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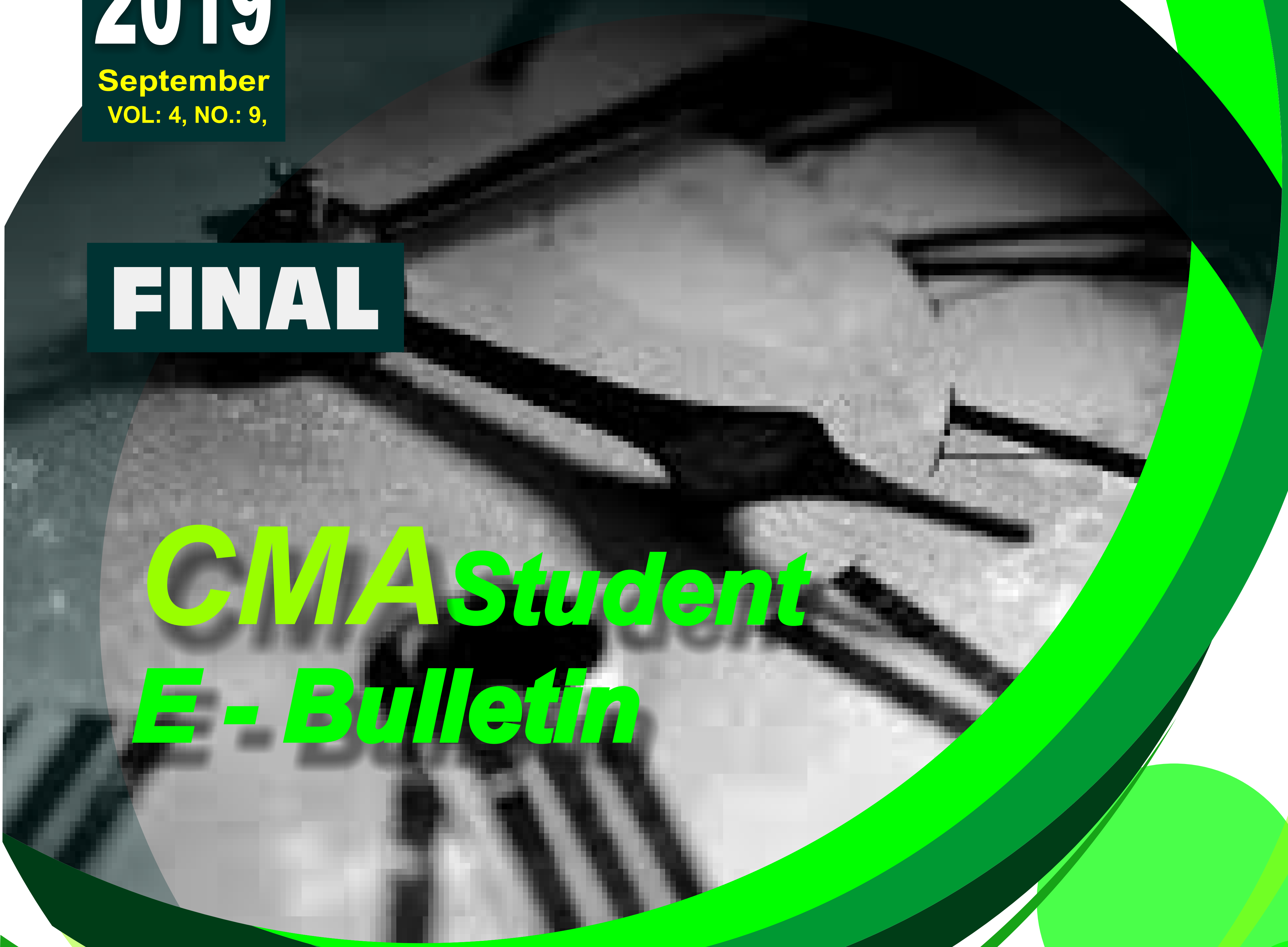

FINAL

CMA Student E - Bulletin

150 YEARS OF CELEBRATING THE MAHATMA

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Behind every successful business decision, there is always a CMA

Message from The Chairman

CMA Biswarup Basu
Vice President & Chairman,
Training & Education Facilities (T& EF) Committee

CMA BISWARUP BASU
Chairman, T & EF Committee
Directorate of Studies

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MESSAGE FROM THE CHAIRMAN

Dear Students,

Greetings,

"Be the change that you want to see in the world".

Mahatma Gandhi is revered the world over as one of history's most transformative and inspirational figures. Today the power of Gandhi's words still inspires us to change the world by changing ourselves.

Education is not just to read and write but to make use of it for their own advantages and to utilize the knowledge for their growth. To live a flawless life, education is very important for every individual. Education is nothing but studying different kinds of subjects to gain knowledge and understanding and trying to apply it in daily life. Education is the ability to think, apply it in the world and to know the value of life.

I am delighted to see that the Directorate of Studies (D.O.S.) is trying continuously to guide you through various publications in e-form; Mock Test Papers (both questions and answers), Work Book (both questions and answers), monthly publication of E-bulletin & conducting of Webinar Sessions; all are for your continuous learning and practice. Try to grab those opportunities.

I am really thankful to all academicians who, despite their busy schedule, have helped the D.O.S. all the way and have encouraged you all by contributing their valuable input and which had also helped the D.O.S. in timely publications of E-bulletin. I hope, you are enjoying those publications and developing yourselves day by day.

My dear future professionals, I stand committed towards your development always and I want to conclude with the words of Swami Vivekananda **"A man is not poor without a rupee but a man is really poor without a dream and ambition."**

I wish you all, Happiness and Prosperity for the forthcoming Durga Puja, & Dussehra festivals.

CMA Biswarup Basu
Vice President & Chairman, Training & Education Facilities and Placement Committee

Be a CMA, be a Proud Indian

150 YEARS OF CELEBRATING THE MAHATMA

"Behind every successful business decision there is always a CMA"

Vol: 4, No.: 9.
September 2019, Issue

CONTENTS

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.

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GROUP: 3, PAPER: 13

CORPORATE LAWS & COMPLIANCE (CLC)

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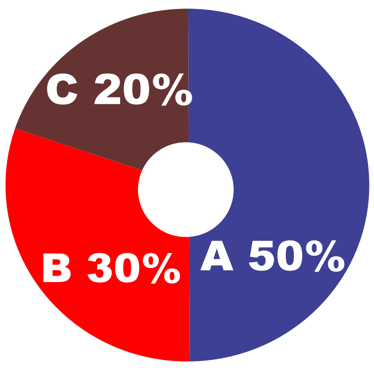
Your Preparation Quick Takes



Syllabus Structure

A Companies Act **50%**
B Other Corporate Laws **30%**
C Corporate Governance **20%**

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.

Role and rights of Shareholders

How to become Shareholders

Both equity and preference shareholders are the owners of the company.

They are the persons whose names appear in the register of members of the company. A person/artificial person become members by following mode.

(i) by allotment: Shares are allotted to him by the company and therefore becomes the first owner of the shares.
(ii) By transfer: existing shareholder transfers share to some person, normally by sale but may be by gift also.
(iii) by transmission: act of God/ Law.
(iv) a process by which a person becomes shareholder by default, i.e. by succession or by way of merger/amalgamation or court order.

Member and Shareholder

A person whose name appears in the Registrar of Members of the company is a member. All persons who are allotted shares or who purchase and intimates the company are entered in the register.

Difference between a shareholder and a member is that all members may not be shareholders and all shareholders may not be member due to time lag in registration of transfer. Let us assume Ramesh holds 1000 shares in ABC Ltd. and sells it to Suresh who immediately doesn't make any application for transfer. In such a case though he is a shareholder, name of Ramesh shall remain as a shareholder in the records of the company.

Cessation of Membership-

1. by cancellation of allotment by the company.
2. by forfeiture of shares: When the value of shares are taken in installments and if someone fails payment of such installment, the value already paid against the shares may be for forfeited.
3. by sale by the holder.
4. by buy back: There is rule and procedure of buy back of shares by the company itself. These shares are ultimately cancelled.
5. incapacity by law to hold shares: There may be legal restriction on some person to hold shares.

Transfer of Shares: Any person who is a shareholder may transfer the shares to any other person. There may be restriction on transfer in case of private companies. While transferring, a Share Transfer Form (Form SH4) have been filled up and signed by the seller of shareholder. The buyer may fill his details or may fill it up latter. The form is valid for days within which he buyer has to lodge the Share Transfer Form duly filled in along with share transfer stamp of value of 0.25% of the sale consideration within 60 days of execution. The original share certificates also have to be attached. The company share certificates also have to be attached. The company registers the share transfer with a period of one month from the date of receipt.

Rights of shareholders: The Law provides for various kinds of rights of a shareholder. However the following rights are very important for a shareholder.

(i) Right to vote: shareholders, other than those holding non voting shares, are entitled to vote in General Meetings of shareholders. Proportionate to the holding, i. e. each share has one vote.
(ii) Right to Rights Shares: Whenever the company decides to increase its share capital the shareholder may decide that further shares shall be allotted to the existing shareholders proportionate to their existing.
(iii) Right to Bonus Shares: When the free reserves of the company arrives at a comfortable position, the company may decide to allot shares without any price to the existing shareholder on proportionate basis. Reserves are undistributed profits which accumulate year after year and free reserves are reserves not specified for any particular purpose.
(iv) Right to dividend: Dividend is a part of a profit earned by the company and distributed to the shareholder as percentage to their shareholding.

Meetings of Members:

These are meetings of the members / shareholders of the company. Member's meetings are of the following types :-

Annual General Meeting:

An Annual general meeting (AGM) must be held by every type of company, public or private, limited by shares or by guarantee, with or without share capital or unlimited company, once a year.

Timing of the meeting:

Every company must in each calendar year hold an annual general meeting. Not more than 15 months must elapse between two annual general meetings. However, a company may hold its first annual general meeting within 18 months from the date of its incorporation. AGM should be held within 6 months of closure of accounting year.

The AGM must be held on a working day during business hours at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated.

Notice:

A notice of at least 21+2+2=25 days before the meeting must be given to members. The time, date and place of the meeting must be mentioned in the notice.

The notice of the meeting must be accompanied by a copy of the annual accounts of the company, director's report on the position of the company for the year and auditor's report on the accounts.

The notice should also state that a member is entitled to attend and vote at the meeting and is also entitled to appoint proxies in his absence.

Default:

In case of default, National Company Law Tribunal(NCLT) shall on application of any member call or direct calling of Annual General Meeting (AGM).

Business to be transacted at Annual General Meeting:

The following matters constitute ordinary business at an AGM: -

a. Consideration of annual accounts, director's report and the auditor's report
b. Declaration of dividend
c. Appointment of directors in the place of those retiring
d. Appointment of and the fixing of the remuneration of the statutory auditors.

Any other business would be considered as special business.

In case any there is any other business (special business) discussed and decided upon, an explanatory statement of the special business must also accompany the notice calling the meeting. Such statement shall explain the background and rationale of the proposal.

Extraordinary General Meeting

Every general meeting (i.e. meeting of members of the company) other than the annual general meeting or any adjournment thereof, is an extraordinary general meeting. Such meeting is usually called by the Board of Directors for some urgent business which cannot wait till the next AGM. Every business transacted at such a meeting is special business, since ordinary business cannot be transacted in Annual General Meeting (AGM).

Extraordinary General Meeting on Requisition:

The members of a company have the right to require the calling of an extraordinary general meeting by the directors. The board of directors of a company must call an extraordinary general meeting if required to do so by the following number of members :-

a. not less than one-tenth of such of the voting rights in regard to the matter to be discussed at the meeting ; or
b. Such meeting should be called by the company within 21 days of receiving the requisition within 45 days of receiving the notice.

The requisition must state the objects of the meetings and must be signed by the requisitioning members.

Power of NCLT to Order Calling of Extraordinary General Meeting:

If for any reason, it is impracticable to call a meeting of a company, other than an annual general meeting, or to hold or conduct the meeting of the company, the Company Law Board may, either i) on its own motion, or ii) on the application of any director of the company, or of any member of the company, who would be entitled to vote at the meeting, order a meeting to be called and conducted as the Company Law Board thinks fit,.

Proxy

In case of a company having a share capital and in the case of any other company, if the articles so authorize, any member of a company entitled to attend and vote at a meeting of the company shall be entitled to appoint another person (whether a member or not) as his proxy to attend and vote instead of himself. Every notice calling a meeting of the company must contain a statement that a member entitled to attend and vote is entitled to appoint one proxy in the case of a private company and one or more proxies in the case of a public company and that the proxy need not be member of the company.

6.2 Quorum (Section 174)

Quorum refers to the minimum number of members who must be present at a meeting in order to constitute a valid meeting. A meeting without the minimum quorum is invalid and decisions taken at such a meeting are not binding.

In case the Company Law Board calls or directs the calling of a meeting of the company, when default is made in holding an annual general meeting, the Government may give directions regarding the quorum including a direction that even one member of the company present in person, or by proxy shall be deemed to constitute a meeting. As per the present law, the quorum requirement is as follows:

Members of the Company upto	Quorum
1000	5
1001-5000	15
5001	30
Private company	02

6.3 Proceedings in Meeting:

The courses of actions which are undertaken in a meeting are termed as proceedings. In a proceeding of a meeting the Chairman of that meetingdescribe in brief the position and performance of the company and actions or initiatives taken for better performance of the company.

6.4 Rights of shareholders:

- To call for Extra Ordinary General Meeting, if necessary.
- To appoint a director in an Annual General Meeting.
- To receive every information about the company.
- To apply to Tribunal in case of oppression and mismanagement of the company.
- To have right in respect of amalgamation and reconstruction.

GROUP: 3, PAPER: 14

STRATEGIC FINANCIAL MANAGEMENT (SFM)

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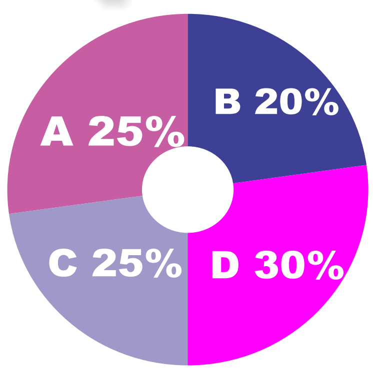
Your Preparation Quick Takes



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

Strategic Financial Management

Direct and Indirect quotations

A direct quote is the price of a foreign currency in domestic currency units. In direct quote, the home currency fluctuates and the foreign currency against which it is quoted remains constant. For example, if we say that $1 = Rs. 68, we are expressing one unit of dollar (a foreign currency for an Indian) in terms of some units of domestic currency. Therefore, it is a dollar direct quote for an Indian in India and it is also expressed as USD/INR 68 or INR 68 per USD.

An indirect quote is the price of the domestic currency in foreign currency units. In indirect quote, the foreign currency fluctuates and the home currency remains constant. Thus, an indirect quote is a quote where the exchange rate is expressed in terms of units of the foreign currency per fixed number of units of home currency. For example, if we say that Re 1 = $0.0147, we are expressing a standard unit of rupee (domestic currency for an Indian) in terms of some units of foreign currency ($).

European terms and American terms

It refers to the quoting of the quantity of a specific currency per one US dollar. It means that whenever a currency's value is quoted, it is quoted in terms of number of units of currency to equal one US dollar. The result is that most currencies are quoted per U.S. dollar--Japanese yen per U.S. dollar, Brazilian real per U.S. dollar and so on.

There are two major expectations to this rule of using European terms: the euro and the U.K pound sterling. Both are normally quoted in American terms; the U.S. dollar price of one euro and the US dollar price of one pound sterling. Additionally, Australian dollars and New Zealand dollars are normally quoted on American terms. Thus in American terms, USD becomes the quoted currency against these currencies (i.e., euro, U.K pound, etc.). American terms are used in quoting rates for most foreign currency options and futures, as well as in retail markets that deal with tourists and personal remittances.

Let us take another example of currency quotations in European terms and American terms. Let us also assume that we are having two currencies-U.S. dollar (USD) and euro (EUR).

European terms	**American terms**
↓	↓
Foreign currency price of one dollar (USD)	US dollar price of one euro (EUR)
↓	↓
USD/EUR 0.7125 Or USD 1.00 = EUR 0.7125	EUR/USD 1.4035 Or EUR 1.00 = USD 1.4035
↓	↓
USD is the base or unit currency EUR is the quoted or price currency	EUR is the base or unit currency USD is the quoted or price currency

Thus, $\frac{1}{\text{EUR}0.7125/\text{USD}} = \text{USD}\,1.4035/\text{EUR}$

It indicates that American terms and European terms are reciprocals.

Illustration 1

Identify whether the following is a direct quote in USA. If not, find it.

a) Rs 69 = 1$
b) GBP 1 = $0.748

Solution

A direct quote is one where one unit of foreign currency is expressed as same units of domestic currency. In USA, $ is the home currency.

a) No. this is indirect quote in USA.
   Direct quote in USA would be

   $$\text{Rs }1 = \$\,\frac{1}{69} = \$0.0144$$

b) This is a direct quote in USA.

Illustration 2

From a Japanese point of view, which of the following is direct quote? Which is the indirect quote?

a) JPY/GBP 310
b) GBP/JPY 0.00322
c) JPY/USD 230
d) USD/JPY 0.00434

Solution

A direct quote is one where one unit of foreign currency is expressed as same unit of domestic currency. For Japan, JPY is the home currency.

a) Direct quote
b) Indirect quote
c) Direct quote
d) Indirect quote

Illustration 3

A quotation is given as USD/CHF 1.6370/75

a) What are the two currencies involved?
b) Is the rate being stated as USD per CHF or CHF per USD?
c) At what rate will the bank giving the quote to buy USD?
d) At what rate will it sell USD?
e) How much is the bid-offer spread in points?

Solution

a) The two currencies are US dollar and Swiss franc
b) The rate is being stated as CHF per USD or CHF price of 1 USD
c) The bank will buy 1 USD for 1.6375 CHF
d) The bank will sell 1 USD for 1.6275 CHF
e) The bid-offer spread is 5 points.

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150 YEARS OF CELEBRATING THE MAHATMA

GROUP: 3, PAPER: 15

STRATEGIC COST MANAGEMENT-DECISIONMAKING (SCMD)

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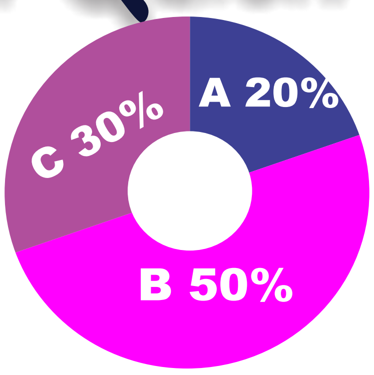
Your Preparation Quick Takes



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:

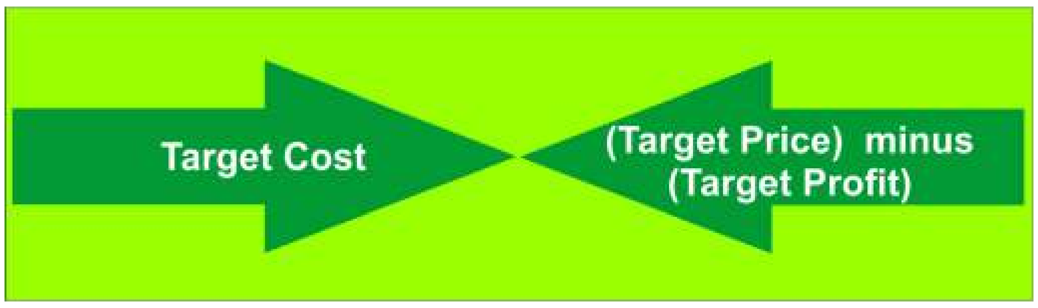
The Strategic cost management framework provides a clear plan of attack for addressing costs and decisions that affect them. It helps to get answers on:

- 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 modelling capability?

Target Costing

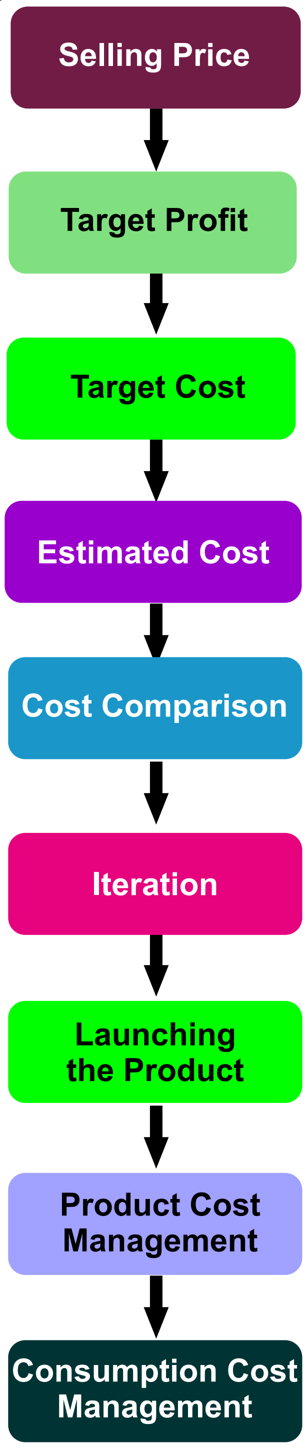
01.00 Philosophy

Effective cost management systems are developed in response to changing competitive conditions. Target Costing is an example of such a system that has a special relevance to companies in the process and assembly industries. Target Costing focuses on searching for opportunities for cost reduction at the product planning stage itself. In addition, it enables continuous cost reductions once a product commences manufacture.



In a competitive economy, product markets influence the determination of the price of the product and the financial markets influence the determination of the cost of capital. Cost of the capital infused by the enterprise sets the benchmark for the quantum of the profit to be achieved. Thus, price of the product as also the quantum of the profit are market driven. The end result is that the product cost boundaries are set by the difference between the price and the profit.

Target Costing advocates the philosophy in which product development is based on what the customer wants and is willing to pay for and not what it costs to produce. Hence it starts with the market determined price; then deducts the desired profit margin; and works back the target cost. Peter Drucker calls this "price-led costing."



And that is how the formulation:
"Target Cost = Target Price – Target Profit" in place of the traditional approach of "Cost + Profit = Selling Price".

In companies where target costing is used, there seems to be a different culture and attitude. They place more emphasis on their relative position in the market and product leadership.

02.00 Process of Target Costing

The stages in the process of target costing may be summarised as:

1. Selling Price: The first step in target costing is the establishment of a selling price for the new product by adopting market driven approach.
2. Target Profit: The second step is that of visualising a target profit by means of an investment driven considerations.
3. Target Cost: The third step enables determining the target cost by subtracting the target profit from the established selling price.
4. Estimated Cost: The fourth step relates to determining the estimated cost for the product on the basis of functional cost analysis and value engineering of individual components and processes.
5. Cost Comparison: Then follows the exercise of comparing the estimated cost with the target cost. The gap between the target cost and the estimated cost of the product reflects the excess cost which must be taken out of the new product.
6. Iteration: After identifying the gap between the target cost and the estimated cost, it is necessary to identify ways to close the gap through iterative processes of cost analysis and value engineering till the estimated cost matches the target cost. Target, or allowable, costs are identified for individual components

or processes and cost improvement teams keep on working to reduce the estimated costs to match the target.

Cost-reduction requirements are applied across all the components and subsystems of the product based on an informed assessment of how much cost can be removed from each component after taking into consideration value to the customer, historical trends and other data. There may also be a process of negotiation between different production departments and between the company and its suppliers to arrive at final target costs for the individual components. This process of cost reduction is an iterative one which continues until the target cost is reached or it is concluded that the overall target cost cannot be reached and a decision is made not to launch the product.

7. Launching the Product: The product is on for launching after the cost estimate is on target.

8. Product Cost Management: Once the target costs have been determined, actual costs can be monitored and managed against the targets using the usual budgeting and costing methods such as standard costing.

9. Consumption Cost Management: A consumer friendly post sale support service should be oriented towards cost management during the consumption cycle of the product.

03.00 Advantages

Target costing offers a range of advantages which include the following:

(i) Top-to-bottom Commitment: Target costing reinforces top-to-bottom commitment to process and product innovation, and is aimed at identifying issues to be resolved, in order to achieve appropriate competitive advantage.
(ii) Market-driven Management: Target costing helps to create a company's competitive future with market-driven management for designing and manufacturing products that meet the price required for market success.
(iii) Best Value: Target costing uses management control systems to support and reinforce manufacturing strategies; and to identify market opportunities that can be converted into real savings to achieve the best value rather than simply the lowest cost.

04.00 Illustration

ABC Limited finds a market niche to an innovative kitchen grinder at a market driven price of Rs.3000/- per piece. The estimated sales volume at that price would work out to Rs.40,000/- pieces per annum aggregating to Rs.12 crores. The projected investment towards designing, developing, producing, marketing and servicing these grinders is estimated to be Rs.8 crores; and the desired return on investment is 15% per annum.

Given the afore said data, the target cost to design, develop, produce, market and service the kitchen grinder of ABC Limited may be formulated as shown in the table that follows.

Target Cost of Kitchen Grinder

Serial	Item	Workings	Amount in Rs.
1	Projected Sales	40,000 pieces @ Rs.3,000/- per piece	12,00,00,000
2	Desired Profit	15% ROI on Rs.8,00,00,00 of Investment	1,20,00,000
3	Target Cost	Projected Sales – Desired Profit	10,80,00,000
4	Target Cost per grinder	Target cost / 40,000 pieces	2,700

The target cost of Rs.1,080 lakhs per annum which computes to Rs.2,700/- per grinder would further be broken down function-wise for the designing, developing, producing, marketing, servicing, and so on. Each of the functional areas would be made responsible to achieve the actual costs in line with the targets.

05.00 Quick Take
Every Indian SME could concentrate on target cost management and be known for being cost competitive at the global front.

CA Vikash Mundhra
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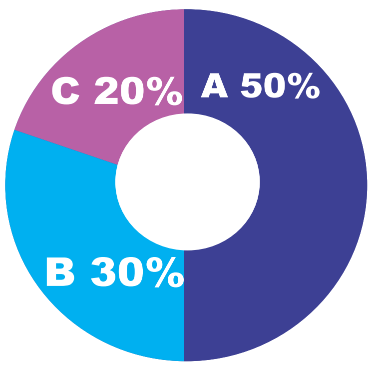
GROUP: 3, PAPER: 16

DIRECT TAX LAWS AND INTERNATIONAL TAXATION (DTI)

Your Preparation Quick Takes



Syllabus Structure

A Advanced Direct Tax Laws **50%**
B International Taxation **30%**
C Tax Practice and Procedures **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.

PENALTY FOR UNDER REPORTING & MISREPORTING

Under the earlier legislation, the levy of penalty for concealment or furnishing of inaccurate particulars of income u/s 271(1)(c) has always been a matter of dispute between the revenue authorities and the taxpayers. There was lack of specificity in terms of quantum of penalty.

Under the earlier provisions, Income-tax Officer had the discretion to levy penalty ranging from 100% to 300% of tax sought to be evaded. The discretion regarding quantum of penalty led to corruption and a large number of pending disputes despite a number of judicial precedents on the interpretation of statutory provisions. The tax authorities always tried to levy the penalty whenever there was an addition or disallowance made by the assessing officer, even in cases where there was no prima facie case against the taxpayer.

Under the new scheme for the imposition of the penalty, matters are classified into two parts:

Under Reporting of Income; and

Misreporting of Income

Penalty for under-reporting and misreporting of income [Sec. 270A]

The

- Assessing Officer; or
- Commissioner (Appeals); or
- Principal Commissioner or Commissioner

may, during the course of any proceedings under this Act, direct that any person who has under-reported his income shall be liable to pay a penalty in addition to tax, if any, on the under-reported income.

Taxpoint

- Penalty proceedings must be initiated before completion of the assessment or appeal order or revision order, as the case may be.
- Penalty order is different from assessment order. Aggrieved with the penalty order passed by the Assessing Officer, the assessee is required to file separate appeal to the Commissioner (Appeals) or separate revision petition u/s 264 or separate rectification petition u/s 154. Further, appeal can be filed with the Tribunal against the penalty order passed by the Commissioner (Appeals) or Principal Commissioner or Commissioner.
- Tribunal cannot impose penalty
- Penalty shall be imposed by the respective income-tax authority on addition made by them. E.g., on addition being made by the Assessing Officer, Commissioner (Appeals) cannot levy penalty. Even the Assessing Officer fails to levy penalty on such addition, Commissioner (Appeals) cannot levy penalty on such addition made by the Assessing Officer. In CIT -vs.- Shadiram Balmukund, the Apex court has held that the Assessing officer can levy penalty on the additions made by him and not on the additions made by Commissioner (Appeals). Similarly, Commissioner (Appeals) can levy penalty on the additions made by him and not on the additions made by the Assessing Officer.

Quantum of penalty [Sec. 270A(7) & (8)]

- **50%** of the amount of tax payable on under-reported income [Sec. 270A(7)]
- **200%** of the amount of tax payable on under-reported income, where under-reported income is in consequence of any misreporting thereof by any person - [Sec. 270A(8)]

Cases of under-reporting of income [Sec. 270A(2)]

A person shall be considered to have under-reported his income, if:

a. the income assessed is greater than the income determined in the return processed u/s 143(1)(a);

b. the income assessed is greater than the maximum amount not chargeable to tax, where no return of income has been furnished;

c. the income reassessed is greater than the income assessed or reassessed immediately before such reassessment;

d. the amount of deemed total income assessed or reassessed u/s 115JB or 115JC is greater than the deemed total income determined in the return processed u/s 143(1)(a);

e. the amount of deemed total income assessed u/s 115JB or 115JC is greater than the maximum amount not chargeable to tax, where no return of income has been filed;

f. the amount of deemed total income reassessed u/s 115JB or 115JC is greater than the deemed total income assessed or reassessed immediately before such reassessment;

g. the income assessed or reassessed has the effect of reducing the loss or converting such loss into income.

Computation of amount of under-reported income [Sec. 270A(3)]

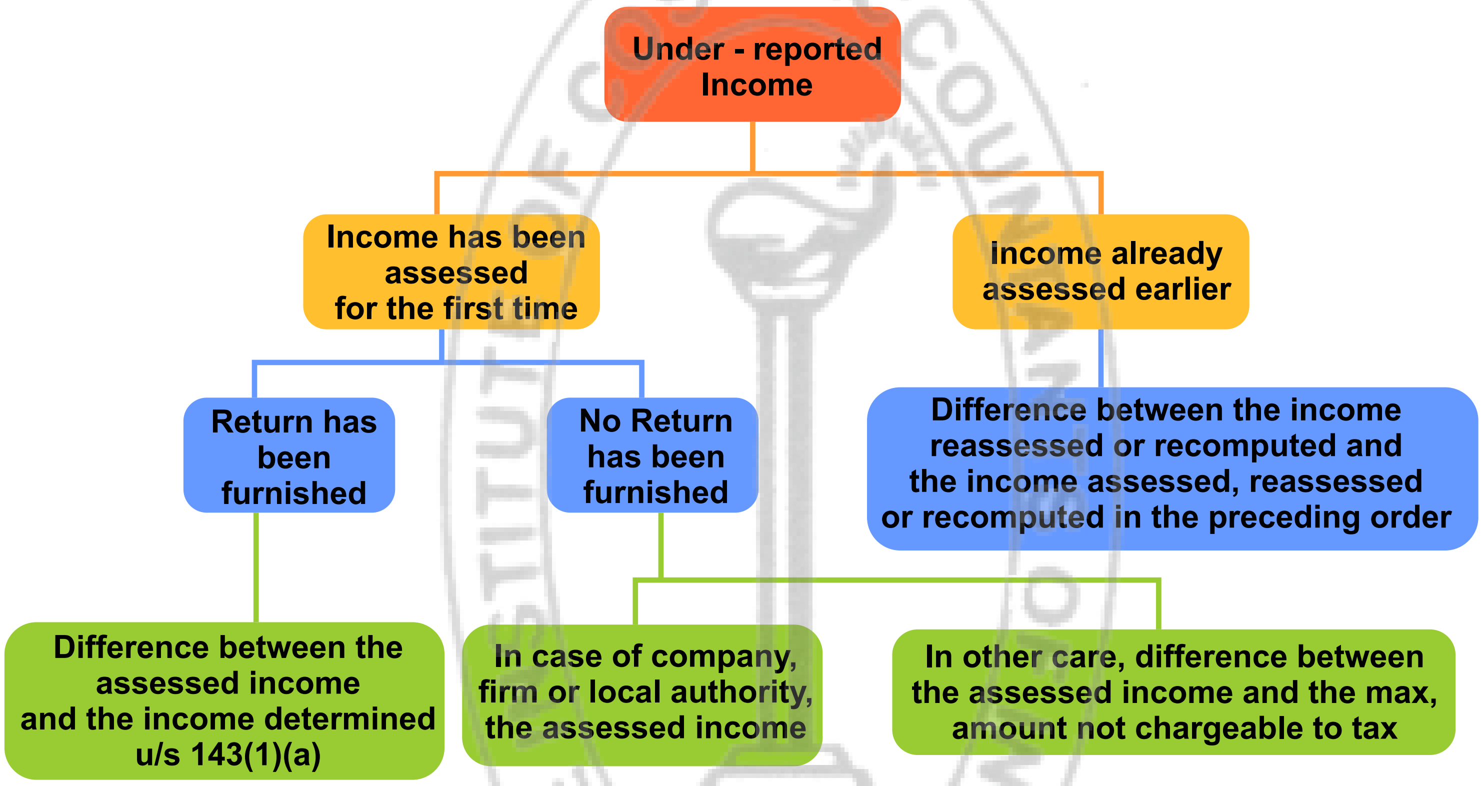
The amount of under-reported income shall be:

- in a case where income has been assessed for the first time:

• If return has been furnished	Assessed Income – Income determined u/s 143(1)a)
• If return has not been furnished	In case of company, firm or local authority: Assessed Income Other persons: Assessed Income – Basis Exemption Limit

- in a case where income has been assessed for the first time:
  Income reassessed or recomputed - Income assessed, reassessed or recomputed in a preceding order

  - Preceding order means an order immediately preceding the order during the course of which the penalty has been initiated.



- in a case where under-reported income arises out of determination of deemed total income in accordance with sec. 115JB or 115JC, the amount of total under-reported income shall be determined in accordance with the following formula:

$$(A - B) + (C - D)$$

Where,

A= Total income assessed as per the provisions other than the provisions contained in sec. 115JB or 115JC (herein called general provisions)

B = Total income that would have been chargeable had the total income assessed as per the general provisions been reduced by the amount of under-reported income;

C = Total income assessed u/s 115JB or 115JC

D = Total income that would have been chargeable had the total income assessed u/s 115JB or 115JC been reduced by the amount of under-reported income.

However, where the amount of under-reported income on any issue is considered both u/s 115JB / 115JC and under general provisions, such amount shall not be reduced from total income assessed while determining the amount under item D.

- in a case where an assessment or reassessment has the effect of reducing the loss declared in the return or converting that loss into income:

  The income or loss assessed or reassessed - Loss claimed

Meaning of under-reported income in a case where source is linked to earlier year [Sec. 270A(4)]

Where:

- the source of any receipt, deposit or investment in any assessment year
- is claimed to be an amount added to income or deducted while computing loss, as the case may be, in the assessment of such person
- in any year prior to the assessment year in which such receipt, deposit or investment appears (hereinafter referred to as "preceding year")
- and no penalty was levied for such preceding year,

then, the under-reported income shall include such amount as is sufficient to cover such receipt, deposit or investment.

Taxpoint

- Such amount shall be deemed to be amount of income under-reported for the preceding year in the following order:
  a. the preceding year immediately before the year in which the receipt, deposit or investment appears, being the first preceding year; and
  b. where the amount added or deducted in the first preceding year is not sufficient to cover the receipt, deposit or investment, the year immediately preceding the first preceding year and so on.
- The assessee can explain that the investment or expenditure is made out of additions made during earlier years – Anantharam Veerasinghaiah & Co. -vs.- CIT (SC)

Example

- Addition made by the Assessing Officer on estimated basis in the preceding year(s) ₹1,00,000
- Penalty levied on the said addition in the preceding year(s)
  [Due to provision of sec. 270A(6)(b) or © Nil
- In subsequent assessment year, such addition is explained as source of investment made by the assessee, citing the decision of the Apex court in the case of Anantharam Veerasinghaiah & Co.
- Despite this confession of concealment on the part of the assessee, no penalty was leviable in such cases as the time limit for initiating concealment penalty proceedings in respect of the earlier year in which addition was made would have expired. Moreover, the penalty could also not be imposed in respect of the year in which the deposit was made as there was no concealment in that year, the deposit having been explained as out of an earlier year's income.
- In this type of case, sec. 270A(4) comes into play which states that under-reported income shall include such amount.

Cases not considered as under-reported income [Sec. 270(6)]

The under-reported income shall not include the following:

a. Proper Explanation: The amount of income in respect of which the assessee offers an explanation and the Assessing Officer or the Commissioner (Appeals) or the Commissioner or the Principal Commissioner, as the case may be, is satisfied that the explanation is bona fide and the assessee has disclosed all the material facts to substantiate the explanation offered.
b. Estimate by the authority: The amount of under-reported income determined on the basis of an estimate, if the accounts are correct and complete to the satisfaction of the Assessing Officer or the Commissioner (Appeals) or the Commissioner or the Principal Commissioner, as the case may be, but the method employed is such that the income cannot properly be deduced therefrom;
c. Estimate by the assessee: The amount of under-reported income determined on the basis of an estimate, if the assessee has, on his own, estimated a lower amount of addition or disallowance on the same issue, has included such amount in the computation of his income and has disclosed all the facts material to the addition or disallowance.
d. Arm's length price: The amount of under-reported income represented by any addition made in conformity with the arm's length price determined by the Transfer Pricing Officer, where the assessee had maintained information and documents as prescribed u/s 92D, declared the international transaction under Chapter X, and, disclosed all the material facts relating to the transaction; and
e. Undisclosed income in search operation: The amount of undisclosed income referred u/s 271AAB

Cases of misreporting of income [Sec. 270A(9)]

The cases of misreporting of income shall be the following:

a. misrepresentation or suppression of facts;
b. failure to record investments in the books of account;
c. claim of expenditure not substantiated by any evidence;
d. recording of any false entry in the books of account;
e. failure to record any receipt in books of account having a bearing on total income; and
f. failure to report any international transaction or any transaction deemed to be an international transaction or any specified domestic transaction, to which the provisions of Chapter X apply.

Computation of tax payable on under-reported income [Sec. 270A(10)]

The tax payable in respect of the under-reported income shall be:

Where no return of income has been furnished and the income has been assessed for the first time	Tax calculated on the under-reported income as increased by the maximum amount not chargeable to tax as if it were the total income	
Where the total income determined u/s 143(1)(a) or assessed, reassessed or recomputed in a preceding order is a loss	Tax calculated on the under-reported income as if it were the total income	
In any other case	Tax on (Under-reported income + Income determined u/s 143(1(a) or income assessed, reassessed or recomputed in a preceding order)	***
	Less: Tax on Income determined u/s 143(1(a) or income assessed, reassessed or recomputed in a preceding order	(**)

Other Points

- No double penalty on same amount: No addition or disallowance of an amount shall form the basis for imposition of penalty, if such addition or disallowance has formed the basis of imposition of penalty in the case of the person for the same or any other assessment year – [Sec. 270A(11)].
- Written order: The penalty shall be imposed, by an order in writing, by the Assessing Officer, the Commissioner (Appeals), the Commissioner or the Principal Commissioner, as the case may be – [Sec. 270A(12)]

Illustration 1

Computation of under-reported income assuming income has been assessed for the first time:

Assessee	Return Filed	Income u/s 143(1)(a)	Assessed Income	Under-reported Income	Tax payable on (a)	Tax payable on (b)	Tax payable on (c)	Penalty
		a	b	c = (b – a)	d	e	f = (e – d)	f x 50%
Individual	Yes	6,00,000	10,00,000	4,00,000	33,800	1,17,000	83,200	41,600
Firm	Yes	17,00,000	20,00,000	3,00,000	5,30,400	6,24,000	93,600	46,800
Firm	Yes	(8,00,000)	20,00,000	28,00,000	-	8,73,600	8,73,600	4,36,800
Individual	Yes	(9,00,000)	(3,00,000)	6,00,000	-	33,800	33,800	16,900
Firm	No	N.A.	8,00,000	8,00,000	-	2,49,600	2,49,600	1,24,800
Individual	No	N.A.	7,50,000	5,00,000#	-	65,000	65,000	32,500

Assessed income as reduced by basic exemption

200% of (f) shall be levied as penalty if the case is misreporting of income.

Illustration 2

Computation of under-reported income assuming income has not been assessed for the first time:

Assessee	Income assessed in the preceding order	Reassessed Income	Under-reported Income
Individual	7,00,000	12,00,000	5,00,000
Company	20,00,000	22,00,000	2,00,000

Illustration 3

Compute penalty leviable u/s 270A in case of X Ltd from the following details:

Particulars	Total Income	Tax on Total Income	Book Profit	Tax on Book Profit
Return of income	80,00,000	24,96,000	2,00,00,000	41,17,360
Assessed income	1,20,00,000	40,06,080	2,10,00,000	43,23,228

Solution

Particulars		Amount
Under-reported income		
Total income computed by the Assessing Officer	A	1,20,00,000
Total income as per return of income	B	80,00,000
Book profit computed by the Assessing Officer	C	2,10,00,000
Book profit as per return of income	D	2,00,00,000
Under-reported income [(A – B) + (C – D)]		**50,00,000**
Tax on under-reported income		
Tax on A	P	40,06,080
Tax on B	Q	24,96,000
Tax on C	R	43,23,228
Tax on D	S	41,17,360
Tax on Under-reported income [(P – Q) + (R – S)]	T	17,15,948
Penalty u/s 270A		
• Minimum (being 50% of T)		8,57,974
• Maximum (being 200% of T)		34,31,896

Illustration 4

In the above example, out of addition of ₹ 10 lakh made in the book profit and ₹ 40 lakh made in the total income (under general provisions), ₹ 3,00,000 was made on the same ground. Compute penalty u/s 270A.

Solution

Computation of penalty

Particulars		Amount
Under-reported income		
Total income computed by the Assessing Officer	A	1,20,00,000
Total income as per return of income	B	80,00,000
Book profit computed by the Assessing Officer	C	2,10,00,000
Book profit as per return of income	D	2,03,00,000
Under-reported income [(A – B) + (C – D)]		
Tax on under-reported income		
Tax on A	P	40,06,080

Tax on B	Q	24,96,000
Tax on C	R	43,23,228
Tax on D	S	41,79,120
Tax on Under-reported income [(P – Q) + (R – S)]	T	16,54,188
Penalty u/s 270A		
• Minimum (being 50% of T)		8,27,094
• Maximum (being 200% of T)		33,08,376

YEARS OF CELEBRATING THE MAHATMA

GROUP: 4, PAPER: 17

CORPORATE FINANCIAL REPORTING (CFR)

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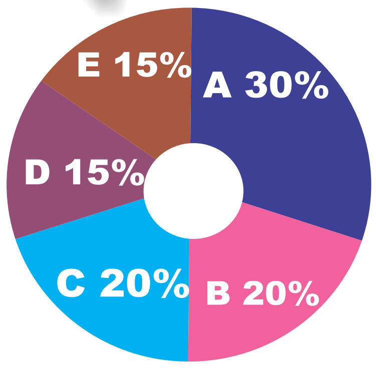
Your Preparation Quick Takes



Syllabus Structure

A GAAP and Accounting Standards **30%**
B Accounting if Business Comminations & Restructuring **20%**
C Consolidated Financial Statements **20%**
D Developments in Financial Reporting **15%**
E Government Accounting in India **15%**

Learning Objectives:

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

- Learn the importance of reporting of Labour Practices and Decent Work Conditions.
- Know the associated GRI-G4 Indicators.

Preparation of Consolidated Balance Sheet (CBS)

A group consists of a parent and its subsidiaries. A **parent** is an entity that **controls** one or more entities. A **subsidiary** is an entity that is controlled by another entity.

By purchase of shares the investor company (parent) acquires control in the investee company (called subsidiary).

Accounting for consolidated financial statements (as per Ind AS 110) is made by combining assets and liabilities of parent and subsidiaries, measuring non-controlling interest [Ind AS 110] and recognizing goodwill [Ind AS 103].

Ind AS 103 states that the acquirer obtaining control over acquiree, recognises and measures in its consolidated financial statements (i) the identifiable assets acquired, the liabilities assumed at Fair Value and (ii) any non-controlling interest in the acquiree at Fair Value or at Proportionate Value and (iii) the goodwill acquired in the business combination or a gain on bargain purchase. In a CBS on the date of acquisition they would be incorporated accordingly.

However for subsequent consolidation the post-acquisition changes in assets and liabilities and in NCI should also be considered but no change should be made to Goodwill/Gain on Bargain Purchase.

At the time of acquisition of shares in Subsidiary company (S) identified assets and liabilities of S are recorded in the consolidated accounts at fair value. Subsequently the non current items (assets and liabilities) of S are carried in the consolidated balance sheet at acquisition date fair value plus subsequent change in book value. However **for current items the revaluation profit or loss on the acquisition date (difference between fair value and book value) is reverted through post acquisition retained earnings#**, and thus the book values of parent and subsidiaries are combined for consolidation. [# Suppose that unsold stocks of S on acquisition date had carrying amount 1000 and Fair Value 1200. After one year, on the reporting date, stock (assumed) being fully sold at 1300, S's post acquisition profits amounting to 300 (1300 – 1000) should be reduced by 200 for consolidation as this 200 has already been considered as revaluation profit at the time of acquisition. In the illustration 1 and in illustration 2 we find application of this treatment.]

In subsequent CBS (Consolidated Balance Sheet), Non-Controlling Interest (NCI) is measured at value at acquisition (as per Ind AS 103) + share of NCI in post acquisition profits. Note that NCI as per Ind AS 103 can be measured at Fair Value or at proportionate value of net assets identified.

In subsequent CBS (Consolidated Balance Sheet) Goodwill/Gain on bargain purchase is recorded at acquisition date value as per Ind AS 103; ie., Consideration + NCI - Fair Value of net assets identified at acquisition.

For finding NCI and Goodwill the fair value of net assets can alternatively be represented by the Equity at acquisition plus pre-acquisition profits (duly adjusted by revaluation profits/losses arising from the difference between carrying amount and fair value of net assets). Share of NCI in pre-acquisition profit of subsidiary may be considered for measurement of NCI (at proportionate value) on the date of acquisition. Equity share capital plus Pre-acquisition profit (including revaluation profit/loss) = Net Assets identified at fair value). When NCI is measured at fair value, share of NCI in pre-acquisition profit of subsidiary is not required. But for consolidation on subsequent date the share of NCI in post acquisition profit or loss of the subsidiary must be added to NCI at acquisition date value. [Illustration 2 suggested].

Illustration 1. Company P Ltd. (a listed company) acquires 60% shares in company Q Ltd. on 1-4-17 at a cost of (Rs.Lakhs) 138, paid by issue of shares of Rs. 10 at par. The abstract of balance sheets of Q (along with fair values at the acquisition date) and P at the beginning and at the end of the year are as follows:

	Q (Rs.Lakhs)			P (Rs.Lakhs)	
	1-4-17 book value	1-4-17 Fair Value	31-3-18 book value	1-4-17	31-3-18
PPE	175	200	190	276	300
Investment in Q					138
Inventories	45	48	50	68	80
Financial Assets	80	60	70	100	120
Total assets	300		310	444	638
Equity Share Capital	130		130	200	338

Other Equity	80		90	120	150
Borrowings	60	60	60	80	100
Trade Paybles	30	28	30	44	50
Total of Equity and Liabilities	<u>300</u>		<u>310</u>	<u>444</u>	<u>638</u>

Prepare consolidated balance sheet of P on 31-3-18 based on Ind AS 110.
Solution:
Abstract of Consolidated balance sheet of P Ltd. and its subsidiary Q Ltd. as at 31-3-18

	working	Rs.Lakhs
PPE	300+215[x]	515
Goodwill		10[#]
Investment		
Financial Assets	120+50[z]	170
Inventories	80+50[y]	130
Total assets		<u>825</u>
Equity:		
Equity Share Capital		338
Other Equity		153[$]
NCI		94[&]
Liabilities:		
Borrowings	100+60	160
Trade Paybles	50+30	80
Total of Equity and Liabilities		<u>825</u>

Working Notes:
1. Net Assets of Q at Fair value (Rs.Lakhs)

Items	On 1-4-17 at book value	On 1-4-17 at Fair Value
PPE	175	200
Investment in Q		
Inventories	45	48
Financial Assets	80	60
Total assets	<u>300</u>	<u>Total = 308</u>
Equity Share Capital	130	
Other Equity	80	
Borrowings	60	60
Trade Paybles	30	28
Total of Equity and Liabilities	<u>300</u>	Total = 88
	Net Assets at Fair value	220

2. NCI at acquisition:

Fair Value of Consideration transferred = 138; NCI recognized at Fair Value: 40%* 138/60% = $92^{@}$;
[Alternative solution: @NCI can be measured at proportionate share of identifiable net assets = 40%*220 = 88; in that case NCI will be less by 4 and Goodwill also less by 4]

3. #: Goowill = Consideration + NCI – Fair Value of Identifiable Net Assets = 138 + 92 – 220 = 10.

4. Balance sheet data of Q (Rs.Lakhs)

	1	2	3	4	5	6
	1-4-17	1-4-17 Fair Value	Change on acquisition	Reversal of change in Current items to Retained Earnings	Change in Bk Value carried to subsequent B/S	Adj. B/S on 31-3-18 (1+3+4+5) or (2+4+5)
PPE	175	200	+25	-	+15	215^{x}
Inventories	45	48	+3	-3^{p}	5	50^{y}
Financial Assets	80	60	-20		-10	50^{z}
Trade Payables	(30)	(28)	+2	-2^{q}		(30)

5. &: NCI at reporting date:
NCI at the time of acquisition (@) = 92;
Post acquisition total comprehensive income of Q = 90 – 80 – 3^{p} – 2^{q} = 5;
Share of NCI = 40%*5 = 2;
Total NCI at the yearend = 92+2 = 94

6. $: Other Equity of P at the end of the year = 150;
Share of post acquisition Total comprehensive income of Q = 60%*5 = 3;
Other equity consolidated = 150 + 3 = 153.

Illustration 2. Company P Ltd. (P) acquires 80% shares of company S Ltd. (S) on 1/10/17 by issue of equity shares at fair value of 440, paid up value 100. Non-Controlling Interest (NCI) should be measured at proportionate Net Assets. The total comprehensive income of P and S in the year amounted to 120 and 140 respectively. The extracts from balance sheets at book values and at fair values at the date of acquisition and at 31-03-2018 are stated below. (Rs. Lakhs)

	On 1-10-17			On 31-3-18	
	P	S	FV of S	P	S
PPE	680	440	700	720	500
Investment in shares of Q				440	
Current Assets	420	360	320	500	400
Total Assets	1100	800		1660	900
Current Liability	300	200	200	340	220
Noncurrent Liability	300	300	300	320	310
Total Liabilities	600	500		660	530

Equity structure of the companies:

	P		S	
	on 01-04-2017	On 31-03-2018	on 01-04-2017	On 31-03-2018
Equity Share Capital	200	300^{x}	100	100
Other Equity	240	700^{x}	130	270

Prepare CBS on 01-10-2017 and on 31-03-2018.

Solution: Working Notes:

1. Analysis of profits of Q:	Pre-acquisition	Post-acquisition
Other Equity on 01-04-2017	130	
Revaluation Profit/Loss (260-40)	220	

Profits during the year	140	
50%*140 pre and 50% post	70	70
Revaluation loss on current asset reverted		40[z]
Other Equity on 01-10-2017	**420**	**110**
Share of P 80%		88[@]
Share of NCI 20%		22[@]

2. Net Assets of Q at Fair Value represented by Equity Share Capital + Pre-acquisition Profits (Other Equity at acquisition):

Equity Share Capital	100
Other Equity on 01-10-2017	420
Net Assets	**520**

3. NCI at acquisition = 20%* 520= 104[$]

4. Goodwill = Purchase Consideration + NCI – Net Assets = 440 + 104 – 520 = 24[#]

Consolidated Balance Sheet of P Ltd. and its subsidiary S Ltd as on 1-10-17

	Workings	(Rs. Lakhs)
PPE	680+700	1380
Goodwill		24#
Current Assets	420+320	740
Total Assets		**2144**
Equity Share Capital	(200+100)	300
Other Equity on 1-10-17	(240+60+340)	640
NCI		104[$]
Noncurrent Liability	300+300	600
Current Liability	300+200	500
Total of Equity and Liabilities		**2144**

Consolidated Balance Sheet of P Ltd. and its subsidiary S Ltd. as on 31-3-18

	Workings	(Rs. Lakhs)
PPE	720+500 +260	1480
Goodwill		24[#]
Current Assets	500+400-40+40[z]	900
Total Assets		**2404**
Equity Share Capital		300[x]
Other Equity	700[x] + 88[@]	788
NCI	104[$] + 22[@]	126
Noncurrent Liability	320+310	630
Current Liability	340+220	560
Total of Equity and Liabilities		**2404**

GROUP: 4, PAPER: 18

INDIRECT TAX LAWS & PRACTICE (ITP)

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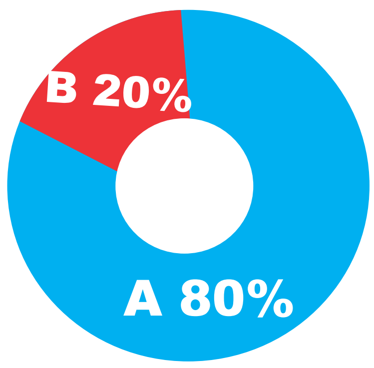
Your Preparation Quick Takes



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

Learning objectives:

After studying this section, you will having an understanding of:

- Determination of Time of Supply of services under Default Rule/ Forward Charge;
- Illustrations on Time of Supply under Forward Charge when invoice is issued within time limit;
- Illustrations on Time of Supply under Forward Charge when invoice is not issued within time limit.

INDIRECT TAX LAWS & PRACTICE
ILLUSTRATIONS OF 'TIME OF SUPPLY' OF SERVICES UNDER FORWARD CHARGE UNDER GST LAW

Introduction

- Time of supply means the point in time when goods/services are considered supplied. It helps in the determination of the date when the event which gives rise to GST liability has occurred. The liability to pay tax on services shall arise at the time of supply, as determined in accordance with the provisions of Sec. 13 of the Central Goods and Services Tax Act, 2017.
- Sec. 13(1) states that the liability to pay tax on services shall arise at the time of supply.
- As per the provisions of the GST, time of supply for services can be classified into three broad categories:
  - Time of Supply for Services – Forward Charge
  - Time of Supply for Services – Reverse Charge
  - Time of Supply for Services – Miscellaneous Provisions

In the following sections we discuss some of the illustrations on time of supply of services under forward charge situations:

Illustration for determining Time of supply of services (Forward Charge/ Default Rule)

- Forward charge refers to the situation in which the buyer of goods pays the taxes to the supplier of the goods, and the supplier, in turn, remits the said taxes to the tax authority.
- According to Sec. 13(2) of the Central Goods and Services Tax Act, time of supply of services is ascertained as follows:

A] When invoice is issued by supplier of service within the period prescribed u/s 31(2)

The time of supply shall be the earlier of the following dates:

- Date of issue of invoice by supplier of service; or
- Date of receipt of payment.

Illustration 1: Time of Supply under Forward Charge – Invoice issued within time limit

Ms. Aruna Ltd. provides pest control services worth Rs 18,000 to Mr. Barun on July 1, 2019. The invoice was issued on July 5, 2019 and the payment for the same was received by Ms. Aruna Ltd. on August 1, 2019.

Here, Date of issue of invoice is July 25, 2019 and Date of receipt of payment is August 1, 2019.

Firstly it is to be checked whether the invoice has been issued within the specified statutory time limit or not. The prescribed time is 30 days from the date of supply i.e. July 31, 2019 in this case. The invoice was issued on July 5, which happens to be within the specified statutory time limit.

We know, in case of forward charge, Time of supply is earliest of the following two dates:

a) Date of issue of invoice = July 5, 2019; or

b) Date of receipt of payment = August 1, 2019.

Therefore, in this case the time of supply happens to be the Date of issue of invoice i.e. July 5, 2019.

B] When invoice is not issued by supplier of service within the period prescribed u/s 31(2)

This case arises when a service is rendered first, and the on the basis of an authorised person's (like service engineer, site supervisor etc.) report, the company issues the tax invoice. In such a case, the time of supply shall be the earlier of the following dates:

- Date of provision of service; or
- Date of receipt of payment.

Illustration 2: Time of Supply under Forward Charge – Invoice issued beyond time limit

M/s Sharma Bros., a cleaning agency provides cleaning services to Jagannath Warehouses Ltd. for cleaning their godown which was lying unused for long-time. The service provider was unable to quote the exact consideration for the cleaning service and it was agreed between the two parties that the final consideration will be decided after the execution of the full job. The cleaning services were rendered to Jagannath Warehouses Ltd. on June 11, 2019. The invoice was issued on July 14, 2019 and the payment for the same was received in full by M/s Sharma Bros. on August 1, 2019.

Here, Date of provision of service is June 11, 2019, Date of issue of invoice is July 14, 2019 and Date of receipt of payment is August 1, 2019.

Firstly it is to be checked whether the invoice has been issued within the specified statutory time limit or not. Clearly, in this case, the invoice has not been issued within the prescribed time limit of 30 days from the date of supply. The invoice was issued on July 14, which happens to be beyond the specified statutory time limit.

We know, in case of forward charge, where the invoice is issued beyond the specified time limit of issue, time of supply of service is earliest of the following two dates:

a) Date of provision of service = June 11, 2019; or

b) Date of receipt of payment = August 1, 2019.

Therefore, in this case the time of supply happens to be the Date of provision of service i.e. June 11, 2019.

Illustration 3: Time of Supply under Forward Charge – Invoice issued beyond time limit

M/s Gupta Bros., a cleaning agency provides cleaning services to Tirupati Warehouses Ltd. for cleaning their godown which was lying unused for long-time. The service provider was unable to quote the exact consideration for the cleaning service and it was agreed between the two parties that the final consideration will be decided after the execution of the full job. The cleaning services were rendered to Tirupati Warehouses Ltd. on June 5, 2019. The invoice worth `1,25,000 was issued on July 10, 2019. As per agreement between the two parties, `20,000 was received in advance on June 3, 2019 and balance was received by M/s Sharma Bros. on August 1, 2019.

Here, Date of provision of service is June 5, 2019, Date of issue of invoice is July 10, 2019 and Dates of receipt of payments are June 3, 2019 and August 1, 2019.

Firstly it is to be checked whether the invoice has been issued within the specified statutory time limit or not. Clearly, in this case, the invoice has not been issued within the prescribed time limit of 30 days from the date of supply. The invoice was issued on July 10, which happens to be beyond the specified statutory time limit.

We know, in case of forward charge, where the invoice is issued beyond the specified time limit of issue, time of supply of service is earliest of the following two dates:

a) Date of provision of service; or

b) Date of receipt of payment.

In this case, there are two dates of payment and as such, the time of supply in each case will be as under:

For payment received on June 3, 2019				For payment received on August 1, 2019			
Date of provision of service	Date of issue of invoice	Date of Receipt of Payment	Time of Supply of service	Date of provision of service	Date of issue of invoice	Date of Receipt of Payment	Time of Supply of service
June 5	July 10	June 3	June 3	June 5	July 10	August 1	June 5

150 YEARS OF CELEBRATING THE MAHATMA

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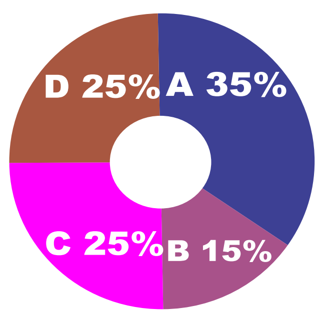
GROUP: 4, PAPER: 19

COST & MANAGEMENT AUDIT (CMAD)

Your Preparation Quick Takes



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

COST AND MANAGEMENT AUDIT

COST AUDIT DOCUMENTATION AND AUDIT PROCESS.

Cost Audit Documentation means the records, in physical or electronic form, including working papers prepared /obtained and retained by the cost auditor, in connection with the performance of the audit. Cost Audit relies on analytical review and substantive testing to establish true and fair view.

THE STAGES OF AUDIT OF COST STATEMENT ARE:

1) Planning stage
2) Performing on Execution stage ,
3) Concluding and reporting stage.

Such stages along with functions are detailed below:

1) Planning stage

Determine audit Strategies

Identify nature and timing of the procedure to the followed.

Gather sufficient appropriate evidence to minimize risk of material mis-tatement at the cost- statement level.

2) Performance or Execution stage

Detailed testing of internal controls, material consumptions, cost accumulation, allocation, apportionment and absorption.

Detailed substantive tests provides the evidence which help auditor to determine whether the cost statements are fairly presented.

3) Concluding and Reporting stage

Auditor arrives at an opinion regarding the fair presentation of the cost statements.

Taking into account the entity's controls, transactions, cost heads, item of cost, related disclosure, understanding of the client reg. risk faced by them etc. the auditor draws conclusion and forms an opinion for expressing the same in cost audit report.

Practical Steps of audit Process:

Step – I: Audit objectives and outlook of management

At the very outset, the purpose of the audit must be made clear; whether the audit is going to meet statutory requirements only or to satisfy certain expectation of management from the audit, such as

- Cost optimization or cost reduction
- Product diversification or change of product mix.
- Identifying profit making or loss making products
- Market expansion or market diversification, and so on.

Step –II: Understanding of the pre-conditions of audit which may be as follows.

- Objectives of cost audit
- Area, nature and scope of audit
- Reporting framework and reporting period.
- Statutory deadlines.

Management's awareness of the scope of work and responsibiliting for the following functions including maintenance of records to facilitate audit works.

Cost records	Maintenance thereof as required.
Cost Statements	Preparation and presentation in compliance with cost accounting standards.
Accounting Policies	Selection and consistent application thereof.
Books of accounts, vouchers, cost records, documents, other records and information which are relevant for preparation of cost statements	Allowing access to the auditor.

Having an understanding of the pre-conditions of an audit, the auditor and the auditee decides the audit fees and payment schedule. Finally the cost auditor gets an engagement letter.

Step –III: Understanding of the Companies' Business. It entails the following.

- Corporate structure and various systems followed.
- Details of Company – Its size, nature of activity, product profile, unit locations, owner ship structure etc.
- Nature of industry which the company is operating in .
- Applicable frameworks reg. regulations, financial reporting, Cost reporting etc.
- Production Process, joint or by products, outsourcing of any
- Subsidiaries, associates and joint ventures
- Key personnel belonging to each department viz. Finance, Accounts, Costing, IT, Administration, production, purchase, sales etc.
- Policies reg. purchase, sales, pricing, expert, import etc.
- Inventory- receipt, issue, storage, physical verification etc.
- Related parties- nature of transition with them
- Indirect tax structure – as applicable

Following systems should be given due importance.

- Internal control system followed by the company
- Internal Audit System – Scope, adequacy, coverage, effectiveness.
- Accounting System and policies followed by the company.
- Cost Accounting System followed by the company.
- MIS, risk identification and management system.
- IT architecture relevant to Financial/cost accounting.

Last but not the least, previous auditor's report should be thoroughly gone through.

Step –IV: Planning the audit

Its coverage is wide enough to include the following.

- Audit period – Timing (dates) and duration (no. of days)
- Audit personnel – Level and number of personnel to be deployed including supervision and review of work done by the audit term.
- Audit partner – Deployment with expected days & dates,
- Overall Audit plan and strategy – This will act as guide to the audit team.
- Materiality & sampling level- To be decided upon.
- Audit procedures – Appropriate formulation thereof
  - Substantive procedure
  - Analytical procedure
  - Test of controls
  - Risk assessment strategies and procedures i. e. the methodology to measure material mis-statements.

- Planning for Discussion with
  - Key personnel of the company
  - Previous cost auditor
  - Statutory financial auditor and
  - Internal auditor

- Documentation of the audit plan that should be shared with the company.
- Adherence to the guidance manual for Audit Quality. It should be ensured during audit.

Step –V: Execution of Audit

- Perform the audit checks and procedure as planned
- Collect all required audit evidences ennobling the auditor to form his opinion. In regard to evidences, the auditor has to
  - Validate their relevance and reliability
  - Check their accuracy, completeness and sufficiency.
  - Check out the source and consistency.
- Preparation of draft observation and discussion with key management personnel.
- Preparation of Final Audit Report.

Step –VI: Audit documentation

- Documentation consists of the following
  - Audit plan, audit strategy
  - Working papers
  - All the audit evidences obtained/collected.
  - Draft observations and discussions.
  - Final Audit report.
- Preservation of documents in a bound folder/file for the prescribed period.

GROUP: 4, PAPER: 20

STRATEGIC PERFORMANCE MANAGEMENT AND BUSINESS VALUATION (SPBV)

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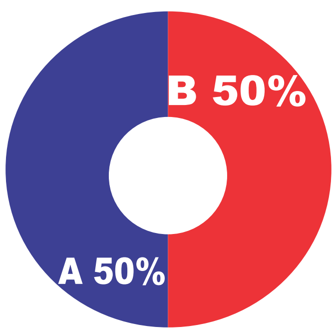
Your Preparation Quick Takes



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

Strategic Performance Management and Business Valuation

H Model

The H model was proposed by Fuller and Hsia and it is also a Two-stage model for growth. This model assumes that earnings growth rate starts at a high initial rate (g_a) and declines linearly during the extraordinary growth phase (which is assumed to last 2H period) and reaches to the stable growth rate (g_n) in steady state. The dividend payout and cost of equity are assumed to be constant overtime and are not affected by the shifting growth rates.

Illustration
The dividend per share of an equity share of XY Ltd. is Rs 6. The present growth rate is 60%. However, this will decline linearly over a period of 12 years and then stabilize at 15%. What is the intrinsic value per share of XY Ltd. if required rate of return is 18%?

Solution
Since high initial growth rate declines linearly during extraordinary growth phase and then reaches to the stable growth rate in steady state, H model is appropriate to value the equity share. According to H model, the intrinsic value of equity share will be:

$$P_0 = \frac{D_0(1+g_n)}{k - g_n} + \frac{D_0.H.(g_a - g_n)}{(k - g_n)}$$

Where,

D_0 = Rs6
G_a = 60%
2H = 12 years; i.e., H = 6 years
g_n = 15%
k = 18 %.

$$P_0 = \frac{6(1+0.15)}{0.18 - 0.15} + \frac{6 \times 6 \times (0.60 - 0.15)}{0.18 - 0.15}$$

$$= \frac{6 \times 1.15}{0.03} + \frac{36 \times 0.45}{0.03}$$

= Rs 230 + Rs540
= Rs 770

Three Stage Growth Model
The three-stage growth model combines the features of the two stage model and H model. This model assumes that there are three phases of growth pattern – an initial stage of stable high growth, a second phase of declining growth and a third phase of stable low growth that lasts forever. The value of the share under this model is given by

$$P_0 = \underbrace{\sum_{t=1}^{n_1} \frac{EPS_0(1+g_a)^t . \pi_a}{(1+k_{hg})^t}}_{\text{High-growth rate}} + \underbrace{\sum_{t=n_1+1}^{n_2} \frac{DPS_t}{(1+k_t)^t}}_{\text{Transition}} + \underbrace{\frac{EPSn_2(1+g_n).\pi_n}{(k_{st}-g_n)(1+k_{st})^n}}_{\text{Stable growth phase}}$$

Where, EPSt = Earnings per share in years t

DPSt = Dividends per share in year t

g_a = Growth rate in high growth phase (lasts n_1 periods)
g_n = Growth rate in stable phase
π_a = Payout ratio in high growth phase
π_n = Payout ratio in stable growth phase
k_{hg}, k_t, k_{st} = Required rate of return in high growth (hg), Transition (t) and stable growth (st) respectively.

Illustration

For the first four years X Ltd. is assumed to grow at a rate of 10 per cent. After four years the growth rate of dividend is assumed to decline linearly to 6 per cent. After 7 years, the firm is assumed to grow at a rate of 6 per cent infinitely. The next year dividend is Rs. 2 and the required rate of return is 14 per cent. Find out the value of the stock.

Solution

The value of the share under three stage growth model is given by

$$P_0 = \sum_{t=1}^{n_1} \frac{DPS_0(1+g_a)^t.}{(1+k_{hg})^t} + \sum_{t=n_1+1}^{n_2} \frac{DPS_t}{(1+k_t)^t} + \frac{DPSn_2(1+g_n).\pi_n}{(k_{st}-g_n)(1+k_{st})^n}$$

Where, $DPS_0 = 2$

DPSt = Dividends per share in year t

g_a = Growth rate in high growth phase (lasts n_1 periods) = 0.10

g_n = Growth rate in stable phase = 0.06

Growth rate of dividend is assumed to decline linearly to 6 per cent after 4th year i.e., 10% to 6%.

k_{hg}, k_t, k_{st} = Required rate of return in high growth (hg), Transition (t) and stable growth (st) respectively.
= 0.14

Now

$$\sum_{t=1}^{n_1} \frac{DPS_0(1+g_a)^t.}{(1+k_{hg})^t} = (2/\ 1.14) + (2 \times 1.1)\ /\ (1.14)^2 + \{(2 \times (1.1)^2\ \}/\ (1.14)^3 + \{(2 \times (1.1)^3\ \}/\ (1.14)^4$$

$$= 1.754 + 1.693 + 1.633 + 1.576 = \text{Rs. } 6.656$$

$$\sum_{t=n_1+1}^{n_2} \frac{DPS_t}{(1+k_t)^t} = \{2\ (1.1)^3(1.09)\}/\ (1.14)^5 + \{2\ (1.1)^3(1.09)(1.08)\}/\ (1.14)^6 + \{2\ (1.1)^3(1.09)(1.08)(1.07)\}/\ (1.14)^7$$

$$= \text{Rs. } 4.2746$$

$$\frac{DPSn_2(1+g_n).\pi_n}{(k_{st}-g_n)(1+k_{st})^n} = \{2\ (1.1)^3(1.09)(1.08)(1.07)\ (1.06)\}/\ (0.14 - 0.06)(2.5023)$$

$$= 3.554/0.2001 = \text{Rs. } 17.7611$$

Thus, P_0= Rs. (6.656 + 4.2746+17.7611) = Rs. 28.69

PRACTICAL Advice

ABOUT YOUR STUDIES - FINAL COURSE

Practical support, information and advice to help you get the most out of your studies.

START

01 Read Study Notes
MTPs, E-Bulletin
Work Books
Webinar seasons

02 Solve Excercises given in Study Note

03 Assess Yourself

04 Appear For Examination

FINISHED

SUBMISSION

Dear Students,

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

We have noted your 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.

Updation of E-Mail Address/Mobile:

Students are advised to update their E-Mail id and Mobile Numbers timely so that important communications are not missed as the same are sent through bulk mail/SMS nowadays. Student may update their E-Mail id/ Mobile Number instantly after logging into their account at www.icmai.in at request option.

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

Message from

Directorate of Studies

Dear Students,

We from the Directorate of studies know your expectations from us and accordingly we are trying to delivery some meaningful tips through the publications of monthly E-bulletins. Other than this we are trying to help you through, Mock Test Papers (MTPs), Work Book, and we have conducted Webinar sessions. Before stepping in to the examination hall, please go through the PPTs on "Achieve your GOAL"; Uploaded by the Directorate of Studies and which will help you to know about certain Do's and Don'ts in the examination.

You know that the nation is celebrating 150th birth anniversary of the father of the nation **M.K. Gandhi**. One of his inspirational message towards the students were:

"Whatever you do will be insignificant. But it is very important that you do it",

Let us observe his memory by following his message.

Certain general guidelines are listed below and which will help you in preparing yourselves:

- Conceptual understanding & Overall understanding of the subject should be clear.
- Candidates are advised to go through the study material provided by the Institute in an analytical manner.
- Students should improve basic understanding of the subject with focus on core concepts.
- The Candidates are expected to give to the point answer, which is a basic pre-requisite for any professional examination.
- To strengthen the answers candidates are advised to give answer precisely and in a structured manner.
- In-depth knowledge about specific terms is required.
- Write question numbers correctly and prominently.
- Proper time management is also important while answering.

Please refer the links mentioned below :

For Mock Test Papers (MTP) : **https://icmai.in/studentswebsite/mtp2016_j19_Final.php**

For PPT on "Achieve your GOAL : **http://icmai.in/studentswebsite**

For Work Book Link : **https://icmai.in/studentswebsite/Workbook-Syl-2016-Final-March2019.php**

Live/Recorded Webinar Link : **https://eicmai.in/Webinar_Portal/Students/StudentLogin.aspx**

Ebulletin Link : **https://icmai.in/studentswebsite/E-Bulletin.php**

We are sure that you will be motivated after looking into the placement news of our students' appeared in the Times of India, newspaper.

GOOD LUCK & Best wishes.

Be Prepared and Get Success;

Few Snapshots

Election of CMA Balwinder Singh as President and CMA Biswarup Basu as Vice-President of the Institute.

CMA Balwinder Singh, President along with CMA Vijender Sharma, Council Member of the Institute welcomes Ms. Lucia Real-Martin, Lead Market Director, Association of Chartered Certified Accountants (ACCA) on 28th August 2019 at CMA Bhawan, New Delhi.

Glimpses of SAFA Foundation Day Conference on the theme "Emerging Challenges and Opportunities for Professional Accountants in South Asia" organised by the Institute on 22nd August 2019 at Hyderabad.

Glimpses of SAFA Foundation Day Conference on the theme "Emerging Challenges and Opportunities for Professional Accountants in South Asia" organised by the Institute on 22nd August 2019 at Hyderabad.

Launching SAP - FICO Course during the meeting of the Council of the Institute on 21st August 2019 at Hyderabad.

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THE INSTITUTE OF COST ACCOUNTANTS OF INDIA

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