% of such levy for every month or part of a month by which such crediting of the tax is delayed.

Penalty

Penalties provisions are as under:

Sec.	Nature of default	Amount of Penalty
171(a)	Fails to deduct the equalisation levy u/s 165	Equal to the amount of equalisation levy
171(aa)	Fails to pay the equalisation levy u/s 165A	
171(b)	Fails to pay levy, after deduction, to the credit of the Central Government	₹ 100 for every day during which the failure continues subject to maximum of amount failed

		to pay
172	Failure to furnish statement as required u/s 172	₹ 100 for every day during which the failure continues

- No penalty shall be imposable:
  1. If the assessee proves to the satisfaction of the Assessing Officer that there was reasonable cause for the said failure.
  2. Without giving reasonable opportunity of being heard to the assessee or ecommerce operator [Sec. 173].
- An assessee or ecommerce operator aggrieved by an order imposing penalty may appeal to the Commissioner of Income-tax (Appeals) within 30 days from the date of receipt of the order in Form 3. It shall be accompanied with fees of ₹ 1,000/-. The provisions relating to appeals are in line with that of the Income-tax Act, 1961. [Sec. 174]
- Similarly, appeals can be filed before the ITAT against the order of the Commissioner (Appeals) in Form 4 within 60 days from the date on which the order sought to be appealed against is received by the assessee (or ecommerce operator) or by the Commissioner. In case appeal before the ITAT is filed by the assessee, it should be accompanied with fees of ₹ 1,000/- [Sec. 175]

Punishment for false statement [Sec. 176]

If a person makes a false statement in any verification or delivers an account or statement, which is false, and which he either knows or believes to be false, or does not believe to be true, he shall be punishable with imprisonment for a term which may extend to 3 years and with fine.

Taxpoint:

- An offence punishable above shall be deemed to be non-cognizable.
- No prosecution shall be instituted against any person for any offence except with the previous sanction of the Chief Commissioner of Income-tax [Sec. 177].

GROUP: 4, PART: 17

CORPORATE

FINANCIAL REPORTING - (CFR)

Dr. Ananda Mohan Pal
Professor,
Department of Business Management,
The University of Calcutta
He can be reached at:
apal59@gmail.com

Your Preparation Quick

Syllabus Structure

A GAAP and Accounting Standards **20%**
B Accounting if Business Comminations & Restructuring **20%**
C Consolidated Financial Statements **20%**
D Developments in Financial Reporting **25%**
E Government Accounting in India **15%**

Learning Objectives:

After studying the present section of Corporate Financial Reporting you will be able to:

- Learn how to highlight the achievements of a company to its investors, creditors, bankers, public, employees, regulatory bodies and Government on a periodic basis
- To convey future based strategic roadmap for the company.

MCQ on Intangible Assets and Impairment of Assets

1. **Z Ltd. produced a data analysis software at a cost of Rs.25,00,000 and declared it as open for anybody to download it for free from internet and to change it to suite one's requirement. Z Ltd. will also get economic benefits from the use of the software**
   a) Intangible asset is recognized at cost Rs. 25,00,000
   b) Intangible asset is not recognized as the entity does not have control over the asset as it is 'open' to download and change
   c) Intangible asset is not recognized since its economic benefits cannot be reliably measured
   d) None of the above

2. **On 01.04.2018 M Ltd. holds a license of the carrying value of Rs.2,000 Lakhs, having useful life of 10 years remaining, with residual value NIL. It holds a trademark whose carrying value is Rs. 3,000 Lakhs with indefinite useful life on 31.03.2019. The recoverable amount of the License is Rs. 1,860 Lakhs and of the Trade Mark is Rs. 2,800 Lakhs. On 31.03.2019:**
   a) Impairment was on License Rs.140 Lakhs and on Trademark Rs.300 Lakhs
   b) Impairment loss on License and on Trademark are NIL
   c) Amortization of License Rs.200 Lakhs and Impairment loss on Trademark Rs.200 Lakhs
   d) Amortization of license is Rs.200 Lakhs and of Trademark Rs.200 Lakhs

3. **X Ltd. purchased a group of assets from B Ltd. at a total cost of Rs.700 Lakhs consisting of License Rs.120 Lakhs, Machinery Rs.400 Lakhs and a Software Rs.100 Lakhs as on 31.03.2018. The License and Software have remaining useful life of 12 years and 10 years respectively with no residual value.**

   On 31.03.2019 the recoverable amount of the assets, considered as a Cash Generating Unit is Rs.580 Lakhs. Annual depreciation on machinery is Rs.60 Lakhs.

   Which of the following statements is false?
   a) Goodwill purchased is recognized at Rs.80 Lakhs on 31.03.2018
   b) Impairment loss is recognized for goodwill on 31.03.2019 at Rs. 40 Lakhs
   c) Amortization of License Rs.10 Lakhs and Trademark Rs.10 Lakhs are chargeable to P & L A/c for

2018-19

d) Impairment loss of License Rs. 20 Lakhs and of Trademark Rs. 20 Lakhs on 31.03.2019

4. **K Ltd. Employed a team of experts to improve the design of its machinery. The experts after a yearlong research activity put forward two alternative designs - I and II and incurred expenditure of Rs. 24,00,000 up to that stage. Management approved design II and the team spent further Rs. 38,00,000 for operating design II on trial basis. The new design will improve the quality of the products and economic benefits will flow to the company.**

   a) No intangible asset would be recognized
   b) Rs. 62,00,000 should be recognized as intangible asset
   c) Rs. 24,00,000 should be recognized as intangible asset and Rs.38,00,000 as expense
   d) Rs. 24,00,000 should be recognized as expense and Rs.38,00,000 as intangible asset

5. **On review of cost of sales of a company it was found that it included the following costs for developing and marketing a new variety of shampoo: (Rs. in Lakhs)**

Advertisement	150
Development costs	480

The fair value of the brand based on probable economic benefits in future has been estimated at Rs.800 Lakhs. The life of the brand is expected to be 10 years. The company applies Ind AS 38 to recognize maximum amount of intangible asset.

(i) Intangible asset to be recognized initially and amortization annual amount are:

   a) Rs.480 Lakhs and Rs.48 Lakhs
   b) Rs.630 Lakhs and Rs.63 Lakhs
   c) Rs.800 Lakhs and Rs.80 Lakhs
   d) Rs.150 Lakhs and Rs.15 Lakhs

(ii) The accounting adjustment to be made is -

   a) Credit cost of sale by Rs.150 Lakhs and debit intangible asset by Rs. 480 Lakhs
   b) Credit cost of sale by Rs.480 Lakhs and debit intangible asset by Rs. 480 Lakhs
   c) Credit cost of sale by Rs.630 Lakhs and debit intangible asset by Rs. 630 Lakhs
   d) None of the above

6. **A project for development of a new drug was started on 01.04.2016. After 2 years of research activities on 01.04.2018 the project was assessed as being technically feasible and commercially viable after another year on 31.03.2019 development the new drug was complete and commercial production started from 01.04.2019 ensuring satisfactory future economic benefits for 10 years.**

Expenditure incurred on the project up to 31.03.2018 was Rs. 26 Lakhs in each year and in 2018-19 Rs. 40 lakhs. What amount should be recognized in financial statements for the years ended on 31.03.2017, 31.03.2018, 31.03.2019 and 31.03.2020?

(i) In statement of P & L

a) Expenses for 2016-17: Rs. 26 Lakhs and expenses for 2017-18: Rs. 26 Lakhs

b) Amortization for 2017-18: Rs. 2.6 Lakhs

   For 2018-19: Rs. 5.2 Lakhs

   For 2019-20: Rs. 9.2 Lakhs

c) Expenses for 2018-19: Rs. 40 Lakhs

d) None of the above

(ii) In balance sheet -

a) Intangible asset on 31.03.2019: Rs. 40 Lakhs

b) Intangible asset on 31.03.2018: Rs. 49.6 Lakhs

c) Intangible asset on 31.03.2020: Rs. 82.8 Lakhs

d) None of the above

(iii) Which of the following is not true?

a) Research expenditure for 2 years up to 31.03.2018 are recognized in P & L A/c as expense

b) Development expenditure in 2018-19 should be recognized as intangible asset

c) Annual amortization starting from 2019-20 is Rs. 4 Lakhs to be charged to P & L A/c

d) The carrying amount of intangible asset on 31.03.2020 is Rs. (40 – 8) Lakhs = 32

Hints:

Year ending on	P & L A/c	Intangible asset
31.03.2017	Expense: Rs. 26 Lakhs	NIL
31.03.2018	Expense: Rs. 26 Lakhs	NIL
31.03.2019	—	Rs. 40 Lakhs
31.03.2020	Amortization: Rs. 4 Lakhs	Rs. 36 Lakhs

Answer Keys:

1	2	3	4	5		6		
b	c	d	d	(i) a	(ii) b	(i) a	(ii) a	(iii) d

GROUP: 4, PART: 18

INDIRECT TAX

LAWS & PRACTICE - (ITP)

CMA Rana Ghosh
Chief Executive Officer,
Institution of Estate Managers & Appraisers
He can be reached at:
ranaham@rediffmail.com

Your Preparation Quick

Syllabus Structure
A Advanced Indirect Tax and Practice **80%**
B Tax Practice and Procedures **20%**

Learning Objectives:

Through the following MCQ, students can refresh themselves about

- Residual Methods
- Self assessed Bill of Entry
- Responsibility of Port Trust Authority
- Import order and Refund order
- Smuggled Goods
- Redemption Fine
- Output services & Pilferage

Indirect Tax

Choose the correct option from the followings –

1. Residual Method often called

(a)Transaction Value Method

(b) Fair Value Method

(c)Best Judgment Method

(d) Protective Method

2. Bill of Entry for imported goods to be submitted for home consumption in

(a) Yellow colour

(b) White colour

(c) Green colour

(d) Pink colour

3. In case of self-assessed Bill of Entry importer shall have to make payment of Customs duty after the return of Bill of entry

(a) On the same day

(b) On the second day

(c) On the third day

(d) On the fourth day

4. If the assessment is delayed for imported goods, then those goods can be stored in public warehouse without executing bond is called as

(a) Deemed warehousing
(b) Warehousing without warehousing
(c) Special warehousing
(d) Public warehousing

5. Under section 16 of the IGST Act exports would be considered as

(a) Exempted supply
(b) Deemed supply
(c) Zero rated supply
(d) Ordinary supply

6. Which of the following is not the responsibility of Port Trust Authorities as Custodian

(a) Keep proper record of goods received from the carriers
(b) Sending a copy of the same to the customs authorities
(c) Liable for payment of duty in respect of pilfered goods
(d) Removal of goods from the customs area with specific permission of the Customs Authorities

7. As per Sect 64 of the Customs Act,1962 after warehousing the goods which one will not be considered as owner's right to deal with the warehoused goods

(a) Inspect the goods
(b) Sort the goods
(c) Show the goods for sale
(d) May take physical control

8. In which of the following import, import duty will not be levied

(a) Cartridge of firearms 60 nos
(b) Gold and silver bar
(c) Alcoholic liquor of two liter
(d) Flat Panel LED television

9. Which one of the following will not be considered as relevant date for filing of refund claim

(a) Date of inspection of goods
(b) Let export order issued
(c) Date of abandonment
(d) Date of destruction of goods as the case may be

10. As per section 17(5) of Customs Act,1962 where the importer or exporter does not accept the reassessment in writing, the proper officer shall pass an order within 15 days from the date of assessment of "Bill of Entry" known as

(a) Provisional Order
(b) Commissioner's Order
(c) Speaking Order
(d) Protest Order

11. Goods imported from a foreign country into India, unable to clear from the port within 3 working days due to delay is from Customs Authorities, then the authorities will issue for bona fide import

(a) Clearance Certificate
(b) Delayed Certificate
(c) Facility Certificate
(d) Detention certificate

12. In case of imported goods are sent to shore in a small cargo due to inadequate depth of sea or vessel may not find the time in having berth in port should accompany

(a) Boat Note
(b) Small Cargo Certificate
(c) Special Customs Note
(d) Port Advice

13. As per Section 110 of the Customs Act, 1962 to take possession of the property contrary to the wishes of the owner of the goods in pursuance of a demand under legal right means

(a) Detention
(b) Seizure
(c) Custody
(d) Confiscation

14. As per Section 151 of the Customs Act, 1962 which of the following officers of other department are not empowered to assist officers of the Customs

(a) Officers of the Central excise department
(b) Officers of the Army
(c) Officers of the Navy
(d) Officers of the Police

15. If the smuggled gold biscuits converted into jewellery then

(a) A special rate of customs duty will be levied

(b) To see whether tax or other dues payable as per other law in force

(c) Commissioner of customs will decide the confiscation for conversion into different forms

(d) The entire value of jewellery is liable for confiscation

16. As per section 125 of the Customs Act, 1962 the term 'Redemption Fine' means

(a) Right to auction of the confiscated goods

(b) Option to pay fine in lieu of confiscation

(c) Goods first confiscated and then pay duty on that

(d) Penalty and fine imposed on confiscated goods after adjudication by assistant Commissioner

17. As per the Customs Act which one of the following will not be called 'Vexation Action' of department officer

(a) An officer of customs facilitated to do fraudulent export

(b) Search of person without reason to believe that they are guilty

(c) Arrest of person without reason to believe that they are guilty

(d) Impose penalty without informing Commissioner / additional Commissioner of Customs

18. As per Customs (Import Of Goods At Concessional Rate Of Duty), Rules 2017; Output Service' means

(a) Supply of service with the use of the imported goods

(b) Service provided by Customs Department related for documentation

(c) Facilities like providing of customs godown, transportation etc for imported goods

(d) Supply of service related to the fixation of import duties and release of imported goods

19. Which of the following statement is not applicable for the valuation based on transaction value as per Customs Act, 1962

(a) Price at which such or like goods are ordinarily sold or offered for sale

(b) When Seller and buyer have some interest in the business of each other

(c) Price is the sole consideration for sale

(d) in the course of international Trade

20. Which of the following circumstances should not exist in order to claim pilferage as per Customs Act –

(a) There should be evidence of tampering with the packages

(b) There should be blank space for the missing articles in the packages

(c) The missing articles should be part articles

(d) The missing articles should be unit articles

ANSWERS

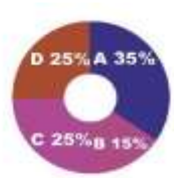
1	c	6	c	11	d	16	b
2	**b**	**7**	**d**	**12**	**a**	**17**	**d**
3	**a**	**8**	**c**	**13**	**b**	**18**	**a**
4	**b**	**9**	**a**	**14**	**b**	**19**	**b**
5	**c**	**10**	**c**	**15**	**d**	**20**	**c**

GROUP: 4, PART: 19,

CMA S S Sonthalia
Practicing Cost Accountant
He can be reached at:
sonthalia_ss@yahoo.co.in

COST & MANAGEMENT AUDIT – (CMAD)

Your Preparation Quick



Syllabus Structure

A Cost Audit **35%**
B Management Audit **15%**
C Internal Audit, Operational Audit and other related issues **25%**
D Case Study on Performance Analysis **25%**

Learning Objectives:

- To verify the correctness of the cost accounting records.
- To find out whether the principles of cost accountancy have been fully and correctly applied in maintaining cost records.
- To search for the deficiencies in the cost record system of the company.
- To attain efficiency in cost accounting systems and procedures.

Understanding Administrative Overheads (CAS – 11)

Introduction

As an organisation prepares for its cycle of production, it has to establish a budget upon which its entire plan of action is depended upon. The organisation has to determine the Cost of Production of its product / service. To determine such cost, one of a cost head namely 'Administrative Overheads' has to be considered. For proper budget based management, the determination of Administrative expenses has to be diligently calculated as any miscalculation has a possibility in adverse effect in the budget analysis.

Moreover, during the determination of Transfer Price for interdepartmental transfer of product / service, the recovery of proportionate administrative cost is important. Even though the overall profitability of an organisation is not affected by the transfer price, the performance of each department is consequential to the ascertainment of such costs. The Cost Accounting Standard 11 directs the transfer of products / service to have a portion of administrative cost related to the product (The determination of such costs have been discussed in following paragraphs.).

For charities and other non-profit organizations, administrative costs are often defined differently from the way for-profit making businesses define them. In many cases, any money that is brought into the charity organization and spent by the organization is counted as an administrative cost. Therefore, all of the costs of running the organization, such as for salaries, rent and utilities, or any expenses would be called administrative expenses.

As the administrative overheads may be eliminated without having to sacrifice any quantity of product being sold or produced, they are typically the first expenses looked into for budget cuts. There is strong motivation from management to maintain low administrative expenses relative to other expenses as an organization may utilize leverage more effectively with lower administrative costs. An entity may work out the sales-to-administrative ratio to gauge the portion of sales revenue attributable to covering administrative costs.

Determination of Administrative Cost.

With reference to Cost Accounting Standard (CAS) 11, Administrative overheads refer to the costs of operating a business that are not directly attributable to the production of goods or services. Administrative Overheads are related to the organization as a whole as opposed to the individual departments.

Administrative Overheads are necessary costs that are associated with the management, administrative, clerical, and general functions within an organization. These are the expenses which are incurred in controlling and directing an organization but cannot be directly identified with the marketing, financing or production operations. The salaries of executives cost of services (such as accounting, contracting, and industrial relations) are the examples of administrative overheads. Administrative overheads are non-technical charges necessary for the basic operation of an entity. These expenses are vital for a company's success as they occur to increase the efficiency of an organization

Some of the particular cases that are described in CAS 11 that helps recognising the Administrative Costs are:

- Remuneration paid to nonexecutive directors computed as per CAS 7 (Employee Cost) - should be treated as Administrative Overheads. The costs for internet landline and mobile telephone services are also included in these expenses.
- Utilities consumed by administrative cost centres are to be collected and measured in accordance with principles laid down by CAS-8.
- Repair and maintenance cost should be measured in accordance with principles laid down by CAS - 12.
- Sometimes referred to as general expenses or operating expenses, administrative expenses involve any costs that offer a wide benefit to the organization. Their benefits cross departmental lines and make it possible for many functions to take place. Any expense that is limited to a particular division or department of the company and which offers little or no direct benefit to other areas of the organization, is not considered an administrative overhead. For e.g. Accounting or legal, can be considered administrative because they benefit the entire organization.

The following are the points that are similar in both Cost Accounting Standards and CRA-1. The company under audit is bound to comply the CRA – 1 as per Companies Act 2013, whereas the Cost Auditor is also bound to ensure compliance of Cost Accounting Standards.

1. In case of Assignment of administrative overheads to the cost objects, the same shall be based on either of the following two principles;

i) Cause and Effect - Cause is the process or operation or activity and effect is the incurrence of cost.

ii) Benefits received – Expenses are to be apportioned to the various cost objects in proportion to the benefits received by them or any other equitable relationship.

2. For an asset used for administration overheads (as defined under standard), in case of leased assets,
   - if the lease is an operating lease, the entire rentals shall be included in the administrative overheads.
   - if the lease is a financial lease, the finance cost portion shall be segregated and treated as part of finance costs and the balance cost related to the period shall be taken as Administrative Overheads.

3. 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.

4. Administrative expenses shall not include any abnormal administrative cost. For e.g. Administrative cost resulting from natural calamity (flood, earthquake, and the like), Sudden breakdown/ loss due to major fire accident

Statutory Requirements and Disclosures.

As per the Companies (Cost Records and Audit) Rules, 2014 – Part B/C 2- Abridged Cost Statements of the Annexure to the Cost Audit Report provides for the amount of expenditure for Administrative Overheads. Those attributed costs are to be segregated and disclosed under those particular head. That disclosure is to satisfy the requirements of CAS 11.

The Company under audit is required to keep all the records as per CRA – 1 (8) that denotes the Administrative Overheads. Following are some of the important rules.

a) Any change in the cost accounting principles applied for the measurement of the administrative Expenses shall be made only if it is required by law or a change would result in a more appropriate preparation or presentation of cost statements of an organisation.

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

One of the major factor for classification of Administration Overheads is the identification of expenses in the Corporate Administration and Plant Administration. The both expenses are to be properly disclosed separately in the cost statement in Annexure to the Cost Audit Report. The classification is to be done by understanding the nature and purpose of the expenses.

The Plant Administration is dedicated to the operation of plant thus is a part of Production Cost. The expenses incurred in the Plant Administration is to be grouped under 'Other Production overheads' rather than 'Administrative Overheads'. Similarly the resources utilised for the Plant administration is to be taken under the 'Other Production Overheads which is a component of Cost of Production/Service.

On the other hand, the Corporate Administration has the function of policy making and mainly carries out activities of fulfilment of the vision of the company. It serves the whole of the company rather than the production process. These type of expenditures are to be shown under 'Administrative Overheads' in cost statements and shall not form part of Cost of Production/Service.

It is to be noted that the placement of the departments is not consequential to the classification of costs as Administrative or otherwise. The importance is to be given as to the purpose / function of the department.

Following are some examples of Corporate and Plant Administration for better understanding.

A. Plant Administration (Other Production Overheads) : Depreciation of assets used by the department, Utilities used by the department, Repairs and Maintenance incurred by the department, Stores and spares used by the department, Stationaries consumed by the department, General Manager of the Plant, Human Resource of the Plant, Finance Manager of Plant, Stock Audit Fees, Production certification fees.

B. Corporate Administration (Administrative Overheads) : Depreciation of assets used by the department, Utilities used by the department, Repairs and Maintenance incurred by the department, Stores and spares used by the department, Stationaries consumed by the department, Finance Management Company as a Whole, Managing Director, CEO, Company's Secretary, Non-executive directors, Financial and Cost Audit Fees.

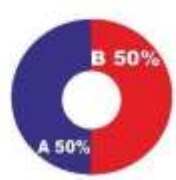
GROUP: 4, PART: 20,

STRATEGIC

PERFORMANCE MANAGEMENT AND BUSINESS VALUATION – (SPBV)

Dr. Ashish Kumar Sana
Professor,
Dept. of Commerce,
He can be reached at:
cu.ashis@gmail.com

Your Preparation Quick



Syllabus Structure
A Strategic Performance Management **50%**
B Business Valuation **50%**

Learning Objectives:

After studying this section on Strategic Performance Management and Business Valuation, you will be able to:

- understand H Model and Three Stage Growth Model of equity share
- solve the problems on H Model and Three Stage Growth Model of equity share

Valuation of Bonds And Mergers and Acquisitions

A bond/debenture is a long-term debt instrument used by the government/government agency (ies) and business enterprises to raise a large sum of money. Most bonds, particularly corporate bonds (i) pay interest half-yearly (semi-annually) at a stated coupon interest rate, (ii) have an initial maturity of 10-years and (iii) have a par/face value of ₹1,000 that must be repaid at maturity.

- Par value is value on the face of the bond.
- Coupon rate is the specified interest rate available on a security.
- Maturity period is the number of years after which the par/ specified value is payable to the bondholders.

Basic Bond Valuation

The value of a bond is the present value of the contractual payments its issuer (corporate) is obliged to make from the beginning till maturity. The appropriate discount rate would be the required return commensurate with risk and the prevailing interest rate.

$$B = I\left[\sum_{t=1}^{n} \frac{1}{(1+k_d)^t}\right] + M \times \left[\frac{1}{(1+k_d)^n}\right]$$
$$= I \times (PVIFA_{k_d,n}) + M \times (PVIF_{k_d,n})$$

where

B = value of the bond at t = 0

I = annual interest paid

n = number of years to maturity (term of the bond)

M = par/maturity value

k_d = required return on the bond

Yield to Maturity (YTM)

Yield to maturity (YTM) is the rate of return an investor earns on a bond held till maturity. The YTM on a bond whose current price equals its par/face value (i.e. purchase price = maturity value) would always be equal to its coupon interest rate.

Example 1

The bonds of the P Ltd. are currently selling for ₹10,800. Assuming (i) coupon rate of interest, 10 per cent, (ii) par value, ₹10,000, (iii) years to maturity, 10 years and (iv) annual interest payment, compute the YTM.

Answer:

Substituting the values in Equation below:

$$B = I\left[\sum_{t=1}^{n}\frac{1}{(1+k_d)^t}\right] + M \times \left[\frac{1}{(1+k_d)^n}\right]$$
$$= I \times (PVIFA_{k_d,n}) + M \times (PVIF_{k_d,n})$$

₹10,800 = [₹1,000 3 (PVIFAk$_{d,10}$) + ₹10,000 3 (PVIFAk$_{d,10}$)]

If k_d = 10 per cent, that is, equal to the coupon rate, the value of the bond would be ₹10,000. Since the value of the bond is ₹10,800, the k_d must be less than 10 per cent. Using 9 per cent discount rate (k_d), we get;

₹ 1,000 × (PVIFA9,10) + Rs 10,000 (PVIF$_{9,10}$) = (₹ 1,000 × 6.418) + (₹ 10,000 × 0.422)

= ₹ 6,418 + ₹ 4,220 = ₹ 10,638

Since the value of the bond (₹10,638) at k_d = 9 per cent is less than ₹10,800 (current market price), we try a lower rate of discount (k_d).

Using 8 per cent, we get (₹ 1,000 3 6.710) + (₹10,000 3 0.463)

= ₹ 6,710 + Rs 4,630 = ₹ 11,340

Since the bond value (₹ 11,340) is higher than the current price of ₹ 10,800, the k_d (YTM) must be between 8 and 9 per cent. The exact value can be found by interpolation, as discussed below.

(i) Difference between the bond values at 8 and 9 per cent = ₹702 (₹ 11,340 –₹ 10,638)

(ii) Difference between desired value (₹ 10,800) and the value with the lower,

k_d = ₹ 540(₹11,340 – ₹ 10,800)

(iii) Percent of the difference/distance across the discount rate range, 8-9 per cent, that is, divide the value from step (i) by the value found in step (ii) = 0.77 (₹ 540 /₹ 702)

(iv) Multiplying the per cent in (iii) by the interval width of 1 per cent (9-8) per cent = 0.77 per cent (0.77 × 1%)

(v) Adding the value in (iv) to the interest rate associated with the lower end of the interval/interest rate = 8.77 per cent (8 + 0.77). Thus, the YTM = 8.77 per cent

Example 2

A Ltd. wishes to acquire B Ltd. on the basis of an exchange ratio of 0.8. Other relevant financial information is as follows:

Particulars	A Ltd.	B Ltd.
Earnings after taxes (EAT) (₹)	1,00,000	20,000
Equity shares outstanding	50,000	20,000
Earnings per share (EPS)	2	1
Market price per share (₹)	20	8

(i) Determine the number of shares required to be issued by A Ltd. for acquisition of B Ltd.

(ii) What would be the exchange ratio if it is based on the market prices of shares of A Ltd. and B Ltd.?

(iii) What is the current price-earnings ratio of the two companies?

(iv) Assuming the earnings of each firm remains the same, what is the EPS after the acquisition?

(v) What is the equivalent EPS per share of B Ltd.?

(vi) Ascertain the gain to shareholders of both the companies (a) at 0.8 exchange ratio, and (b) an exchange ratio based on market price.

Answer:

(i) Shares required to be issued by A Ltd: Shares of B Ltd (×) Exchange ratio

= 20,000 × 0.8 = 16,000.

(ii) Exchange ratio based on market prices:

Market price per share of B Ltd/Market price per share of A Ltd = ₹ 8/₹ 20 = 0.4. For every 10 shares of B Ltd, 4 shares of A Ltd would be issued.

(iii) P/E ratio of the companies (before merger)

Particulars	A Ltd.	B Ltd.
Market price per share	20	8
EPS	2	1
P/E ratio	10	8

(iv) EPS after merger

(a) Exchange ratio 0.8 = (₹1,00,000 + ₹ 20,000)/(50,000 + 16,000) =₹ 1.82

(b) Exchange ratio 0.4 = (₹1,00,000 +₹ 20,000)/(50,000 + 8,000) = ₹2.069

(v) Equivalent EPS per share of B Ltd = (EPS after the acquisition × exchange ratio)

= ₹1.82 x 0.8 = ₹1.45.

(vi) Gain from the merger

Post-merger market value of the firm		₹12,00,000
(Post-merger earnings × P/E ratio of A Ltd)		
Less: Pre-merger market values		
A Ltd (50,000 × ₹ 20	=₹10,00,000	
B Ltd (20,000 × ₹ 8	= ₹1,60,000	₹11,60,000
		₹**40,000**

Apportionment of gains between shareholders of the two companies

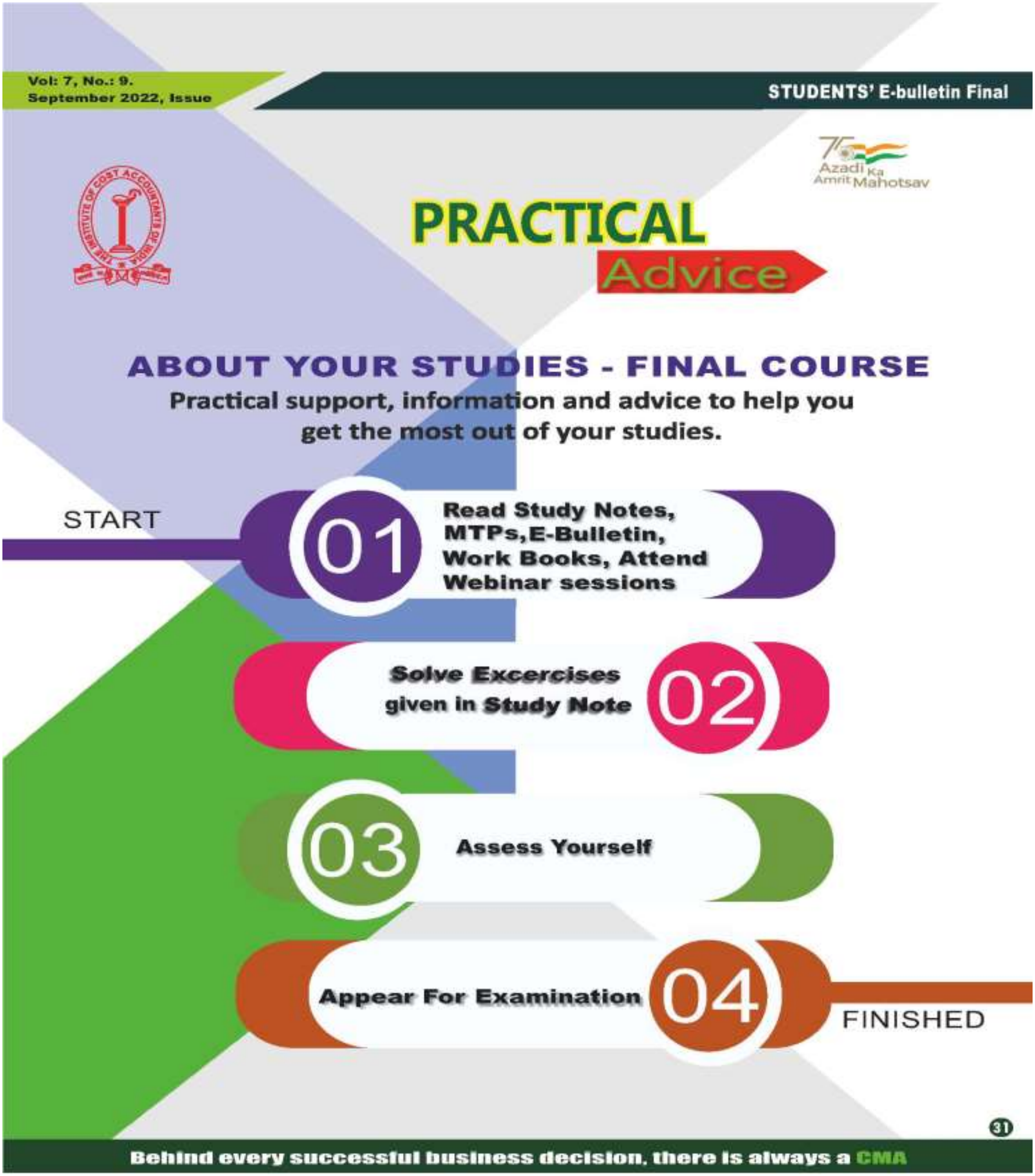
Particulars	Exchange ratio 0.8		Exchange ratio 0.4	
	A Ltd.	B Ltd.	A Ltd.	B Ltd.
Post-merger value	Rs 9,09,091[1]	Rs 2,90,909[2]	Rs 10,34,483[3]	Rs 1,65,517[4]
Less pre-merger value	10,00,000	1,60,000	10,00,000	1,60,000
Gain (Loss)	(90,909)	1,30,909	34,483	5,517

[1]12,00,000 x 50/66; [2]12,00,000 x 16/66; [3]12,00,000 x 50/58; [4]12,00,000 x 8/58

Examination Time Table

Day & Date	Final Examination Syllabus-2016 (Time: 02:00 P.M. to 05:00 P.M)	
	(Group – I)	(Group – II)
Thursday, 5th January, 2023	Corporate Laws & Compliance (P-13)	....
Friday, 6th January, 2023	....	Corporate Financial Reporting (P-17)
Saturday, 7th January, 2023	Strategic Financial Management (P-14)	....
Sunday, 8th January, 2023	....	Indirect Tax Laws & Practice (P-18)
Monday, 9th January, 2023	Strategic Cost Management – Decision Making (P-15)	....
Tuesday, 10th January, 2023	....	Cost & Management Audit (P-19)
Wednesday, 11th January, 2023	Direct Tax Laws and International Taxation (P-16)	....
Thursday, 12th January, 2023	....	Strategic Performance Management and Business Valuation (P-20)

Practical Advice



Submissions

Vol: 7, No.: 9.
September 2022, Issue

SUBMISSIONS

150 YEARS OF CELEBRATING THE MAHATMA

Azadi Ka Amrit Mahotsav

Submissions

Dear Students,

We are very much delighted to receive responses from all of you; for whom our effort is!

We have noted queries and your requests will definitely be carried out. Further, requesting you to go through the current edition of the bulletin. All the areas will be covered gradually. Expecting your responses further to serve you better as we believe that there is no end of excellence! One of the mails received is acknowledged below.

Please put your opinions so that we can make your e-bulletin everything that you want it to be.

Send your Feedback to:
e-mail: studies.ebulletin@icmai.in
website: http://www.icmai.in

Message form Directorate of Studies

Dear Students,

We from the Directorate of Studies understand your expectations from us and accordingly we are trying to deliver some meaningful tips through various publications in soft versions like-E-bulletins, Mock Test Papers (MTPs), and we also have conducted Webinar Sessions for the benefit of the students. Supplementary and Amendments are also uploaded from time to time to keep the students updated about the recent changes made in the papers; wherever applicable.

You must be aware that India is celebrating Azadi Ka Amrit Mahotsav, which is an initiative of the Government of India to celebrate and commemorate 75 years of independence and the glorious history of its people, culture and achievements. Along with pan India, your Institute has also observed and took part in various meaningful activities throughout the year. We also expect that our students should also take part in the development of the nation and make the country proud.

"Freedom has only one motto, may our country be happy and prosperous" ....

let you all observe the message cited above.

- Certain general guidelines are listed below and which will help you in preparing for the examinations:
- Conceptual understanding and overall understanding of the subjects should be clear,
- Students are advised to go through the study material provided by the Institute meticulously,
- Students should know and learn the basic understandings of the subjects with focus on core concepts,
- Students are expected to give to the point answer which is a pre-requisite for any professional examination,
- To strengthen the answers, students are advised to answer precisely and in the structured manner,
- Proper time management is also important while answering.

Please refer the link mentioned below:

https://icmai.in/studentswebsite/index.php

GOOD LUCK

Be prepared and be successful

Few Snapshots

Few Snapshots

Lighting of the Lamp: CMA Avijit Goswami, former Central Council Member, CMA Amal Kumar Das, Past President, CMA Biswarup Basu,Immediate Past President,CMA (Dr.) Sunder Ram Korivi, Academic Head, HSNC University& Adjunct Faculty of IICA, MCA, CMA Basant Maheswari, Portfolio Manager and CMA Chittaranjan Chattopadhyay, Chairman, BFSI Board (L to R)

President & VicePresident of the Institute congratulated the newly joined Secretary to the Government of India, Ministry of Corporate Affairs on 02 November 2022.

The Institute of Cost Accountants Of India has signed an MoU with Mallapuram District Panchayath for a GST Course to the students of the Panchayath. Glimpses of MoU sharing ceremony.

Corporate Laws Committee in association with Southern India Regional Council & Cochin Chapter of the Institute of Cost Accountants of India & Kochi Chapter of SIRC of the ICSI organised one day Seminar on "Powering towards inclusive and sustainable growth- Role of Professionals" at Kochi on 22nd October 2022.

Corporate Laws Committee in association with Southern India Regional Council & Cochin Chapter of the Institute of Cost Accountants of India & Kochi Chapter of SIRC of the ICSI organised one day Seminar on "Powering towards inclusive and sustainable growth- Role of Professionals" at Kochi on 22nd October 2022.

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA
(Statutory body under an Act of Parliament)
Headquarters: CMA Bhawan, 12, Sudder Street, Kolkata - 700 016
Phone: +91-33-2252-1031/34/35/1602/1492/1619/7373/7143
Delhi office: CMA Bhawan, 3, Institutional Area, Lodhi Road, New Delhi - 110 003
Phone: +91-11-2462-2156/2157/2158