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150 YEARS OF CELEBRATING THE MAHATMA

e Bulletin

FINAL

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Behind every successful business decision, there is always a CMA

Message from

The Chairman

CMA Manas Kumar Thakur

Chairman,
Training & Education Facilities (T& EF) Committee

CMA MANAS KUMAR THAKUR
Chairman, T & EF Committee
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MESSAGE FROM THE CHAIRMAN

Dear Students,

Greetings,
"By education, I mean an all-round drawing of the best in child and man in body, mind and spirit" –M.K.Gandhi.

On the eve of commemorating 150 th birth anniversary of Mahatma Gandhi by the Government of India, let us try to believe in line of his thinking that there is someone or something higher than you. You don't need to believe in God, but believing that everyone is equal and you are no less or more than someone else. It is knowing your values, ethics and morals. Faith is not following others blindly especially when someone else is doing something that your heart says is not right.

Mohandas Karamchand Gandhi; father of the nation, lived in India during the '30s and '40s when he was following certain principles. We live in a society and amongst a generation that has a lot more technology, is more materialistic and we are not fighting for the same reasons (we have 'freedom'(opportunities to do what we want to do)).

I have full faith on you and I strongly believe that you can contribute to the development of 'Make in India'. I am very much thankful to the academicians and industry experts for engaging their valuable timing and to help in your preparation. Despite their individual other commitments, they are trying to provide you important tips and trying to help you to make your preparation better.

The Directorate of Studies is assisting in your preparation by providing you various kinds materials and supports in the forms of Revisionary Test Papers (RTPs), Mock Test Papers (MTPs), Work Book along with all the recent amendments in papers related to Direct and Indirect taxation, Laws, Accounting etc. and also have arranged for live Webinar session through which you may directly interact with the faculties and clear your doubts. Prior preparation is required to make the Webinar more live and vibrant and which in turn may help you to resolve your problems. Try to grab the opportunities and make yourself prepare to face the challenges, afterwards.

December,2018 term of examination will be held soon. On my personal behalf I want to tell you that **stay positive, work hard and make it happen. Don't stress. Put your best and forget the rest at least for the time being.**

"Persistent questioning and healthy inquisitiveness are the first requisite for acquiring learning of any kind"-M. K. Gandhi.

Wishing you Good luck on your examination,

CMA Manas Kumar Thakur

Be a CMA, be a Proud Indian

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

STUDENTS' E-bulletin Final
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150 YEARS OF CELEBRATING THE MAHATMA

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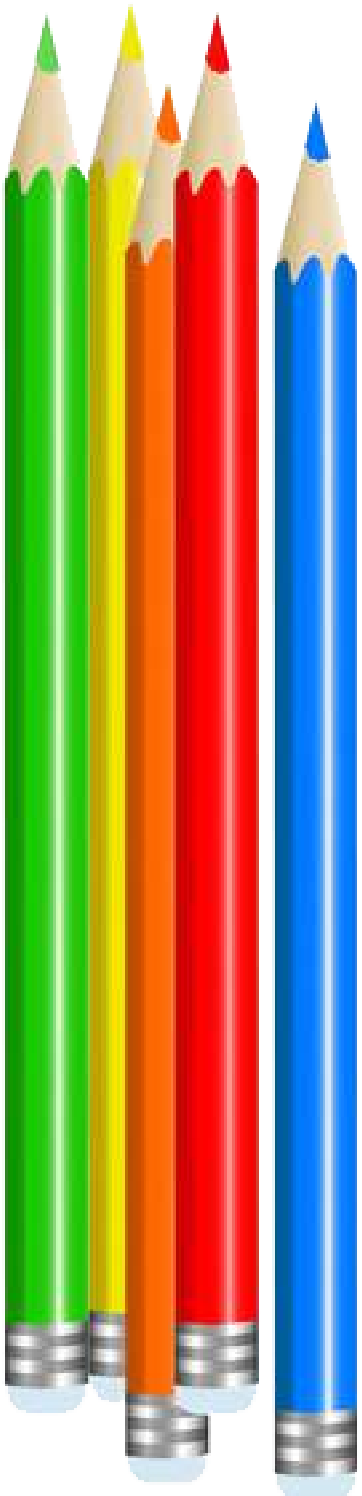

KNOWLEDGE Update

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, PAPER: 13

CORPORATE
LAWS & COMPLIANCE (CLC)

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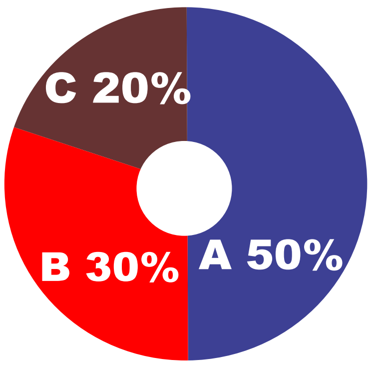
Your Preparation Quick Takes



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.

ACCOUNTS, AUDITS AND DIVIDEND

1.0 ACCOUNTS:

Accounts are record of financial transaction of a company and needs to be finalised every year for a particular period commonly known as "accounting period". As per Companies Act, all companies shall follow an accounting year commencing from 1st April to 31st March.

1.1 The proper books of account.

Every company shall maintain proper books of accounts which must satisfy the following:

True and fair view should be recorded.

(i) Accrual basis accounting: the income and expenditure should relate to particular period year even when they are received paid in the same year.
(ii) Shall exhibit and explain the financial position.
(iii) These shall disclosure relating to goods, i.e. goods sold, purchased etc.
(iv) Shall be prepared in ink and not in pencil.
(v) Shall be as per the accounting standard prescribed by the Central Government. It may be mentioned that Central Govt. has the power to prescribe accounting standards i.e. all companies should have uniform method of interpretation and calculation of profit valuation of assets, depreciation etc. Presently the standards issued by the Institute of Chartered Accountants of India is the applicable accounting standards.
(vi) Shall be kept in electronic form also.

1.2 Keeping of books of account :

Books of accounts may be kept at the registered office of the company or any other place(s) in India as decided by the Board of Directors. The company shall within 7 days file with the Registrar a notice in writing giving the full address of the place. If the company has any branch office within or outside India proper returns of such branch offices shall be sent periodically to head office.

1.3 Contents of books of account.

As per section 128 of the Companies Act, 2013, every company shall keep proper books of account in respect of the following:

(i) All receipts and expenditures made by the company.
(ii) The sale and purchase of the goods by the company.
(iii) The assets and liabilities of the company.
(iv) If the company is engaged in manufacturing, processing, production or mining activities the cost accounting records as prescribed by the Central Govt.

1.4 Consolidation of Accounts:

As per section 129(3) of the new Act, Every company having more than one subsidiary shall prepare a consolidated financial statement of the company with all its subsidiaries in the same form and manner as that of its own which shall also be laid in the before the annual general meeting of the company along with the standalone financial statement of the company. The consolidated financial statement should contain the financial information relating to its subsidiaries, its associates companies and its joint ventures. The consolidated financial statement should be in Form AOC-1.

1.5 Annual accounts and legal requirements (Section 129 and 130)

(1) **Laying of annual accounts in the AGM:** A balance sheet as at the end of the financial year and a profit and loss account along with the cash flow statement and statement showing changes in equity of the company for the financial year shall be laid before the AGM for the approval and adoption of the shareholders. Along with financial Statements consolidated financial statements of all the subsidiaries including Associate Companies and joint ventures of the company shall be laid before the Annual General Meeting.
(2) The Forms and contents of the financial statements will be as per Schedule III.

1.6 Authentication of Balance sheet and Profit & loss account (section 134)

As per the new Companies Act, 2013 all the financial statements including the consolidated financial statement shall be required to be signed by the following persons:

(i) By the Chairperson of the Company, where he is authorised by the Board.
(ii) By two Directors out of which one shall be Managing Director, if any.
(iii) Chief Financial Officer and Company Secretary of the Company, if required.

1.7 Circulation of Annual accounts (section 136)

The company shall send the copies of the financial statements including consolidated financial statements to the members and every trustee for the debenture holder. In addition to the above the company is required to place its financial statements including consolidated financial statements, if any, and all other documents required to be attached, thereto on the website of the company.

Further every company is also required to place separate audited accounts in respect of each of its subsidiary, if there is any.

Every company is required to keep its financial statements at the registered office of the company for inspection by any member and debenture trustee during business hours. A listed company may send only the salient features of the documents and keep the document for inspection as above.

1.8 Filling of Financial Statements (including consolidated financial statements) with Registrar of Companies (section 137)

(a) within 30 days of Annual General Meeting.

(b) If AGM is not held within 30 days of the day on which the AGM is ought have been held. The Registrar shall take on record the un-adopted financial statements as provisional statements till the accounts are adopted in the Annual General Meeting.

(c) If the AGM held but the annual accounts are not prepared on that date the AGM shall be adjourned till the accounts shall prepared but such adjournment shall not be beyond the statutory period of AGM i.e. 18 months.

(d) If the AGM is held but did not approve the annual accounts the accounts shall be filed within 30 days of the AGM specifying the reason of disapproval.

(e) One person company shall file its financial statements along with all its necessary documents required to be attached with its financial statements to the registrar within 180 days of the closure of financial Year.

(f) As per the new Act every company from now on shall attach financial statements of each of its subsidiary which are established outside India and do not have any place of business in India.

1.9 Accounts of Holding and Subsidiary companies :

Along with the balance sheet of the holding company the following documents of the subsidiary company shall be attached:

(a) a copy of the balance sheet, profit & loss account, director's report.

(b) A copy of the auditor's report.

© A statement of the holding company's interest in the subsidiary.

GROUP: 3, PAPER: 14
STRATEGIC FINANCIAL MANAGEMENT (SFM)

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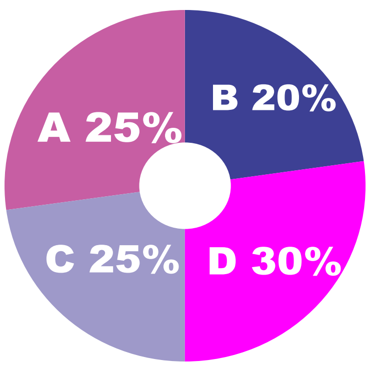
Your Preparation Quick Takes



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

Behind every successful business decision, there is always a CMA

Learning objectives:

After studying this section, you will be able to apply simulation technique for assessing risk in capital budgeting decision

Strategic Financial Management

Example

X Co. is evaluating an investment proposal which has uncertainty associated with the three important aspects: original cost, useful life and annual net cash flows. The three probability distributions for these variables are shown below:

Original Cost		Useful life		Annual net cash inflows	
Value	Probability	Period	Probability	Value	Probability
Rs. 60,000	0.30	5 years	0.40	Rs. 10,000	0.10
Rs. 70,000	0.60	6 years	0.40	Rs. 15,000	0.30
Rs. 90,000	0.10	7 years	0.20	Rs. 20,000	0.40
				Rs. 25,000	0.20

The company wants to perform five simulation runs of this project's life. The firm's cost of capital is 15% and the risk-free rate is 6%; for simplicity it is assumed that these two values are known with certainty and will remain constant over the life of the project.

To simulate the probability distribution of original cost, useful life and annual net cash inflows, are the following are the sets of random numbers:

09, 84, 41, 92, 65; 24, 38, 73, 07, 04; and 07, 48, 57, 64, 72 respectively each of the five simulation runs.

Solution

To simulate the probability distribution corresponding to original cost, useful life and annual net cash inflows, we assign an appropriate set of random numbers as shown in the following table:

Original Cost

Value	Probability	Cumulative Probability	Random Numbers
1,20,000	0.30	0.30	00-29
1,40,000	0.60	0.90	30-89
1,80,000	0.10	1.00	90-99

Useful Life

Period	Probability	Cumulative Probability	Random Number
6	0.40	0.40	00-39
7	0.40	0.80	40-79
8	0.20	1.00	80-99

Net Cash Inflows

Value (Rs.)	Probability	Cumulative Probability	Random Probability
20,000	0.10	0.10	00-09
30,000	0.30	0.40	10-39
40,000	0.40	0.80	40-79
50,000	0.20	1.00	80-99

The five simulation runs are now performed and the results are tabulated below:

Simulation Worksheet

Simulation Run	Original Cost		Useful life		Annual net cash inflows	
	Random Number	Value (Rs.)	Random Number	Period (years)	Random Number	Value (Rs.)
1	09	1,20,000	24	6	07	20,000
2	84	1,40,000	38	6	48	40,000
3	41	1,40,000	73	7	57	40,000
4	92	1,80,000	07	6	64	40,000
5	65	1,40,000	04	6	72	40,000

Now let us calculate NPV for run 1 to run 5.

Run 1

(1)Period	(2) Cash flows	(3)PV factor @ 6%	Present Value (4)= (2) x (3)
0	-1,20,000	1.000	-1,20,000
1	20,000	0.943	18,860
2	20,000	0.890	17,800
3	20,000	0.840	16,800
4	20,000	0.792	15,840
5	20,000	0.747	14,940
6	20,000	0.705	14,100

Net Present Value = Rs. 21,660

Run 2

(1)Period	(2) Cash flows	(3)PV factor @ 6%	Present Value (4)= (2) x (3)
0	-1,40,000	1.000	-1,40,000
1	40,000	0.943	37,720
2	40,000	0.890	35,600
3	40,000	0.840	33,600
4	40,000	0.792	31,680
5	40,000	0.747	29,880
6	40,000	0.705	28,200

NPV = Rs.-56,680

Run 3

Period	Cash flows
0	-1,40,000
1	40,000
2	40,000
3	40,000
4	40,000
5	40,000
6	40,000
7	40,000

Therefore, NPV = (40,000 x PV of annuity factor for 7 years @ 6%) – 1,40,000
= (Rs. 40,000 x 5.582) – Rs. 1,40,000
= (Rs. 2,23, 280 – 1,40,000) = Rs. 83,280

Run 4

Period	Cash flows
0	-1,80,000
1	40,000
2	40,000
3	40,000
4	40,000
5	40,000
6	40,000

Therefore, NPV = (40,000 x PV of annuity factor for 6 years @ 6%) – 1,80,000
=Rs. (40,000 x 4.917) – Rs. 1,80,000
= Rs. 1,96,680 – 1,80,000 = Rs. 16, 680

Run 5

Period	Cash flows
0	-1,40,000
1	40,000
2	40,000
3	40,000
4	40,000
5	40,000
6	40,000

Therefore, NPV = (Rs.40,000 x PV of annuity factor for 6 years @ 6%) – Rs.1,40,000
=Rs. (40,000 x 4.917) – Rs. 1,40,000
=Rs. (1,96,680 – 1,40,000) =Rs. 56680

YEARS OF CELEBRATING THE MAHATMA

GROUP: 3, PAPER: 15

STRATEGIC COST MANAGEMENT- DECISION MAKING (SCMD)

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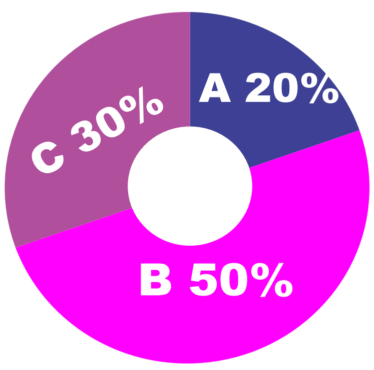
Your Preparation Quick Takes



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?

An important technique of Cost Reduction

01.00 Concept

Value Analysis (VA) is one of the important techniques of cost reduction and control. It is a scientific approach that ensures all the functions of a product or service are carried out at the minimum cost without compromising quality, reliability, performance and appearance.

Society of American Value Engineers (SAVE) states "Value analysis is the systematic application of recognised techniques which identify the function of a product or service to establish a monetary value for the function and to provide the necessary function reliability at the lowest overall cost."

02.00 Value Matrix

Value analysis is a methodical approach to sharpening the efficiency and effectiveness of any process. Value, in the context of value analysis, refers to economic value, which may reflect:

> Value =
>
> Quality, performance, style, design and cost in relation to a product or service

(i) Use value
(ii) Cost value
(iii) Exchange value, or
(iv) Esteem value.

'Use Value' reflects the intrinsic value. It is the measure of properties, qualities and features which make the product or service useful for the consumer. Use value, therefore, is the price paid by the buyer or the cost incurred by the manufacturer in order to ensure that the product or service performs its intended function efficiently.

'Cost Value' is the sum of all costs incurred in producing the product or rendering a service. Cost value, thus, is the sum of raw material cost, labour cost, and overheads expended to produce the product or service.

'Exchange Value' is the measure of all the properties, qualities and features of the product or service which make the product or service possible of being traded for another product or service or for money. In a conventional sense, 'exchange value' refers to the price that a purchaser is willing to offer for the product or service, the price being dependent upon the satisfaction level that is derived from the product or service.

'Esteem Value' is the measure of properties, features, attractiveness graphic packaging and the like which increases sales appeal or which attracts customers and create in them a strong desire to own the product. "Esteem value", therefore, is the price paid by the buyer or the cost incurred by the manufacturer beyond the use value. It is the perception value.

Use value may be construed as the fundamental form of economic value. An item without use value can have neither exchange value nor esteem value. Summing up it may be stated that value is: quality, performance, style, design and cost in relation to a product or service.

03.00 Value Equation

Value analysis aims to simplify products and process, thereby increasing efficiency. Value analysis enables people to contribute towards value addition by continuous focus on product design and services. Value analysis provides a structure through initiatives in the direction of cost saving, cost reduction and continuous improvement.

Value Equation:
Value = (Performance + Capability)/Cost = Function/Cost

Value addition is not a matter of, just, minimizing the cost. It is a 3D technique. Value can be increased either by increasing function or reducing the cost or by doing both simultaneously. The concept is that of adding value by enhancing the functional worth

Any attempt to improve the value of a product must consider two elements. The first element is the utility of the product, i.e. the use value. The second element relates to the value of ownership, i.e. esteem value.

The concept can, better, be explained by the price discrimination being practiced in relation to a luxury car and a basic small car. From the use point of view both the cars fulfil the same function, viz. both of them offer safe economical travel (use value); but the luxury car has a greater esteem value and hence priced at a phenomenal value.

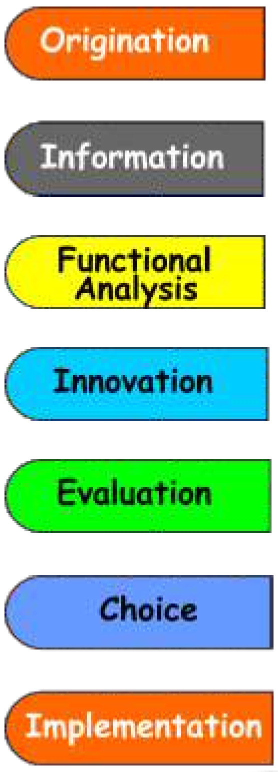
Another example could be the exorbitantly priced gold-plated ball pen in comparison to a disposable pen. Even though the use value for both the pens is nearly the same, the factor of esteem value enables a privileged pricing for gold-plated ball pen.

04.00 Phases of Value Analysis

Value Analysis may consist of the following seven phases.

(i) **Origination:** The phase of origination starts with the identification of a project to undertake value analysis. After selecting the project, a project team consisting of experts from various fields and departments is constituted.

(ii) **Information:** The second phase is that of collecting relevant information. In this phase, the relevant facts relating to specifications, drawings, methods, materials, etc. are collected. Costs are, also, ascertained for each of the elements that are being studied.



(iii) **Functional Analysis: Then** follows the important phase of functional analysis. After familiarisation with the relevant facts & figures, a functional analysis is carried out to determine the functions and uses of the product and its components. The cost and importance of each function are identified. A value index is computed on the basis of cost benefit ratio for each of the functions. A list of the functions is prepared wherein the functions are arranged in decreasing order of their value.

(iv) **Innovation:** This is the creative phase concerned with the generation of new alternatives to replace or remove the existing ones. The objective is to produce ideas and to formulate alternative means and methods for accomplishing the essential functions and improving the value of the element under consideration. Creative problem solving techniques are utilized to discover alternatives that will provide essential or required functions at the lowest possible cost.

(v) **Evaluation: During the stage of evaluation,** each and every alternative is analysed and the most promising alternatives are selected. These alternatives are further examined for economic and technical feasibility. The alternatives finally selected must be capable of performing the desired functions satisfactorily. They must meet the standards of accuracy, reliability, safety, maintenance and repairs, environmental effects, and so on.

(vi) **Choice:** In this phase, the decision makers choose the best of alternatives. The programs and action plans are then developed to implement the chosen alternative.

(vii) **Implementation:** The chosen alternative is put to the actual use with the help of the programs and action plans. The progress of implementation is continuously monitored and followed up to ensure that the desired results are achieved.

05.00 Value Engineering (VE)

'VA' and 'VE' are closely related terms so much so that they are, frequently, used interchangeably. Though the philosophy of understanding the two is the same, the difference lies in the time and stage at which the technique is applied.

"Value Analysis" is the application of a set of techniques to an existing product with a view to improve its value. Thus, it is a remedial process. "Value Engineering" is the application of exactly the same set of techniques to a new product at the design stage to ensure that bad features are not added. Thus, it is a 'preventive' measure. In that sense, 'VE' is fundamental and VA is collateral because 'prevention is better than cure."

06.00 Cost Reduction

The core advantage of using value analysis is its potential for reducing costs, which is a benefit that permeates all advantages of the system. Because of the fact that value analysis breaks down a product or service into components, it enables the analysis of each of the components on its own, evaluating its importance and efficiency. A value analysis correctly implemented and applied enables the entity to identify components that are not worth the cost they require and that can be eliminated or replaced with an alternative. In this manner, the process for the product or service being analyzed is refined to be done at less expense.

07.00 Quick Take

Cost-Value judgment is a function of 'Applied Consumption Sense'. VA can provide opportunities for effective decision making in various spheres of Industrial and Business activities.

GROUP: 3, PAPER: 16

DIRECT TAX

LAWS AND INTERNATIONAL TAXATION (DTI)

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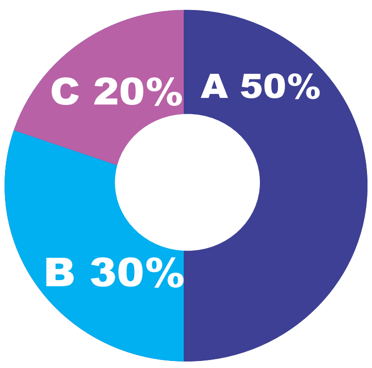

Syllabus Structure

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.

Basics of Transfer Pricing

"Transfer Pricing is not an exact science but does require the exercise of judgement on the part of both the tax administration and taxpayer"

Commercial transactions between the different parts of the multinational groups may not be subject to the same market forces shaping relations between the two independent firms. One party transfers goods or services to another for a price. That price is known as "transfer price". This may be arbitrary and dictated, with no relation to cost and added value, diverge from the market forces. Transfer price is, thus, a price which represents the value of goods or services between independently operating units of an organisation. But, the expression "transfer pricing" generally refers to prices of transactions between associated enterprises which may take place under conditions differing from those taking place between independent enterprises. It refers to the value attached to transfers of goods, services and technology between related entities. It also refers to the value attached to transfers between unrelated parties which are controlled by a common entity.

Suppose a company A purchases goods for ₹ 100 and sells it to its associated company B in another country for ₹ 200, who in turn sells in the open market for ₹ 400. Had A sold it direct, it would have made a profit of ₹ 300. But by routing it through B, it restricted it to ₹ 100, permitting B to appropriate the balance. The transaction between A and B is arranged and not governed by market forces. The profit of ₹ 200 is, thereby, shifted to the country of B. The goods is transferred on a price (transfer price) which is arbitrary or dictated (₹ 200), but not on the market price (₹ 400).

Thus, the effect of transfer pricing is that the parent company or a specific subsidiary tends to produce insufficient taxable income or excessive loss on a transaction. For instance, profits accruing to the parent can be increased by setting high transfer prices to siphon profits from subsidiaries domiciled in high tax countries, and low transfer prices to move profits to subsidiaries located in low tax jurisdiction. As an example of this, a group which manufacture products in a high tax countries may decide to sell them at a low profit to its affiliate sales company based in a tax haven country. That company would in turn sell the product at an arm's length price and the resulting (inflated) profit would be subject to little or no tax in that country. The result is revenue loss and also a drain on foreign exchange reserves.

Computation of income from international transaction or specified domestic transaction having regard to arm's length price [Sec. 92]

The provisions are as under:

Provisions	Example	Treatment	Impact on income
Any income arising from an international transaction shall be computed having regard to the arm's length price.	X Ltd., resident, sold goods or services to its associated enterprises, XY Plc. (a foreign company), for ₹ 5 lacs whereas the arm's length price of such goods or services is ₹ 9 lacs	While computing income of X Ltd., ₹ 9 lacs shall be considered as sale value	Income of X Ltd. will be increased by ₹ 4 lacs.
The allowance for any expense or interest arising from an international transaction or specified domestic transaction shall also be determined having regard to the arm's length price.	R Ltd. takes a loan of ₹ 20 lacs from an associated enterprise in Ireland @ 20% p.a. whereas the arm's length rate of interest is 12% p.a.	Interest @ 12% p.a. shall be allowed as deduction to R Ltd.	Income of R Ltd. will be increased by ₹ 1,60,000/-

Where in an international transaction or specified domestic transaction, two or more associated enterprises enter into a mutual agreement or arrangement for the apportionment of, or any contribution to, any cost incurred in connection with a benefit, service or facility provided to any such enterprises, the cost apportioned to (contributed by), any such enterprise shall be determined having regard to the arm's length price of such benefit, service or facility.	An enterprise in Germany makes research on a new product and incurred ₹ 50 lacs. Out of this, ₹ 40 lacs has been allocated to its Indian associated enterprises dealing in the same product.	While computing income of Indian enterprise, it will be required to be examined whether the Indian enterprise is deriving proportionate benefit to the research expenditure allocated	If no such benefit is available to the Indian enterprise, total income of such enterprises is suitably increased by disallowing proportionate allocated cost.
The provisions (in any of aforesaid situation) shall not apply in a case where the computation of income or the determination of the allowance for any expense or interest or the determination of any cost or expense allocated or contributed has the effect of reducing the income chargeable to tax or increasing the loss, as the case may be, computed on the basis of entries made in the books of account in respect of the previous year in which the international transaction or specified domestic transaction was entered into.	X Ltd., resident, sold goods or services to its associated enterprises, XY Plc. (a foreign company), for ₹ 5 lacs whereas the arm's length price of such goods or services is ₹ 3 lacs	The provision of transfer pricing is not applicable	No Impact

Meaning of associated enterprise [Sec. 92A]

Associated enterprise, in relation to another enterprise, means an enterprise:

(a) which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or

(b) in respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Deemed associated enterprise [Sec. 92A(2)]

For the above purpose, two enterprises shall be deemed to be associated enterprises if, at any time during the previous year fulfill any of the following conditions (if one of following conditions are not satisfied, then mere participation in management or control or capital of the other enterprise, etc. shall not make them associate):

(a) one enterprise holds (directly or indirectly) shares carrying not less than 26% of the voting power (i.e., equity shares in case of company) in the other enterprise; or

(b) any person or enterprise holds (directly or indirectly) shares carrying not less than 26% of the voting power in each of such enterprises; or

(c) the manufacture or processing of goods or articles or business carried out by one enterprise is wholly (not partially) dependent on the use of know-how, patents, copyrights, trade-marks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights; or

(d) 90% or more of the raw materials and consumables required for the manufacture or processing of goods or articles carried out by one enterprise, are supplied by the other enterprise **or** by persons specified by the other enterprise, **and** the prices and other conditions relating to the supply are influenced by such other enterprise; or

(e) the goods or articles manufactured or processed by one enterprise, are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by such other enterprise; or

(f) where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual; or

(g) where one enterprise is controlled by a Hindu undivided family, the other enterprise is controlled by a member of such Hindu undivided family, or by a relative of a member of such Hindu undivided family, or jointly by such member and his relative; or

(h) where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds not less than 10% interest in such firm, association of persons or body of individuals; or

(I) a loan advanced by one enterprise to the other enterprise constitutes not less than 51% of the **book value** of the total assets of the other enterprise; or

Taxpoint: Revaluation of asset shall not be ignored.

(j) one enterprise guarantees not less than 10% of the total borrowings of the other enterprise; or

(k) more than $\frac{1}{2}$ of the board of directors or members of the governing board, **or** one (not $\frac{1}{2}$ of total number of executive director) or more executive directors or executive members of the governing board of one enterprise, are **appointed** by the other enterprise; or

Taxpoint: Mere power to appoint director is not sufficient, such power must be exercised.

(l) more than $\frac{1}{2}$ of the directors or members of the governing board, **or** one or more of the executive directors or members of the governing board, of each of the two enterprises are **appointed** by the same person or persons; or

(m) there exists between the two enterprises, any relationship of mutual interest, as may be prescribed.

Equity Holding	Management	Activities	Control
1. >= 26% direct / indirect holding by enterprise OR **2.** By same person in each enterprise **3.** Loan >= 51% of Total Assets **4.** Guarantees > = 10% of debt > 10% interest in Firm / AOP / BOI	**6.** Appointment > 50% of Directors / one or more Executive Director by an enterprise OR 7. Appointment by same person in each enterprise	8. 100% dependence on use of intangibles for manufacture / processing / business **9.** Direct / indirect supply of > = 90% Raw Materials under influenced prices and conditions 10. Sale under influenced prices and conditions	**11.** One enterprise controlled by an individual and the other by himself or his relative or jointly **12.** One enterprise controlled by HUF and the other by - a member of HUF - his relative or Jointly by member and relative

Computation of arm's length price [Sec. 92C]

- The arm's length price in relation to an international transaction or specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely:

  Transaction Based Methods

  a. comparable uncontrolled price method;

  b. resale price method;

  c. cost plus method;

  Profit Based Methods

  d. profit split method;

  e. transactional net margin method;

  f. such other method as may be prescribed by the Board.

Illustration

Discuss whether adjustment is required in the context of transfer pricing provisions where the transfer price adopted for an international transaction of sale of goods by an Indian company during the financial year 2017-18, is ₹ 50 lacs whilst the Arm's Length Price determined using the most appropriate method are ₹ 48 lacs and ₹ 56 lacs. Assume that the rate of permissible variation prescribed by the Central Government is 2% of the transfer price for this class of international transaction.

Solution

The proviso to section 92C(2) provides that where more than one price is determined by the most appropriate method, the arm's length price (ALP) shall be taken to be the arithmetical mean of such prices. However, if the arithmetical mean, so determined, is within such percentage of the transfer price notified by the Central Government, then, the transfer price shall be deemed to be the arm's length price and no adjustment is required to be made.

The arithmetical mean of the prices = (₹ 48 + ₹ 56) / 2 = ₹ 52 lacs.

The rate of permissible variation prescribed by the Central Government is 2% i.e. ₹ 1 lacs (₹ 50 lacs x 2%).

Since the variation between the arm's length price of ₹ 52 lacs and the transfer price of ₹ 50 lacs is not within the limit of 2% of TP (i.e., ₹ 1 lacs), the arm's length price shall be ₹ 52 lacs.

The Assessing Officer may compute the total income of the Indian company having regard to the arm's length price of ₹ 52 lacs so determined. No deduction shall be allowed under Chapter VI-A or section 10AA in respect of ₹ 2 lacs, being the amount of income by which the total income of the Indian company is enhanced after application of the arm's length price of ₹ 52 lacs.

Note: It is assumed that the assessee has not entered into an Advance Pricing Agreement and has also not opted to be subject to Safe Harbour Rules

150 YEARS OF CELEBRATING THE MAHATMA

GROUP: 4, PAPER: 17

CORPORATE FINANCIAL REPORTING (CFR)

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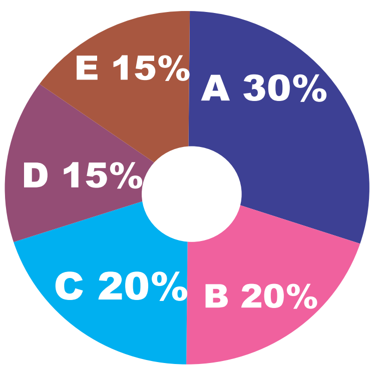
Your Preparation Quick Takes



Syllabus Structure

A GAAP and Accounting Standards **30%**
B Accounting if Business Cominations
& 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.

Corporate Financial Reporting

The concepts of Sustainability, Sustainability Reporting and GRI-G4 frameworks have already been elaborately discussed in June, 2018 and September, 2018 issues of e-bulletin. Triple Bottom Line philosophy considers three important factors such as the 'People, Planet and Profit' which are of utmost important for overall sustainability of the business. 'People' or the human resources of the organization are considered to be the most valued resource which ensures effective, efficient and optimum utilization of the other available resources such as physical resource, financial resource and technological resource. Considering the crucial role to be played by the human resource, every organization should properly manage it by adequately motivation, developing, compensating, integrating and empowering them so that they individually and collectively contribute towards the achievement of the broad organizational goals. It is the responsibility of the organizations to ensure proper health, safety and security measures to protect the interest of the workers. Exploitation of labour in any form may result in the serious industrial disputes which will negatively affect the productivity, performance and ultimately the share price of the company. Different organizations both at national and international level are continuously engaged into the activity of ensuring 'decent work' conditions for workers as proposed by ILO. Because of the importance of the human resources in steering the fate of the organization and its overall sustainability, the investors across the globe are interested in knowing the labour practices adopted by the different organizations. In GRI framework there are different indicators which are associated with the labour conditions and decent work. Different companies across the globe are following the GRI G4 framework to report for their best practices in managing the human resources.

Let us look at some of the GRI-G4 guidelines relating to Labour Practices and Decent Work:

Codes	Description of Labour Practices and Decent Work
G4-10	❖ Reporting of total number of employees by employment contract and gender. ❖ Reporting of total number of permanent employees by employment type and gender. ❖ Reporting of the total workforce by employees and supervised workers and by gender. ❖ Reporting of the total workforce by region and gender. ❖ Reporting of whether a substantial portion of the organization's work is performed by workers who are legally recognized as self-employed, or by individuals other than employees or supervised workers, including employees and supervised employees of contractors. Reporting of any significant variations in employment numbers.
G4-11	Reporting of the percentage of total employees covered by collective bargaining agreements
G4-LA1	❖ Reporting of the total number and rate of new employee hires during the reporting period, by age group, gender and region. Reporting of the total number and rate of employee turnover during the reporting period, by age group, gender and region.
G4-LA2	❖ Reporting of the benefits which are standard for full-time employees of the organization but are not provided to temporary or part-time employees, by significant locations of operation such as life insurance, health care, disability and invalidity coverage, parental leave retirement provision, stock ownership and others. Reporting of the definition used for 'significant locations of operation'.
G4-LA3	❖ Reporting of the total number of employees that were entitled to parental leave, by gender. ❖ Reporting of the total number of employees that took parental leave, by gender. ❖ Reporting of the total number of employees who returned to work after parental leave ended, by gender. ❖ Reporting of the total number of employees who returned to work after parental leave ended who were still employed twelve months after their return to work, by gender. Reporting of the return to work and retention rates of employees who took parental leave, by gender.
G4-LA4	❖ Reporting of the minimum number of weeks' notice typically provided to employees and their elected representatives prior to the implementation of significant operational changes that could substantially affect them. Reporting of whether the notice period and provisions for consultation and negotiation are specified in collective agreements or organizations with collective bargaining agreements.

G4-LA5	❖ Reporting of the level at which each formal joint management-worker health and safety committee typically operates within the organization. Reporting of the organizations with collective bargaining agreements the percentage of the total workforce represented in formal joint management-worker health and safety committees.
G4-LA6	❖ Reporting of the types of injury, injury rate, occupational diseases rate, lost day rate, absentee rate and work-related fatalities, for the total workforce that is, total employees plus supervised workers), by region and gender ❖ Reporting of the types of injury, injury rate, occupational diseases rate, lost day rate, absentee rate and work-related fatalities for independent contractors working on-site to whom the organization is liable for the general safety of the working environment, by region and gender Reporting of the system of rules applied in recording and reporting accident statistics.
G4LA7	Reporting of the whether there are workers who are involved in occupational activities who have a high incidence or high risk of specific diseases.
G4-LA8	❖ Reporting of the whether formal agreements (either local or global) with trade unions cover health and safety Reporting of the extent, as a percentage, to which various health and safety topics are covered by these agreements.
G4-LA9	Reporting of the average hours of training that the organization's employees have undertaken during the reporting period,
G4-LA10	❖ Reporting on the type and scope of programs implemented and assistance provided to upgrade employee skills. Reporting on the transition assistance programs provided to facilitate continued employability and the management of career endings resulting from retirement or termination of employment.
G4-LA11	Reporting of the percentage of total employees by gender and by employee category who received a regular performance and career development review during the reporting period.
G4-LA12	❖ Reporting of the percentage of individuals within the organization's governance bodies in each of the following diversity categories such as gender, age group (under 30 years old, 30-50 years old, over 50 years old), minority groups, other indicators of diversity where relevant. Reporting of the percentage of employees per employee category in each of the following diversity categories such as gender, age group (under 30 years old, 30-50 years old, over 50 years old), minority groups, other indicators of diversity where relevant.
G4-LA13	❖ Reporting of the ratio of the basic salary and remuneration of women to men for each employee category, by significant locations of operation. Reporting of the definition used for 'significant locations of operation'.
G4-LA14	Reporting of the percentage of new suppliers that were screened using labor practices criteria.
G4-LA15	❖ Reporting of the number of suppliers subject to impact assessments for labor practices. ❖ Reporting of the number of suppliers identified as having significant actual and potential negative impacts for labour practices. ❖ Reporting of the significant actual and potential negative impacts for labour practices identified in the supply chain. ❖ Reporting of the percentage of suppliers identified as having significant actual and potential negative impacts for labour practices with which improvements were agreed upon as a result of assessment. Reporting of the percentage of suppliers identified as having significant actual and potential negative impacts for labour practices with which relationships were terminated as a result of assessment, and why.

G4-LA16	❖ Reporting of the total number of grievances about labour practices filed through formal grievance mechanisms during the reporting period. ❖ Reporting of the identified grievances. ❖ Reporting of the grievances addressed during the reporting period ❖ Reporting of the grievances resolved during the reporting period Reporting of the total number of grievances about labor practices filed prior to the reporting period that was resolved during the reporting period.

Consider the following information as disclosed in the Sustainability Report 2017 of ITC Ltd.

"In ITC, on-site refers to the place of work i.e. factory, hotel, office, etc. which is under direct operational control of ITC. In 2016-17, the total number of on-site Lost Time Accidents (LTA) was 16 (against 18 in 2015-16). Out of these 16 accidents, 6 accidents occurred to ITC employees and balance 10 to the service providers' employees. All of these accidents occurred to male employees. There was one unfortunate fatal accident in 2016-17 to a service provider's employee who sustained burn injuries during a boiler start up. Detailed investigations are carried out for all accidents, injuries, near misses and dangerous occurrences to identify the root causes. Further analysis of the root causes of the accidents have identified the need for strengthening the process of risk assessments and planned job observations and improvement in the supervision of service providers' employees. Accordingly, necessary corrective and preventive measures have been implemented across the Units. Since 2012-13, ITC has started reporting safety performance of its service providers' employees working within ITC premises. Loss Time Accident (LTA) is defined as accident due to which the injured does not return to work in the next scheduled shift. As can be seen from the following graph, total LTA (including service providers' employees) reflect a reducing trend despite a significant increase in number of manufacturing units and total employees. Lost Day Rate (LDR) is defined as the number of man days lost due to accidents for every 200000 man hours worked. As can be seen from the graph (on the next page), though there has been a drop in the LDR during 2016-17, it remains an area of concern and ITC is committed to continually improve upon this performance. Injury Rate (IR) is defined as the frequency of LTA in relation to total time worked. Though there has been an improvement in the performance, it is of utmost concern that ITC still had a fatal accident in one of its factories. ITC accordingly has been revalidating its entire approach to safety and is focused on creating a culture of safety across the Organisation."(Source:Page 139 Sustainability Report 2017)

Labour and Employment:

Year	2015	2016	2017
Total workforce	32115	32138	32337
Total Female Employees	3414	3490	3602
Total New Hires	5224	5884	6609
Total Attrition Percentage	16%	19%	18%
Total Training Mandays	142547	149264	121653

Source: Page 131of Sustainability Report 2017

Task for the students:
Try to map the G4 Guidelines which have been followed and reported by ITC Ltd. regarding the Labour Practices and Decent Work.

GROUP: 4, PAPER: 18

INDIRECT TAX
LAWS & PRACTICE (ITP)

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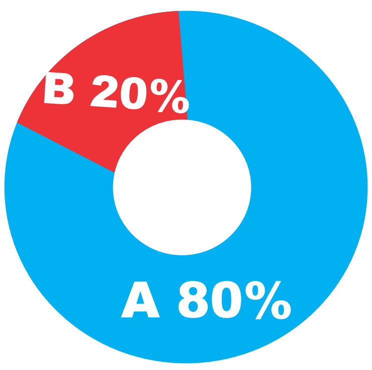
Your Preparation Quick Takes



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:

- Concept of Mixed Supply under GST law;
- Conditions for Mixed Supply;
- Time of Supply in case of Mixed Supply;
- Treatment of Mixed Supply under GST.

'MIXED SUPPLY' UNDER GST

Introduction

- A taxable event under GST is 'supply' of goods or services or both. GST gets leviable and payable on every supply of goods or services or both, unless otherwise exempted. The term 'supply' is a very interesting and is subject to wide connotations, interpretations and applications.
- In most cases, goods or services are supplied individually by a supplier to its customer. For correct the ascertainment and payment of GST, the applicable rate of GST on such individual goods or services or both needs to be separately identified. Prior to that, its classification (whether as goods or services, the category of goods and services) is also essential to charge applicable rate of GST on the particular supply. The process of classification and thereafter the rate poses no problem if the supply is of individual goods or services, as in that case the classification and the applicable rate is clearly identifiable.
- In today's market scenario combination of goods and services are supplied together to make a product attractive and saleable to the customers. This leads to the concepts of Bundled Supply. A bundled supply refers to a supply which is a combination of goods and/or services. Under the existing GST law, bundled supplies of two or more goods or services can be considered as either Composite supply and Mixed supply. Schedule II of the CGST Act, 2017 sets out the provisions for such classification.

Concept of Mixed Supply

- As per Sec. 2(74) of CGST Act, 2017, Mixed Supply means two or more individual supplies of goods or services, or any combination thereof, made in conjunction with each other by a taxable person for a single price where such supply does not constitute a composite supply. In other words, a mixed supply refers to a supply made by a taxable person to a recipient consisting of is two or more independent products or services which are offered together as a bundle but can also be sold separately.
- This concept of mixed supply is entirely new under the GST law and did not exist under any of the earlier indirect tax laws.
- Examples of mixed supply:
  - Diwali gift boxes consisting of canned foods, sweets, chocolates, cakes, dry fruits, aerated drinks and fruit juices supplied for a single price is a mixed supply. Each of these items is independent of each other and is capable of being supplied separately.
  - A departmental store offering a free bucket on purchase of 2 Kg. detergent powder is an example of mixed supply.
  - Supply of shaving razor with shaving cream in a mens' grooms kit in which the cream is claimed to be given free is a mixed supply.

Conditions for Mixed Supply

For a service to qualify as mixed supply the following conditions must be satisfied:

- The supply consists of supply of two or more goods and/ or services;
- Such supply of goods and/ or services is made together at a single price;
- The supplies are not naturally bundled in the ordinary course of business; and
- They are independent of each other and are capable of being supplied separately.

NB: For designating a supply as mixed supply, it should first 'be a bundled supply' and thereafter it should 'not be a composite supply'. In other words, a bundled supply has to be ruled out as a composite supply. So, supply can be a mixed supply only if it is not a composite supply.

Time of Supply in case of Mixed Supply

The provisions regarding ascertainment of timing of supply in the event of mixed supply are as follows:

- **When tax rate of a service component is highest**: The mixed supply, if involves supply of a service liable to tax at higher rates than any other constituent supplies, such mixed supply would qualify as supply of services, and accordingly the provisions relating to time of supply of services would be applicable.
- **When tax rate of a service component is highest**: The mixed supply, if involves supply of goods liable to tax at higher rates than any other constituent supplies, such mixed supply would qualify as supply of goods and accordingly the provisions relating to time of supply of services would be applicable.

Treatment of Mixed Supply under GST

- The tax liability on a composite supply is provided u/s 8 of the CGST Act, 2017.
- It states that a mixed supply comprising two or more supplies shall be treated as a supply of that particular supply which attracts the highest rate of tax.
- **Applicable Tax Rate on Composite Supply**: The tax rates applicable in case of mixed supply would be the rate of tax

attributable to that one supply (goods or service) which attracts the highest rate of tax from amongst the supplies forming part of the mixed supply.

Illustration 1: A plant nursery sells cut flowers, ornamental plants, and gardening services together as a bundle. When they're sold separately, the plants and flowers incur GST at a rate of 5%, and the gardening services incur GST at a rate of 18%. When they're offered together as a bundle, the whole bundle will incur GST at the 18% rate.

Illustration 2: A house is given on rent one floor of which is to be used for residence and the other for housing an office to a particular tenant. Such renting for two different purposes is not naturally bundled in the ordinary course of business. Therefore, if a single rent deed is executed it will be treated as a service comprising entirely of such service which attracts the highest liability (here, the rate applicable for office renting, as residential renting is an item of the Negative List).

150 YEARS OF CELEBRATING THE MAHATMA

GROUP: 4, PAPER: 19

COST & MANAGEMENT AUDIT (CMAD)

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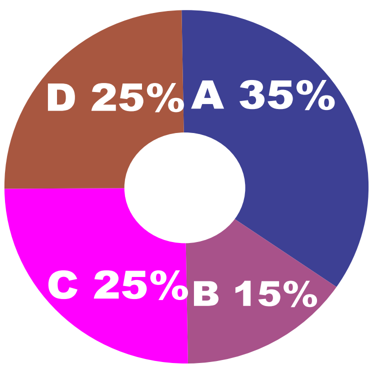
Your Preparation Quick Takes



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

Internal Audit of Current Asset with specific reference to Receivables.

Introduction

Internal auditing is an independent appraisal activity within an organization for the review of operations as a service to the management. It improves managerial control by measuring and evaluating the effectiveness of other controls, and by maintaining a vigilant watch over risks.

Section 138 of the Companies Act 2013, deals with provisions of internal audit. As per section 138 (1) Such class or classes of companies as may be prescribed shall be required to appoint an internal auditor, who shall either be a chartered accountant or **a cost accountant,** or such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the company.

Constitution of Current Assets

Current Assets are those assets which can reasonably be expected to be sold, consumed, or exhausted through the normal operations of a business within the current fiscal year or operating cycle, whichever period is longer.

As per Schedule III, Part – 1 of The Companies Act 2013, Current Assets comprises of the following

a) Current Investments
b) Inventories
c) Trade Receivables
d) Cash and cash equivalents
e) Short term loans and advances
f) Other current assets

It has been noted that trade receivable constitute one of the major elements of current assets after inventory for majority of business entities and its correct evaluation and presentation in annual accounts of the company plays avery important role for the true and fair view of affairs of the company. The Cost and Management Accountants are best suited for evaluation, valuation and control of trade receivables for the management. Trade receivables are amounts due from customers for goods sold or services performed in normal course of business. All receivables which are normal and emerging out of genuine trade transactions only, are to be taken for the purpose of evaluation of Trade Receivables.

Receivables which are not related to normal business transactions or are older than six months or are in the nature of unrecoverable/ bad debts are to be treated as non-current assets. In order to ascertain the one has to study the previous balance sheets and look for repeated items of receivables and wherever necessary seek the clarification from management. Trade Receivables are generallycalculated or consisting of the followings:

a. Sales amount billed to customers
b. Accrued sales for goods delivered but not billed
c. Contract retentions
d. Suppliers' debit balances
e. Less: Prevision for bad debts
f. Less: Credits for returns
g. Less: Allowances

Receivables should be presented at net realizable amounts (i.e. amounts realistically anticipated to be collectible). Deductions should be taken for amounts estimated to be uncollectible and also for estimated returns, allowances and other discounts to be taken by customers prior to or at time of payment.

Review / verification of receivable

While reviewing the Trade receivables, the auditor should examine the following points:

a) Existence – That the amount recorded in respect of debtors are outstanding as on a particular date.
b) Completeness – The details re complete and there are no unrecorded debtors.
c) Valuation – That the basis of valuation of debtor is appropriate and the recoverability is realistic.
d) Disclosure – That the debtors are disclosed, classified and described in accordance with recognised accounting policies and practices.
e) Verification – The verification of debtors may be carried out by applying an analytical review of records and through direct conformation procedure from debtors.

Further, all material adjustments in debtors' accounts, particularly those relating to rebates, allowances, commissions etc. should require approval of competent authority. Similarly, the writing off of bad debts should be done after follow up of prescribed procedure and due approval of the competent authority.

The following are some of the indicative situations which lead to arise of doubtful and uncollectible of trade receivables.

a) The terms of credit have been repeatedly ignored.
b) There is stagnation, or lack of healthy turnover, in the account.
c) Payments are being received but the balance is continuously increasing.
d) Payments, though being received regularly, are quite small in relation to the total outstanding balance.
e) An old bill has been partly paid (or not paid), while later bills have been fully settled.
f) The cheques received from the debtor have been repeatedly dishonoured.
g) The debt is under litigation, arbitration, or dispute.
h) The auditor becomes aware of unwillingness or inability of the debtor to pay the dues e.g., a debtor has either become insolvent, or has closed down his business, or is not traceable.

i) Amounts due from employees, which have not been repaid on termination of employment.
j) Collection is barred by statute of limitation.

In addition to the indicative situations discussed above, the following analytical review procedures is also helpful as a means of obtaining audit evidence regarding the various assertions relating to trade receivables.

a) Comparison of closing balances of debtors, loans and advances with the corresponding figures for the previous year;
b) Comparison of the relationship between current year debtor balances and the current year sales with the corresponding figures for the previous year;
c) Comparison of actual closing balances of debtors, loans and advances with the corresponding budgeted figures, if available;
d) Comparison of current year's aging schedule with the corresponding figures for the previous year;
e) Comparison of significant ratios relating to debtors, loans and advances with the similar ratios for other firms in the same industry, if available;
f) Comparison of significant ratios relating to debtors, loans and advances with the industry norms, if available.

The Companies Act, 2013 has provided general instructions for presentation of Trade receivables in the Balance sheet(Point 'P' of the Part – 1 of Schedule III) in the following manner:

Trade Receivables

i. Aggregate amount of Trade Receivables outstanding for a periodexceeding six months from the date they are due for payment should be separately stated.
ii. Trade receivables shall be sub-classified as:
(a) Secured, considered good;
(b) Unsecured, considered good;
(c) Doubtful.
iii. Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.
iv. Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

GROUP: 4, PAPER: 20

STRATEGIC PERFORMANCE MANAGEMENT AND BUSINESS VALUATION (SPBV)

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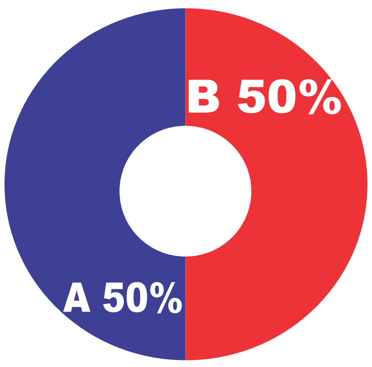
Your Preparation Quick Takes



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:

- comprehend the concept of Free Cash flow to the Firm
- know the FCFF and other cash flow measures
- understand firm valuation

Strategic Performance Management and Business Valuation

The Free Cash flow to the Firm

The free cash flow to the firm is the sum of the cash flows to all claim holders in the firm, including stockholders, bondholders and preferred stockholders. There are two ways of measuring the free cash flow to the firm (FCFF). One is to add up the cash flows to the claim holders, which would include cash flows to equity (defined either as free cash flow to equity or dividends), cash flows to lenders (which would include principal payments, interest expenses and new debt issues) and cash flows to preferred stockholders (usually preferred dividends).

FCFF = Free Cash flow to Equity + Interest Expense (1 - tax rate) + Principal Repayments - New Debt Issues + Preferred Dividends

However, the process can be reversed to get the free cash flow to equity, where payments to lenders and preferred stockholders are subtracted to estimate the cash flow left for stockholders. A simpler way of getting to free cash flow to the firm is to estimate the cash flows prior to any of these claims. Thus, we could begin with the earnings before interest and taxes, net out taxes and reinvestment needs and arrive at an estimate of the free cash flow to the firm.

FCFF = EBIT (1 - tax rate) + Depreciation - Capital Expenditure - Working Capital

Since this cash flow is prior to debt payments, it is often referred to as an unlevered cash flow. Note that this free cash flow to the firm does not incorporate any of the tax benefits due to interest payments. This is by design, because the use of the after-tax cost of debt in the cost of capital already considers this benefit and including it in the cash flows would double count it. (Damodaran, 2nd ed.)

FCFF and other cash flow measures

The differences between FCFF and FCFE arise primarily from cash flows associated with debt -- interest payments, principal repayments, new debt issues and other non-equity claims such as preferred dividends. For firms at their desired debt level, which finance their capital expenditures and working capital needs with this mix of debt and equity. As for the use of debt issues to finance principal repayments, the free cash flow to the firm will exceed the free cash flow to equity.

One measure that is widely used in valuation is the earnings before interest, taxes, depreciation and amortization (EBITDA). The free cash flow to the firm is a closely related concept but it takes into account the potential tax liability from the earnings as well as capital expenditures and working capital requirements. (Damodaran, 2nd ed.)

Three measures of earnings are also often used to derive cash flows. The earnings before interest and taxes (EBIT) or operating income comes directly from a firm's income statements. Adjustments to EBIT yield the net operating profit or loss after taxes (NOPLAT) or the net operating income (NOI). The net operating income is defined to be the income from operations, prior to taxes and non-operating expenses. Each of these measures is used in valuation models and each can be related to the free cash flow to the firm. Each, however, makes some assumptions about the relationship between depreciation and capital expenditures that are made explicit in the Table 1.

Table 1: Free Cash Flows to the Firm: Comparison to other measures

Cash flow used	Definition	Use in valuation
FCFF	Free Cash flow to firm	Discounting free cash flow to the firm at the cost of capital will yield the value of the operating assets of the firm. To this, you would add on the value of non-operating assets to arrive at firm value.
FCFE	FCFF - Interest (1-t) – Principal repaid + New Debt Issued – Preferred Dividend	Discounting free cash flows to equity at the cost of equity will yield the value of equity in a business.
EBITDA	FCFF + EBIT(t) + Capital Expenditures + Change in working capital	If you discount EBITDA at the cost of capital to value an asset, you are assuming that there are no taxes and that the firm will actively disinvest over time. It would be inconsistent to assume a growth rate or an infinite life for this firm.

EBIT (1-t) (NOPLAT is a slightly modified version of this estimate and it removes any non-operating items that might affect the reported EBIT.)	FCFF + Capital Expenditures – Depreciation + Change in working capital	If you discount after-tax operating income at the cost of capital to value a firm, you are assuming no reinvestment. The depreciation is reinvested back into the firm to maintain existing assets. You can assume an infinite life but no growth.

(Damodaran, 2nd ed.)

Firm Valuation: The Cost of Capital Approach

The value of the firm is obtained by discounting the free cash flow to the firm at the weighted average cost of capital. Embedded in this value are the tax benefits of debt (in the use of the after-tax cost of debt in the cost of capital) and expected additional risk associated with debt (in the form of higher costs of equity and debt at higher debt ratios). Just as with the dividend discount model and the FCFE model, the version of the model used will depend upon assumptions made about future growth. As with the dividend discount and FCFE models, a firm that is growing at a rate that it can sustain in perpetuity – a stable growth rate – can be valued using a stable growth model. (Damodaran, 2nd ed.)

A firm with free cash flows to the firm growing at a stable growth rate can be valued using the following equation:

$$\text{Value of firm} = \frac{FCFF_1}{WACC - g_n}$$

where,
$FCFF_1$ = Expected FCFF next year
WACC = Weighted average cost of capital
g_n = Growth rate in the FCFF (forever)

There are two conditions that need to be met in using this model. First, the growth rate used in the model has to be less than or equal to the growth rate in the economy – nominal growth if the cost of capital is in nominal terms, or real growth if the cost of capital is a real cost of capital. Second, the characteristics of the firm have to be consistent with assumptions of stable growth. In particular, the reinvestment rate used to estimate free cash flows to the firm should be consistent with the stable growth rate. The best way of enforcing this consistency is to derive the reinvestment rate from the stable growth rate.

Like all stable growth models, this one is sensitive to assumptions about the expected growth rate. This is accentuated, however, by the fact that the discount rate used in valuation is the WACC, which is significantly lower than the cost of equity for most firms. Furthermore, the model is sensitive to assumptions made about capital expenditures relative to depreciation. If the inputs for reinvestment are not a function of expected growth, the free cash flow to the firm can be inflated (deflated) by reducing (increasing) capital expenditures relative to depreciation. If the reinvestment rate is estimated from the return on capital, changes in the return on capital can have significant effects on firm value. (Damodaran, 2nd ed.)

Basics in Business Letter-Writing

CMA (Dr.) Sreehari Chava
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01.00 Concept

The printed business letter is still the preferred way to convey important information. A carefully crafted letter presented on an attractive letterhead can be a powerful communication tool. To make sure you are writing the most professional and effective letter possible, follow these basics in business letter-writing.

02.00 Professional Letterhead

A letterhead is as important as a brand, in that it represents a company and can impart a first impression to its potential customers. It should, therefore, be a unique and distinct reflection of your business entity. Once the letterhead is researched and chosen, all of the stationery that the company uses must be customised to feature it. It is important that all company stationery matches, as this will do much to reinforce not only the corporate image, but also what your business stands for. So, **select a professional letterhead design that suits your business.**

03.00 Standard Format

Use a standard business letter format and template. The most widely used format for business letters is "block style," where the text of the entire letter is justified left. The text is single spaced, except for double spaces between paragraphs. Typically margins are about 1 inch (25.4 mm) on all sides of the document, which is the default-setting for most of the word-processing programs.

Listed hereunder are standard business template fields:

(i) Number & Date
(ii) Sender's Address
(iii) Receiver's Address
(iv) Subject
(v) Reference
(vi) Opening Salutation
(vii) Body Text
(viii) Call to Action
(ix) Concluding Salutation
(x) Signature Block
(xi) Enclosures
(xii) Carbon Copy

A specimen response to credit recovery letter is enclosed hereto as appendix 1. The **templates are illustrated with the help of the specimen in appendix 2.**

04.00 Tone & Texture

I. **Professional Tone: Use a professional tone.** Your printed business letter should be friendly but more professional at the same time. As a well known author on contemporary business communication suggests, "The business writer should strive for an overall tone that is confident, courteous, and sincere; that uses emphasis and subordination appropriately; that contains non-discriminatory language; that stresses the "you" attitude." That said, be sure to sound like yourself - you don't want your letter to read as if a machine wrote it.

II. **Write clearly:** State your point clearly in your letter. To avoid any miscommunications, use straightforward, concise language. Skip the industry jargons. Instead choose lively, active words to hold your reader's attention.

III. **Organise Information: Organize your information logically.** Group related information into separate paragraphs. In a long, information-packed letter, consider organizing information into sections with subheads.

IV. **Colour Highlighters: Use colour highlighters to emphasize words in text.** It is easy to highlight a few words in colour to draw attention to them.

V. **Be persuasive:** Establish a positive relationship with your reader right away. If you have a connection to the reader – you have met before or have a mutual colleague, for example - mention it in your introductory paragraph. Whether you think your reader will agree with the point of your letter or not, it is important to find common ground and build your case from there.

VI. **Understand: Understand your reader** well enough to anticipate how he or she will react while reading your letter. Address his or her needs or wishes, or a specific problem, and then outline your solution. Provide proof by way of examples and/or expert opinions to back up your point. Make sure to maintain a friendly tone.

VII. **Call to Action: Conclude your letter with a "call to action."** State clearly what your reader needs to do or believe to achieve the desired solution and then state what you, the writer, intend to do next to follow up.

VIII. **Proofread: Proofread your letter without fail.** All your careful crafting and printing can't cover up spelling or punctuation errors, which leave a lasting negative impression.

05.00 Quick Take

Now that you've learned the secrets of writing an effective business letter, you're ready to start composing. Good luck!

Appendix 1

In this specimen 'response to credit recovery letter', Ramesh Jadav of Yojana Distributors responds to Dreamtime Movies with reference to their reminder about the overdue payment of Rs.2.50 crores.

Yojana Distributors Limited

54, Civil Lines, Nagpur – 440 001, Tel: (0712) 2234567, Email: info@ydl.co.in

In reply please quote No. YDL/ Credit/ 2018-19/ 205 November 2, 2018

Dreamtime Movies Limited
69 Fort, Mumbai- 400 001
Tel: (022) 22345677

Subject: **Overdue amount of Rs.2.50 Crores**

Reference: **Your letter No. /Mktg/ 282 dated 4th October 2018**

Dear Mr. Krishnakant,

The payment of your invoice No. 1713 dated September 1, 2018, due for payment on 1st October 2018 was withheld **because of defective material.** The defective material having been replaced by you on 30th October, we have transferred the money through RTGS, vide UTR NO. xxxxxxxx of ABC Bank.

Kindly confirm the settlement of the account.

Yours faithfully

(Ramash Jadav)
Finance Manager

Encl: UTR Receipt
CC: Distribution Manager

Appendix 2

Illustration of the Templates with the help of the specimen

(i) Number & Date:

In reply please quote No. YDL/ Credit/ 2018-19/ 205 November 2, 2018

(ii) Sender's Address:
Yojana Distributors Limited
54, Civil Lines, Nagpur – 440 001
Tel: (0712) 2234567
Email: info@ydl.co.in

(This information is already incorporated into the letterhead)

(iii)Receiver's Address:
Dreamtime Movies Limited
69 Fort, Mumbai- 400 001
Tel: (022) 22345677

(iv)Subject:

Overdue amount of Rs.2.50 Crores

(v) Reference:

Your letter No. /Mktg/ 282 dated 4th October 2018

(vi)Opening Salutation:

Dear Mr. Krishnakant,

(vii) Body Text:

The payment of your invoice No. 1713 dated September 1, 2018, due for payment on 1st October 2018 was withheld **because of defective material**. The defective material having been replaced by you on 30th October, we have transferred the money through RTGS, vide UTR NO. xxxxxxxx of ABC Bank.

(viii) Call to Action:

Kindly confirm the settlement of the account.

(ix) Concluding Salutation:

Yours faithfully

(x) Signature Block:

(Ramesh Yadav)

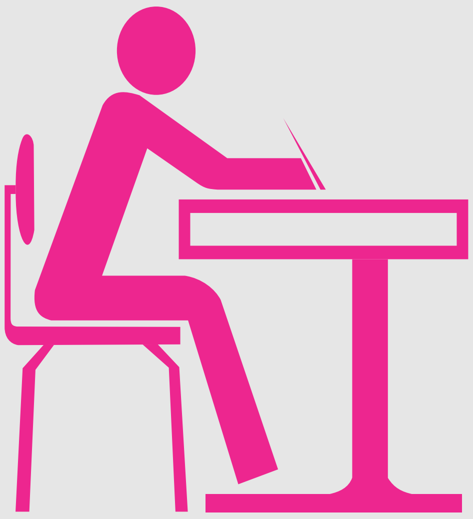
Finance Manager

(xi) Enclosures:

Encl: UTR Receipt

(xii) Carbon Copy

CC: Distribution Manager



Examination TIME TABLE

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA

(Statutory body under an Act of Parliament)

Day & Date	Final Examination Syllabus-2016 Time 2.00 p.m. to 5.00 p.m.
10th December, 2018 (Monday)	Corporate Laws & Compliance (Paper 13) (Group - III)
11th December, 2018 (Tuesday)	Corporate Financial Reporting (Paper 17) (Group - IV)
12th December, 2018 (Wednesday)	Strategic Financial Management (Paper 14) (Group - III)
13th December, 2018 (Thursday)	Indirect Tax Laws & Practice (Paper 18) (Group - IV)
14th December, 2018 (Friday)	Strategic Cost Management - Decision Making (Paper 15) (Group - III)
15th December, 2018 (Saturday)	Cost & Management Audit (Paper 19) (Group -IV)
16th December, 2018 (Sunday)	**Direct Tax Laws and International Taxation (Paper 16) (Group - III)**
17th December, 2018 (Monday)	**Strategic Performance Management and Business Valuation (Paper 20) (Group - IV)**

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
Live Webinar

02 Solve Excercises given in Study Note

03 Assess Yourself

04 Appear For Examination

FINISHED

SUBMISSION

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.

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.

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

Message from

Directorate of Studies

Dear Students,

We have stepped into November,2018 and in the next month your December,2018 term of examination will start. We from the Directorate of Studies know your expectations from us and accordingly we are trying to deliver some meaningful tips through the **publications of monthly E-bulletins**. Other than this we are trying to help you through **Revisionary Test Papers (RTPs), Mock Test Papers (MTPs), Work book**, and we are conducting **Webinar sessions (live)** and where your active participation is amazing. 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 Dont's 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:

"Learn as if you were to live forever".

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) : **http://icmai.in/studentswebsite/mtp2016_j18_fnd.php**

For Revision Test Papers (RTP) : **https://icmai.in/studentswebsite/rtp2016_d18.php**

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

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

Live Webinar Link : **http://icmai.in/icmai/news/889.php**

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

GOOD LUCK & We wish you all the best in your forthcoming examination.

Be Prepared and Get Success;

Few Snapshots

15th National Awards for Excellence in Cost Management-2017 on October 16, 2018 at New Delhi.

15th National Awards for Excellence in Cost Management-2017 on October 16, 2018 at New Delhi.

CMA Amit A Apte, President of the Institute lighting the lamp in the presence of Technical Committee Members and Invitees to start the two days meeting of the Technical Cell of the Institute Chaired by CMA (Dr.) Dhananjay V Joshi, Former President of the Institute on 24th October 2018 at Bengaluru Chapter.

Glimpses of Seminar on Redefining the Trends towards Business Sustainability through Cost Management Strategies on 23rd October 2018 at Bengaluru jointly hosted by the CASB and PD&CPD Committee in association with Bengaluru Chapter of the Institute

Shri Suresh Chandra, Secretary to the Govt. of India, Department of Legal Affairs, Ministry of Law & Justice releasing CAT e Bulletin Vol 1 No 1 2018 on 31st October 2018.

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Behind every successful business decision, there is always a CMA