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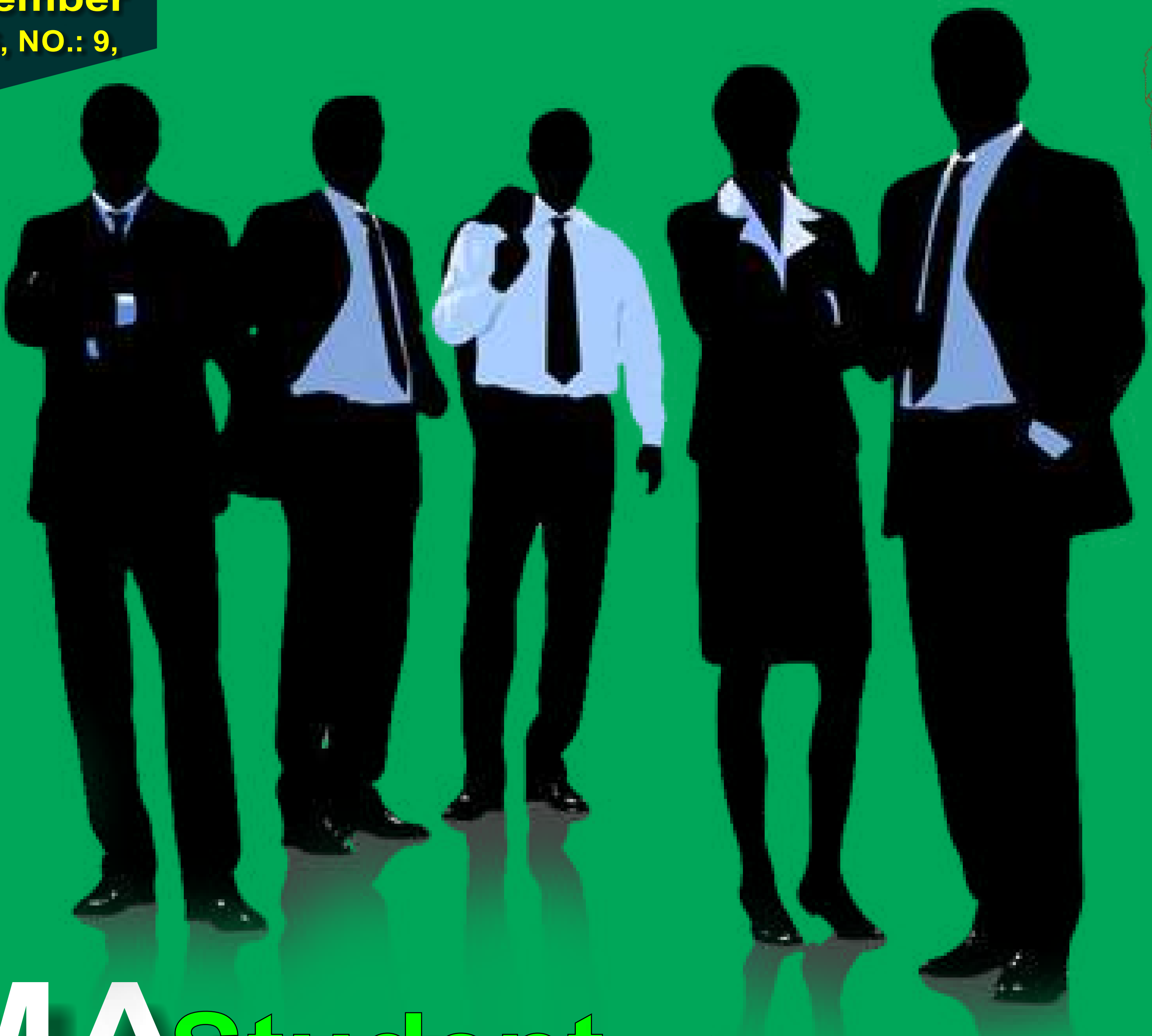

YEARS OF CELEBRATING THE MAHATMA

CMA Student E - Bulletin

FINAL

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Behind every successful business decision, there is always a CMA

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150 YEARS OF CELEBRATING THE MAHATMA

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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YEARS OF CELEBRATING THE MAHATMA

GROUP: iii, PAPER: 13

CORPORATE LAWS & COMPLIANCE (CLC)

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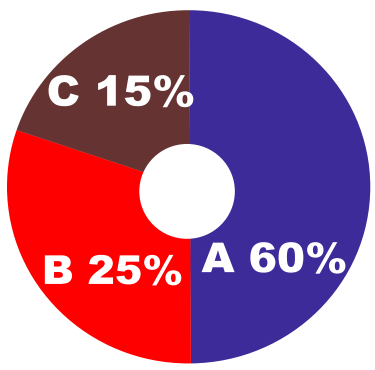
Your Preparation Quick Takes



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

Learning Objectives:

Read the Study Material minutely.

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

Company Capital

CHAPTER 7

COMPANY CAPITAL

Any business including a company will have two sources of capital, i.e. own capital (equity) and loan capital.(long term credit),there can be a financial instrument which is converted from loan to equity. Normally equity is not converted into loan, though there is no legal bar.

Shares and Debentures

Shares and debentures are the main source of long term source of capital. Companies Act does not consider working capital as capital and therefore the restrictions relating to treatment of capital do not apply to working capital.

Shares defined

A share is defined as unit of ownership that represents an equal proportion of a company's capital. It entitles its holder (the shareholder) to an equal claim on the company's profits and an equal obligation for the company's debts and losses.

Two major types of shares are (1) ordinary shares (common stock), which entitle the shareholder to share in the earnings of the company as and when they occur, and to vote at the company's general meetings of shareholders, and (2) preference shares (preferred stock) which entitle the shareholder to a fixed predetermined rate of dividend but generally do not have voting rights. The dividend is payable only when the Company makes adequate profits. This kind of shares is preferred for both payment of dividend and the payment of principal (redemption) on liquidation. Otherwise also preference shares have to be redeemed within 10 years (20 years in case of infrastructure companies)

Types of Share Capital:

There are various terms used in connection with the share capital of the company. They are as follows:

Authorized / Registered / Nominal Capital-

This is the Maximum Capital which the company can raise in its life time. This is mentioned in the Memorandum of the Association of the Company. It is also called Registered Capital or Nominal Capital. Authorised capital may be increased by altering the Memorandum of Association.

Issued Capital-

This is the part of the Authorised Capital which is issued to the public for Subscription i.e. any person to whom the invitation is made may subscribe for shares. Private limited companies can issue shares to its existing shareholders by way of rights issue or by way of giving them bonus shares or it can issue securities through private placements. The act of creating new issued shares is called issuance, allocation or allotment. After allotment, a subscriber becomes a shareholder. The number of issued shares is a subset of the total authorized shares.

Subscribed Capital-

The issued Capital may not be fully subscribed (applied for) by the investor/public. Subscribed Capital is that part of issued Capital for which applications are received from the public. In case applications are for more than the issued capital we call it oversubscription. If it is less, it is called under subscription.

Paid-up Capital-

The part of subscribed capital which have been paid to the company by the investors i.e. the Company may require 50% of the value of shares while making subscriptions. In such case 50% of the value received by the company shall be the paid up capital.

For any company, paid-up capital is important as many provisions of the Act and Rules require various types f compliances based on paid-up capital.

Debentures
A debenture is a type of long term debt instrument which acknowledges debt. Debentures are backed only by the general creditworthiness and reputation of the issuer. Both corporations and governments frequently issue this type of bond to secure capital. Debentures may be secured or unsecured.
Types of Debenture:

The major types of debentures are redeemable, irredeemable, convertible, non-convertible, fully, partly, secured, unsecured, fixed, floating rate, zero coupon, deep discount. Following are the various types of debentures vis-a-vis their basis of classification:

Redeemable and Irredeemable (Perpetual) Debentures

Redeemable debentures carry a specific date of redemption on the certificate. The company is legally bound to repay the principal amount to the debenture holders on that date. On the other hand, irredeemable debentures, also known as perpetual debentures, do not carry any date of redemption. This means that there is no specific time of redemption of these debentures. They are redeemed either on the liquidation of the company or when the company chooses to pay them off to reduce their liability by issues a due notice to the debenture holders beforehand.

Convertible and Non-Convertible Debentures

Convertible debenture holders have to convert their holdings into equity shares. The rate of conversion and the period after which the conversion will take effect are declared in the terms and conditions of the agreement of debentures at the time of issue. On the contrary, non-convertible debentures are simple debentures which will continue to be debentures till redemption. However, if option is given to the investor to convert or not to convert the debenture into shares, this kind of debenture is called optionally convertible debentures.

Fully and Partly Convertible Debentures

Convertible Debentures are further classified into two – Fully and Partly Convertible. Fully convertible debentures are completely converted into equity whereas the partly convertible debentures have two parts. Convertible part is converted into equity as per agreed rate of exchange based on terms of issue. Non-convertible part remains as redeemable debenture which is repaid after the expiry of the agreed period.

Secured and Unsecured Debentures

When the debenture is secured by the charge on some asset or set of assets it is known as secured or mortgage debenture and when it is issued solely on the credibility of the issuer is known as the naked or unsecured debenture. In case of unsecured debenture, the Debenture holder is like any other unsecured creditor. In case of secured debenture, there is a security created by the company on its assets. In case of issue of debenture on private placement basis, the security can be decided by the issuer company and the investor. Public issue of debentures have to be secured, if the maturity period is more than 18 months. In such case, a debenture trustee is appointed, to whom the security is mortgaged with a condition that if the company fails to repay interest or principal, the debenture trustee shall have right to sale off the property and satisfy the claims of debenture holders both interest and principal.

Fixed and Floating Rate Debentures

Fixed rate debentures have fixed interest rate over the life of the debentures. The floating rate debentures have the floating rate of interest which is dependent on some benchmark rate and goes on fluctuating depending on market conditions.

Zero Coupon Debentures

Zero coupon debentures do not carry any coupon rate (interest) or we can say that there is zero coupon rate. The debenture holder will not get any interest on these types of debentures. In such case a warranty is issued with a debenture which may have entitlement to get a share at discount. This compensates the interest foregone. However, zero coupon rate debentures may be issued at discount and are normally called "discounted bonds". If the maturity period is long it is called "deep discount bond".

Raising of Capital
Public issue of share means getting subscription (money) from general public through prescribed procedure, after which shares can be traded in stock exchange. This is called listing of shares. However, if company do not want listing, it can issue to any person or institutional, which is called private placement.

PROSPECTUS

Any notice / circular / advertisement / other documents inviting deposits from the public or offer from the public for the subscription or purchase of any shares in or debentures of a body corporate. In simple words, a prospectus means a document issued by a company which seeks to invite:

a. Public deposits, or,
b. Offers from the public to subscribe to its shares / debentures.

CONTENTS OF PROSPECTUS

1. Name and address of registered office of the company
2. Name of stock exchange where the present issue to be listed.
3. Declaration about minimum subscription.
4. Date of opening of issue
5. Date of closing of issue
6. Name and address of auditors and lead managers
7. Name and address of underwriters and the amount underwritten by each of them.
8. Terms of present issue
9. Particulars of the issue

10. particulars about company, management and project
11. Financial information report of accounts.

MINIMUM SUBSCRIPTION

Minimum Subscription implies the minimum amount which in the opinion of the Board of Directors, must be raised by the issue of the share capital.

2. No company shall proceed to allot shares unless the amount stated as minimum subscription in the prospectus has been subscribed to the extent of 90% within 90 days of closure of subscription list.

3. Where a company fails to receive 90% of minimum subscription within 90 days of closure of the issue, the company must return the money to the applicants within the next 10 days otherwise if later then with the prescribed rates of interest also.

YEARS OF CELEBRATING THE MAHATMA

GROUP: iii, PAPER: 14

STRATEGIC FINANCIAL MANAGEMENT (SFM)

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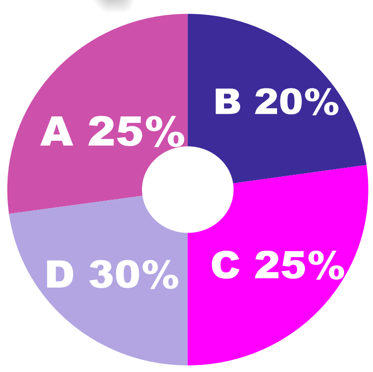
Your Preparation Quick Takes



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

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

➢ **Technical Analysis**

- ***Concept of Technical Analysis***

As mentioned earlier, technical analysis attempts to analyse various market generated time series data (e.g., price and volume data) with respect to any security traded in the market, in an attempt to predict the direction and extent of movement in the price of such security. In other words, based on an examination of past behaviour of price (and in some cases the volume), technical analysis helps investors anticipate the 'likely' price over time. The analysis may be based on intraday, daily, weekly or monthly price information over a considerable period of time (few days to few years). The technical is applicable for any asset whose price is determined by demand and supply forces in an active market. However, most importantly, it is used in the context of stocks, indices, commodities and derivative instruments.

- ***Assumptions Underlying Technical Analysis***

Technical Analysis is based on a number of assumptions as follows:

- In a market, interaction of demand and supply ultimately determines the price of a security.
- Demand and supply are again influenced by both rational as well as irrational factors.
- Whatever be the driving force behind the price movement, security prices tend to move in persistent trends.
- It is possible to decode the shift in demand and supply with the help of charts.
- Analysis of the change in demand and supply and also of the prices help to identify the underlying trend and accordingly it is possible to predict the future price behavior.

- **The Basis of Technical Analysis - The Six Tenets of Dow Theory**

At the turn of the century, the Dow Theory laid the foundations for what was later to become modern technical analysis. However, Dow Theory is not basically a single theory but a collection of theories about how financial markets move over time. There are six Dow Theory tenets, which were put forward by Charles Dow in a collection of editorials he wrote between 1900-1902. He was also famous for the Dow Jones industrial average that he introduced along with Edward Jones and co-founded the Wall Street Journal newspaper.
The 6 tenets or principles that would be applied to a Dow theory portfolio are as follows:

a) The market discounts everything
b) There are 3 kinds of market trends
c) Market trends have three phases
d) The averages must confirm each other
e) Volume should confirm the price
f) Trends persist until there is a clear reversal

The tenets are discussed below.

a) ***The market discounts everything:*** Technical analysts believe that the current price fully reflects all information because all information is already reflected in the price. Thus, the price represents the fair value and should form the basis for analysis.

b) ***There are 3 kinds of market trends:*** According to Dow, there are three kinds of trends that can be observed in the market. These three types of trends are split by the length of time they occupy. These are:

i. Primary trends last a year or more and are the major market trends. They can be bull markets (price travelling up), bear markets (price trending down) or sideways ranges.
ii. Secondary trends last a few weeks or perhaps months and usually counter-trend corrections, where the price moves in the opposite direction to the primary trend.
iii. Minor trends last less than three weeks are the hunting grounds for day traders but considered noise by long-term investors.

c) ***Market trends have three phases:*** Be it the bull trend or the bear trend, either way there are three well defined phases for each. For uptrend, the phases are Revival of confidence (accumulation), Response (public participation), Over-confidence (Speculation). On the other hand, the three defined stages of the Primary Bear Trend are Abandonment of hope (Distribution), Selling on decreased earnings (doubting), Panic (distressed selling).

d) ***The averages must confirm each other:*** Here, averages may be interpreted as indices. According to Dow, the trend must be confirmed by more than one average or indices. Thus, the signal from one index will be more acceptable when it gets support form another index which represents the cause of the former. Initially, when the US was a growing industrial power, Dow had formulated the two averages. One would reflect the state of manufacturing and the other, the movement of those products in the economy. The logic was that if there is production, then those who move them about should also be benefiting and hence new peaks in the industrial average needed to be confirmed by the peaks in the transportation average.

e) ***Volume should confirm the price:*** Dow was of the opinion that trends in prices could be confirmed by volumes. When the movements in price were accompanied by high volumes, they would depict the 'true' movement of the prices.

f) ***Trends persist until there is a clear reversal:*** Irrespective of the day-to-day erratic movement and market noise observed in prices, they move in trends. Reversals in trends are hard to predict. However, a trend is believed to be in action unless definitive proofs of reversal emerge.

Thus, to conclude, prices are not purely random. They do exhibit trends. Thus, if the trends can be appropriately identified, it will be possible to predict the future direction and extent of price movement. Thus, the knowledge of technical analysis will help the analysts and investors to make more informed judgement in the context of investment.

- **Basic Elements of Technical Analysis**

Technical analysis always resorts to the following basic elements:

a) **Trends:** Security price movement is characterized by inertia and hence exhibit clear trends. Supported by a certain pattern of demand-supply relationship, price moves along a certain path (up or down) continually until it is opposed by another trend arising out of a new demand-supply relationship.

b) **Volume:** Volume supports trends. Hence a major upturn (bull) starts when volume of trading increases along with price rise and a major downturn (bear) begins when volume of trading decreases along with fall in price.

c) **Support and Resistance**: According to technical analysts, it is difficult for the price of a security to fall below a certain level, known as 'Support' and to rise above a certain level, known as 'Resistance'. They say that when investors find that price falls after their purchase, instead of selling the shares at low and experience loss, they wait for the price to rise back to the previous level to recover their loss. At this level they sell the shares and break even. As a result, there arises sufficient supply of shares that restricts the price to rise further and creates a 'Resistance'. Similarly, when price falls to its previous level from where it began to increase with large volume, many investors, who had missed the opportunity previously, now create demand for the security. This demand restricts the price to fall further and creates the 'Support'. Technical analysts often use these two levels to properly time the investment strategies.

- ***General Steps to Technical Evaluation***

Many technicians employ a top-down approach to Technical Analysis which involves three steps –

a) Broad market analysis through the major indices such as the S&P 500, Dow Industrials, Nifty 500, BSE 200 etc.

b) Sectoral analysis to identify the strongest and weakest groups within the broad market.

c) Individual stock analysis to identify the strongest and weakest stocks within the select group.

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GROUP: iii, PAPER: 15

STRATEGIC COST MANAGEMENT-DECISION MAKING (SCMD)

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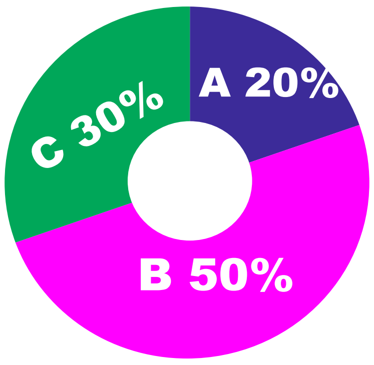
Your Preparation Quick Takes



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:

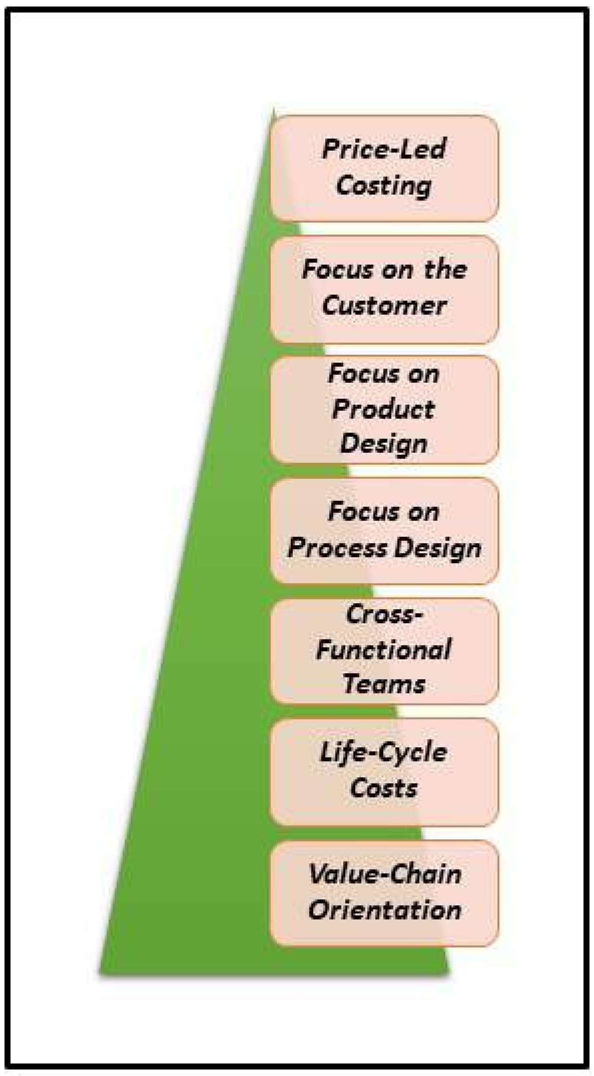
The Strategic cost management framework provides a clear plan of attack for addressing costs and decisions that affect them. It helps to get answers on:

- 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?

Key Principles of Target Costing

01.00 Key Principles

Conceptually, target Costing needs to be perceived as an unique management tool that helps reduction of overall cost of a product over its life cycle. The process embraces all the stages of value addition by the producer as also value consumption by the customer. It does include the stages of research, design, development, manufacturing, administration, marketing, distribution and post-sales support by the producer; utilisation, maintenance and disposal by the consumer. A significant realisation is that product designing stage throws up a lot many opportunities concerning cost reduction. It is, therefore, desirable to set the target cost first and then design the product to fit into the target formulations converging price and profit.



Here follow the Seven Key Principles that encompass Target Costing.

1. Price-Led Costing: Target costing sets the target cost by first determining the price at which a product can be sold in the marketplace. Subtracting the target profit margin from this target price yields the target cost, that is, the cost at which the product must be manufactured. Notice that in a target costing approach, the price is set first, and then the target product cost is determined. This is opposite from the order in which the product cost and selling price are determined under traditional cost-plus pricing.

Key Derivation: Cost = Price - Profit

2. Focus on the Customer: To be successful at target costing, management must listen to the company's customers. What products do they want? What features are important? How much are they willing to pay for a certain level of product quality? Management needs to aggressively seek customer feedback, and then products must be designed to satisfy customer demand and be sold at a price they are willing to pay. In short, the target costing approach is market driven.

Key Derivation: Customer is the Philosopher

3. Focus on Product Design: Design engineering is a key element in target costing. Engineers must design a product from the ground up so that it can be produced at its target cost. This design activity includes specifying the raw materials and components to be used as well as the labour, machinery, and other elements of the production process. In short, a product must be designed for manufacturability.

Every component in the Nano is stated to have been studied from a functionality, cost and performance requirements. There was no other way to reduce costs.

Key Derivation: Manufacturable Product Design forms the Base

4. Focus on Process Design: Every aspect of the production process must be examined to make sure that the product is produced as efficiently as possible. The use of touch labour, technology, global sourcing in procurement and every aspect of the production process must be designed with the product's target cost in mind.

Key Derivation: Efficient Process Design is the Pillar

5. Cross-Functional Teams: Manufacturing a product at or below its target cost requires the involvement of people from many different functions in an organisation: market research, sales, design engineering, procurement, production engineering, production scheduling, material handling and cost management. Individuals from all these diverse areas of expertise can make key contributions to the target costing process. Moreover, a cross-functional team is not a set of specialists who contribute their expertise and then leave; they are responsible for the entire product.

Key Derivation: Team Work does the Trick

6. Life-Cycle Costs: In specifying a product's target cost, analysts must be careful to incorporate all of the product's life-cycle costs. These include the costs of product planning and concept design, preliminary design, detailed design and testing, production, distribution and customer service. Traditional cost-accounting systems have tended to focus only on the production phase and have not paid enough attention to the product's other life-cycle costs.

Key Derivation: Life Cycle Perception is the Approach

7. Value-Chain Orientation: Sometimes the projected cost of a new product is above the target cost. Then efforts are made to eliminate non-value-added costs to bring the projected cost down. In some cases, a close look at the company's entire value chain can help managers identify opportunities for cost reduction.

Key Derivation: Value Addition is the Crux

02.00 Case Study: Unveiling the Indian Nano

Talking of the Indian scenario, no other car launch in the history of Indian auto industry had received as much global press as the "people's car", the "Tata Nano". No other car promised to revolutionise motoring as the Nano has. Clever marketing apart, some frugal and out-of-the-box engineering had gone into the making of Nano. Nano modelled Indian Target Costing too.

Much like what Henry Ford had in the beginning of the 20thcentury with his Model T in 1908 at a price of $825, exactly 100 years after Ratan Tata unveiled Nano, the Indian ultra-low-cost car. At Rs. one lakh, the Nano was the world's cheapest car and made motoring affordable to millions of Indians. Even its deluxe models, featuring air-conditioning and power windows, were fairly cheaper than the then cheapest car in the country, the Maruti 800.

The tale of the creation and design of the Nano is one of innovation and ingenuity, both inside and outside Tata's own organization. Every component in the Nano is stated to have been studied from a functionality, cost and performance requirements. There was no other way to reduce costs. From an outsourcing perspective, the company put in place an Early Vendor Integration Programme.

At first, Ratan Tata called a meeting of his top parts suppliers and, after showing them the early, earnest but flawed prototypes, asked them to help. Companies including Germany's Bosch, which makes the computer that is the heart of car's engine, were sceptical. So were local Indian players.
But Tata persisted, pointing out that not only could a company's specific developments for the Nano help to make history but they could also improve their companies' businesses and bottom lines. Soon most of Tata's traditional suppliers were on board.

The company had a lot of design inputs from vendors that either facilitated manufacturing or brought the cost down. This could be for lamps, seats or for any other component.

The Nano is completely indigenised. At the same time over 85 per cent of the Nano is sourced from outside vendors. Vender parks were put in place with the objective of ensuring that the components between vendors and the assembly line moved smoothly and just in time. Keeping costs down was a major problem for vendors, and they found innovative ways to achieve it.

Rane Group, for instance, makes a rack and pinion steering system. It focused on reducing the weight of the materials used, replacing the steel rod of the steering with a steel tube -- a major cost-reducer. Typically, the product is made of two pieces, but it was redesigned as one to save on machining and assembling costs.

GKN Driveline India, a subsidiary of global auto parts leader GKN, made the driveshaft -- the component that transfers power from the engine to the wheel. The team spent a year developing 32 experimental variants to create the perfect driveshaft for the Nano. It roped in designers from the company's French and Italian operations and changed the design to make it lighter and easier to manufacture.

All the suppliers have similar stories. And although none would disclose specific cost savings, most stuck to Tata's mandate to cut costs. The initial effort was towards cost prevention, which involved selecting a design concept with the least cost. Later on, it is a perpetual cost-reduction effort.

When Ratan Tata addressed an Automotive Component Manufacturers' Association (ACMA) meeting saying that can we all get together to produce an Asian peoples' car, the response was lukewarm – as in the case of Henry Ford. Tata too encountered considerable amount of ridicule from certain close quarters. Even the vendors took it to be a hypothetical project. But, Ratan Tata didn't budge; he went ahead and did it.

The initial idea was to come up with a low-cost car that Malaysia, Indonesia and India could produce jointly. As it turned out, it was left to Ratan Tata to respond to the FT Reporter at Geneva Motor show to commit an Indian Nano at about 1,00,000 rupees. The news got flashed, and it happened. Nano had restructured the dynamics of the car manufacturers all over the world.

What shook the automobile world most was the fact that the designers seem to have done the impossible: The sleek, sophisticated Nano doesn't look flimsy or inexpensive. If it had been an upgraded scooter on four wheels, Tata still would have been applauded for making a family of four safer on Indian roads. The Nano, however, afforded both safety and status.

As Ratan Tata put it in his interview to the Economic Times in January 2008; "The real challenge is when you have some strength and you really choose to throw out the gauntlet that you can do X. And it ought to be the kind of challenge which somebody says that can't be done because then that really becomes the engine of innovation. …. We haven't said we will send a man to Mars, we may put landers on Mars, but we have not done those kinds of things. It is those areas which really create the innovation that we need".

Still, the story of the Nano is not confined to its impact on the auto industry. It's a tale that illuminates the India of today -- an eager, ambitious nation with a combination of engineering talent, a desire for low costs and value, and the hunger of young managers looking to break from a hidebound corporate environment.

And here stands the Modern Indian Cost Manager Model, Ratan Tata, with an everlasting quest for out- of- the-box challenges.

03.00 Quick Take

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

GROUP: iii, PAPER: 16

DIRECT TAX

LAWS AND INTERNATIONAL TAXATION (DTI)

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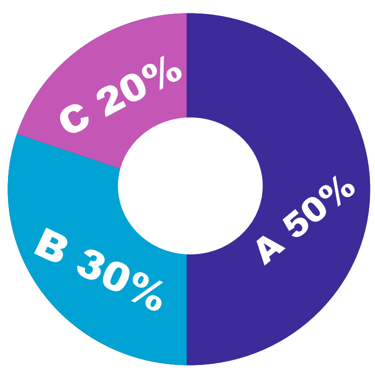
Your Preparation Quick Takes



Syllabus Structure

A Advanced Direct Tax Laws **50%**
B International Taxation **30%**
C Case StudyAnalysis **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.

Thin Capitalization

A company is typically financed or capitalized through a mixture of debt and equity. The way a company is capitalized often has a significant impact on the amount of profit it reports for tax purposes as the tax legislations of countries typically allow a deduction for interest paid or payable in arriving at the profit for tax purposes while the dividend paid on equity contribution is not deductible. Therefore, the higher the level of debt in a company, and thus the amount of interest it pays, the lower will be its taxable profit. For this reason, debt is often a more tax efficient method of finance than equity. Multinational groups are often able to structure their financing arrangements to maximize these benefits. For this reason, country's tax administrations often introduce rules that place a limit on the amount of interest that can be deducted in computing a company's profit for tax purposes. Such rules are designed to counter cross-border shifting of profit through excessive interest payments, and thus aim to protect a country's tax base.

Under the initiative of the G-20 countries, the Organization for Economic Co-operation and Development (OECD) in its Base Erosion and Profit Shifting (BEPS) project had taken up the issue of base erosion and profit shifting by way of excess interest deductions by the MNEs in Action plan 4. The OECD has recommended several measures in its final report to address this issue.

In view of the above, sec. 94B was inserted in line with the recommendations of OECD BEPS Action Plan 4, to provide that interest expenses claimed by an entity to its associated enterprises shall be restricted to 30% of its earnings before interest, taxes, depreciation and amortization (EBITDA) or interest paid or payable to associated enterprise, whichever is less.

The provisions of sec. 94B are enumerated here-in-below:

Applicable to

Indian company, or a permanent establishment of a foreign company in India, being the borrower

- *Permanent establishment* includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.

Conditions

a) The borrower has debt issued by a non-resident, being an associated enterprise of such borrower.
   - *Debt* means any loan, financial instrument, finance lease, financial derivative, or any arrangement that gives rise to interest, discounts or other finance charges that are deductible in the computation of income chargeable under the head "Profits and gains of business or profession";

b) He incurs any expenditure by way of interest or of similar nature exceeding ₹ 1 crore;

c) Such expenditure is deductible in computing income chargeable under the head "Profits and gains of business or profession"

Effect

If all the aforesaid conditions are satisfied then, excess interest shall not be deductible in computation of income under the said head.

- Excess interest means lower of the following:
  a) An amount of total interest paid or payable in excess of 30% of earnings before interest, taxes, depreciation and amortisation (EBITDA) of the borrower in the previous year; or
  b) Interest paid or payable to associated enterprises for that previous year

Taxpoint

- *Guarantee*: Where the debt is issued by a lender which is not associated but an associated enterprise either provides an implicit or explicit guarantee to such lender or deposits a corresponding and matching amount of funds with the lender, such debt shall be deemed to have been issued by an associated enterprise.
- *Exception*:

  The provision of sec. 94B is not applicable:

  a) to an Indian company or a permanent establishment of a foreign company which is engaged in the business of banking or insurance; or

b) to interest paid in respect of a debt issued by a lender which is a permanent establishment in India of a non-resident, being a person engaged in the business of banking

- *Carry forward*: Where for any assessment year, the interest expenditure is not wholly deducted against income under the head "Profits and gains of business or profession", so much of the interest expenditure as has not been so deducted, shall be carried forward to the following assessment year(s), and it shall be allowed as a deduction against the profits and gains, if any, of any business or profession carried on by it and assessable for that assessment year to the extent of maximum allowable interest expenditure.
- *Maximum carried forward*: No interest expenditure shall be carried forward for more than 8 assessment years immediately succeeding the assessment year for which the excess interest expenditure was first computed.

Example

Computation of interest expenses disallowed u/s 94B: ₹ in crore

Particulars	Case 1	Case 2	Case 3
EBIDTA of the Indian Borrower	100	100	100
30% of the above **[A]**	30	30	30
Interest payable to associated enterprise **[B]**	35	Nil	15
Interest payable to non-associated enterprise **[C]**	Nil	35	20
Total Interest expense incurred **[D = B + C]**	35	35	35
Total interest expenses incurred in excess of 30% of EBITDA **[E = D - A]**	5	5	5
Interest payable to associated enterprise **[B]**	35	Nil	15
Excess interest [lower of (E) and (B)] being disallowed u/s 94B	**5**	**Nil**	**5**

YEARS OF CELEBRATING THE MAHATMA

GROUP: iv, PAPER: 17

CORPORATE FINANCIAL REPORTING (CFR)

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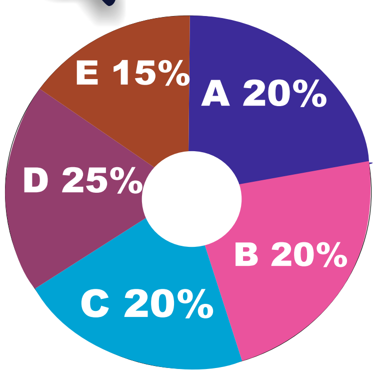
Your Preparation Quick Takes



Syllabus Structure

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

Learning Objectives:

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

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

Corporate Financial Reporting

An overview of Ind AS 116: Leases

At inception of a contract, an entity shall assess whether the contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the **right to control the use of an identified asset** for a period of time in exchange for consideration.

To assess whether a contract conveys the right to control the use of an identified asset for a period of time, an entity shall assess whether, throughout the period of use, the customer has both of the following: (a) the right to obtain substantially all of the economic benefits from use of the identified asset; and (b) the right to direct the use of the identified asset.

Accounting of leases in the books of the Lessee:

At the commencement date, the lessee shall recognise (I) a right-of-use asset and (II) a lease liability.

Exemption: A lessee may elect not to recognise under this standard

(i) short-term leases; and

(ii) leases for which the underlying asset is of low value.

No asset/ liability recognized under Ind AS 116 if the contract is not, does not contain a lease.

At the commencement date, **a lessee shall measure the right-of-use asset at cost**. The cost of the right-of-use asset shall comprise:

(i) the amount of the initial measurement of the lease liability

(ii) any lease payments made at or before the commencement date, less any lease incentives received;

(iii) any initial direct costs incurred by the lessee; and

(iv) an estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset, restoring the site on which it is located or restoring the underlying asset.

At the commencement date, a lessee shall measure the lease liability at the present value of the lease payments that are not paid at that date. **The lease payments shall be discounted using the interest rate implicit in the lease**, if that rate can be readily determined. If that rate cannot be readily determined, the lessee shall use the lessee's incremental borrowing rate.

At the commencement date, the **lease payments included in the measurement of the lease liability** comprise the following payments for the right to use the underlying asset during the lease term that are not paid at the commencement date:

(i) fixed payments (including in-substance fixed payments as described in paragraph B42), less any lease incentives receivable;

(ii) variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;

(iii) amounts expected to be payable by the lessee under residual value guarantees;

(iv) the exercise price of a purchase option if the lessee is reasonably certain to exercise that option; and

(v) payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

After the commencement date, a lessee shall measure the right-of-use asset applying a cost model, unless it applies the revaluation model as applied to the particular class of PPE.

To apply a cost model, a lessee shall measure the right-of-use asset at cost: (a) less any accumulated depreciation and any accumulated impairment losses; and (b) adjusted for any remeasurement of the lease liability specified.

A lessee shall **apply the depreciation requirements in Ind AS 16, Property, Plant and Equipment**, in depreciating the right-of-use asset (for the lease term or the useful life based on the lease condition).

If during lease any increase or decrease in liability arises when there exists a balance in ROU, to that extent ROU will be debited/credited and the balance would be transferred to P&L.

A lessee shall either present in the balance sheet, or disclose in the notes:

(a) **right-of-use assets separately from other assets**. If a lessee does not present right-of-use assets separately in the balance sheet, the lessee shall:

(i) include right-of-use assets within the same line item as that within which the corresponding underlying assets would be presented if they were owned; and

(ii) disclose which line items in the balance sheet include those right-of-use assets.

(b) **lease liabilities separately from other liabilities**. If a lessee does not present lease liabilities separately in the balance sheet, the lessee shall disclose which line items in the balance sheet include those liabilities.

The above requirement does not apply to right-of-use assets that meet the definition of investment property, which shall be **presented in the balance sheet as investment property**.
In the statement of profit and loss, a lessee shall present **interest expense** on the lease liability **separately from the depreciation charge** for the right-of-use asset. Interest expense on the lease liability is a component of finance costs, to be presented separately in the statement of profit and loss.

In the statement of cash flows, a lessee shall classify:

(a) cash payments for the principal portion of the lease liability within financing activities;

(b) cash payments for the interest portion of the lease liability within financing activities applying the requirements in Ind AS 7, Statement of Cash Flows, for interest paid; and

(c) short-term lease payments, payments for leases of low-value assets and variable lease payments not included in the measurement of the lease liability within operating activities.

(d) Any payments of **unrecognized lease arrangement** should also be treated like ©

Accounting of leases in the books of the Lessor:
A lessor shall classify each of its leases as either an operating lease or a finance lease.
A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset.
A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership of an underlying asset.
Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being **classified as a finance lease** are:

(a) the lease transfers ownership of the underlying asset to the lessee by the end of the lease term;
(b) the lessee has the option to purchase the underlying asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception date, that the option will be exercised;
(c) the lease term is for the major part of the economic life of the underlying asset even if title is not transferred;
(d) at the inception date, the present value of the lease payments amounts to at least substantially all of the fair value of the underlying asset; and
(e) the underlying asset is of such a specialised nature that only the lessee can use it without major modifications.

The net investment in the lease consists of the present value of the lease payments plus the present value of the guaranteed residual value, both discounted at the interest rate implicit in the lease, plus the present value of unguaranteed residual value, less deferred selling profit. (Deferred selling profit is calculated as the lease receivable less the carrying amount of the underlying asset, net of unguaranteed residual.) It may be mentioned that the net investment in the lease is subject to the same considerations as other assets when classifying its components as current or noncurrent assets in the balance sheet.
Interest income includes interest on the lease receivable, accretion of the unguaranteed residual value and amortisation of deferred selling profit. The rate for recognising interest income to produce a constant periodic rate of return on the remaining net investment is IRR.

Operating Lease
A lessor shall recognise lease payments from operating leases as income on either a straight-line basis or another systematic basis. The lessor shall apply another systematic basis if that basis is more representative of the pattern in which benefit from the use of the underlying asset is diminished.

A lessor shall recognise costs, including depreciation, incurred in earning the lease income as an expense.

A lessor shall add initial direct costs incurred in obtaining an operating lease to the carrying amount of the underlying asset and recognise those costs as an expense over the lease term on the same basis as the lease income.
The depreciation policy for depreciable underlying assets subject to operating leases shall be consistent with the lessor's normal depreciation policy for similar assets. A lessor shall calculate depreciation in accordance with Ind AS 16 and Ind AS 38.
A lessor shall apply Ind AS 36 to determine whether an underlying asset subject to an operating lease is impaired and to account for any impairment loss identified.

A manufacturer or dealer lessor does not recognise any selling profit on entering into an operating lease because it is not the equivalent of a sale.

Presentation
A lessor shall present underlying assets subject to operating leases in its balance sheet according to the nature of the underlying asset.

Disclosure
The objective of the disclosures is for lessors to disclose information in the notes that, together with the information provided in the balance sheet, statement of profit or loss and statement of cash flows, gives a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of the lessor.
A lessor shall disclose the following amounts for the reporting period:

(a) for finance leases: (i) selling profit or loss; (ii) finance income on the net investment in the lease; and (iii) income relating to variable lease payments not included in the measurement of the net investment in the lease.

(b) for operating leases, lease income, separately disclosing income relating to variable lease payments that do not depend on an index or a rate.

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150 YEARS OF CELEBRATING THE MAHATMA

GROUP: iv, PAPER: 18

INDIRECT TAX LAWS & PRACTICE (ITP)

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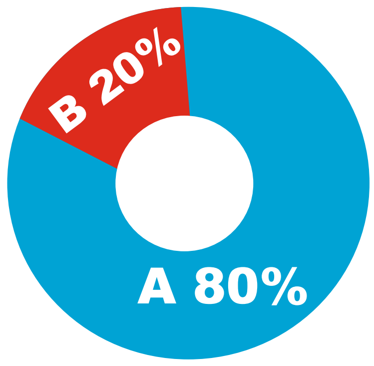
Your Preparation Quick Takes



Syllabus Structure

A Advanced Indirect Tax and Practice **80%**

B Tax Practice and Procedures **20%**

Learning Objectives –

Through the following MCQ, students can refresh themselves about

- Supply of services
- Composition levy
- Exempted supply / service
- Charitable activities
- Non taxable supply
- Nil rate of GST
- GST rates on services

INDIRECT TAX

Choose the correct option from the followings –

1. Which of the following will not be considered as Supply of Service.

(a) Transfer of right in goods or share (undivided) in goods without the transfer of title
(b) Lease, tenancy, easement, license to occupy land.
(c) Goods forming part of business are transferred or disposed off by the owner whether or not for a consideration.
(d) Any treatment or process which is applied to another person's goods.

2. Manufacturer of which following product can eligible to opt for composition levy

(a) Ice cream,other edible ice, whether or not containing cocoa.
(b) Vinegar and substitute for vinegar obtained from arctic acid.
(c) Tobacco and manufactured tobacco substitute.
(d) Aerated water.

3. In which of the following case power for granting exemption with the Central Government by notification will not apply

(a) General exemption
(b) Absolute exemption
(c) Conditional exemption
(d) Recommended exemption

4. In relation to conditional exemption which of the following statement is correct –

(a) Taxable person may avail the benefits
(b) Taxable person may or may not avail the benefits
(c) Taxable person must have to avail some part of the benefits
(d) Taxable person have to avail the partial benefits as per the recommendation of GST Council.

5. Which of the following will be considered ass exempted goods

(a) Exercise books
(b) Printed books
(c) Staplerrs
(d) pencils

6. For air embarking or terminating in an airport for transport of passengers with or without accompanied belongings in which of the Airport will be considered exempted service?

(a) Bagdogra Airport at Siliguri (West Bengal)
(b) Swami Vivekananda Airport at Raipur (Chhattisgarh)
(c) Dabolim Airport at Goa (Goa)
(d) Pantnagar Airport at Kumaon (Uttarakhand)

7. Which of the following will be considered Charitable activities in relation to advancement of educational program or skill development relating to

(a) Residents of old age home
(b) Person residing at asylum
(c) Pensioners
(d) Senior citizen residing at rural area

8. **Any school allow other school to the name, it's logo and moto and received collaboration fees , comprised of non refundable amount and annual fees against those, will be considered as**
   (a) Branch
   (b) Partnership
   (c) Association
   (d) Franchise service

9. **Which one of the following will be considered as exempted supply / service provided by Government or Local Authority**
   (a) Transport of goods or passengers
   (b) Express Parcel Post Office services by department of post provided to a business entity
   (c) Speed Post services provided by department of post to a business entity
   (d) Other services provided to business entity whose P.Y. turnover is 22 lakhs.

10. **Which of the following is Non Taxable Supply**
   (a) Residential house taken on rent for commercial purpose
   (b)Renting of precincts place meant for general public managed by an entity registered as charitable trust
   (c)House is given on rent and the same is used as a hotel or lodge
   (d) Rooms in a hotel or a lodge let out where tariff per day per room Rs 1000/- or more

11. **Which of the following service relating to transportation of passengers not covered under NIL rate of GST?**
   (a) Metro
   (b) Tramways
   (c) Metered cab
   (d) Air conditioned railway coach

12. **GST rate for transportation of goods by Rail or Vessel is**
   (a) 5%
   (b) 9%
   (c) 12%
   (d) 18%

13. **Which of the agricultural activities exempted from GST**
   (a) Commission on sale of agriculture product
   (b) Warehousing of processed agricultural product
   (c) Agriculture extension services
   (d) Services by any agricultural produce marketing committee

14. **Which one of the following is not exempt from GST**
   (a) The Central Electricity Authority
   (b) A State Electricity Board
   (c) A State Transmission Utility
   (d) Supplier of power through Generator in rural areas.

15. **Services by way of right to admission to a Planetarium is exempt from GST if admission is not more than**
   (a) Rs 100/-
   (b) Rs 250/-
   (c) Rs 500/-
   (d) Rs 750/-

16. **Mr X is a practicing CMA provided services to CMA Institute by way of teaching to students**
   (a) Taxable supply
   (b) Exempted supply
   (c) Nil rate of tax
   (d) TCS will be applicable

17. **Goods disposed off by way of a free sample**
   (a)Recipient can claim ITC
   (b)ITC can be claimed by upplier
   (c)ITC can not claim by supplier
   (d)If value of the sample is less than Rs 500/- ITC can be claimed

18. **Supply of lottery authorised by State Government shall attract GST**
   (a) @ 5%

(b) @ 12%
(c) @ 18%
(d) @ 28%

19. Services supplied by Insurance Agent to any person carrying on insurance business, the liability to pay GST will be
(a) An insurance agent
(b) Insurance company
(c) Recipient of service
(d) Policy holder

20. Which one of the following will not be considered as exempt supply
(a) Supplies taxable at NIL rate of tax
(b) Non GST supply
(c) Supplies that are wholly or partially exempted from GST or IGST by way of a notification.
(d) Non taxable supplies as defined under Section 2(78)

ANSWERS

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

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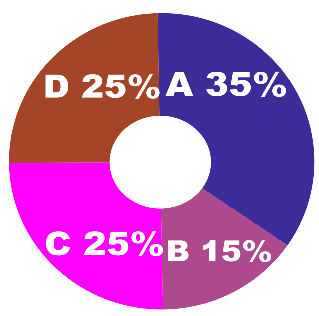
GROUP: iv, PAPER: 19

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

Problem on Reconciliation of Cost Records and Financial Records

Question

The Profit & Loss Account of ABC Steels Ltd for the year ended 31st March 2021 is as follows.

(Rupees)

Si. No.	Particulars	Year ended 31.03.2021
1.	Income	
	a. Revenue from Operation	4,50,45,300
	b. Other income	39,10,510
	Total Income	**4,89,55,810**
2.	Expenses	
	a. Cost of Material Consumed	3,02,17,200
	b. Change in inventories of finished goods	28,12,480
	c. Cost of Utilities	42,01,460
	d. Employee Cost	44,10,150
	e. Finance cost	8,93,820
	f. Depreciation & Amortisation	11,29,030
	g. Other expenses	8,46,760
	Total Expenses	**4,45,10,900**
3.	**Profit /(Loss) before exceptional item & Tax**	**44,44,910**
4.	Exceptional Items	2,34,700
5.	**Profit before Tax**	**42,10,210**

On review of above Profit and Loss Account during course of cost audit, the following issues observed.

Sl. No.	Particulars	Rupees.
1.	Revenue from operation includes Exceptional Rebate allowed to customers	1,28,550
2.	**Cost of materials includes :-**	
I	Demurrage charge on Raw materials	12,300
ii.	Cost of Material includes prior period adjustments	37,800
iii.	Raw Material brought from USA valued in F/A as on date of payment. Values as on the date of payment-	2,15,000

	Values as on the date of transaction- Values as on the date of receipt of material-	2,40,000 2,50,500
3.	**Other income in F/A includes: -**	
I	Profit on Sale of Fixed Assets	2,05,000
ii.	Bad debt recovered	45,850
iii.	Insurance Claim received for natural disaster	2,08,700
iv.	Profit from Retail trading activity	80,430
v.	Interest Income from Inter-Corporate Deposits	1,61,500
4.	**Employee Cost in F/A includes**	
I	Overtime premium	4,25,000
ii.	Arrear salary relating to 2017-18	85,760
iii.	Salary paid to contractual employee	78,900
iv.	Free housing and free conveyance	1,45,650
v.	Recruitment cost & training cost	80,500
vi.	Penalty due to noncompliance to Labour act	65,600
5.	**Other expenses includes:**	
I	Donation Paid	75,000
ii.	Loss on Sale of Investments	33,600
6.	Decrease in value of Closing WIP and Finished goods inventory :-	
	as per Financial Accounts	28,12,430
	as per Cost Accounts	36,02,500

You are required to arrive the Profit / (Loss) as per Cost records and prepare a Reconciliation Statement between the two Accounts for the year ended March 31, 2021.

Answer:

Reconciliation of Profit between Cost and Financial Accounts for the year ended March 31, 2021

Particulars	Amount (Rs.)	Amount (Rs.)
Profit as per Financial Accounts		**42,10,210**
Add: Expenses considered in financial accounts but not considered in cost records		
Demurrage charge on Raw material	12,300	
Cost of Material includes prior period adjustment	37,800	
Loss on Sale of Investments	33,600	
Arrear salary relating to 2017-18	85,760	
Penalty due to noncompliance to Labour Act	65,600	
Rebate allowed to customers	1,28,550	
Donation Paid	75,000	
		4,38,610

Less: Income considered in financial accounts but not considered in cost records		
Difference in valuation of imported raw material (2,40,000-2,15,000)	25,000	
Profit on Sale of Fixed Assets	2,05,000	
Bad debt recovered	45,850	
Interest Income from Inter-Corporate Deposits	1,61,500	
Insurance Claim received for natural disaster	2,08,700	
Profit from Retail trading activity	80,430	
Decrease in value of Closing WIP and Finished goods inventory :-(36,02,500 - 28,12,430)	7,90,070	
		15,16,550
Profit as per Cost Accounts		**31,32,270**

Note:

1. As per CAS-6, The forex component of imported material cost shall be converted at the rate on the date of the transaction. Any subsequent change in the exchange rate till payment or otherwise shall not form part of the material cost.

2. As per CAS-7:

i. Employee cost includes benefits paid to temporary, part time & contract employees.

ii. Employee cost includes benefit paid to employee such as free housing, free conveyance etc.

iii. Overtime premium, recruitment cost & training cost are part of employee cost.

150 YEARS OF CELEBRATING THE MAHATMA

GROUP: iv, PAPER: 20

STRATEGIC PERFORMANCE MANAGEMENT AND BUSINESS VALUATION (SPBV)

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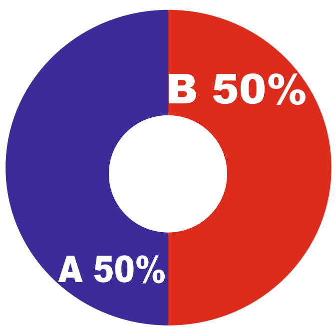
Your Preparation Quick Takes



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

Problem 1

D Ltd. furnishes the following information relating to the previous three years:

(Rs. In Lakhs)

Particulars	2014	2015	2016
Profit before interest and tax	75.00	5.00	150.00
Loss in Sale of Assets	3.00	-	18.00
Non-operating income	12.00	7.25	8.00

Inflation was 9% for 2015 and 15% for 2016. The capitalization factor considering internal and external value drivers to the brand is 14. Assume an all-inclusive future tax rate of 35%.

(i) Compute year-wise brand earnings. 3 Marks

Answer:

Valuation of Brand of D Ltd. as at 31-3-2016 (Rs. in lakhs)

Particulars	2014	2015	2016
Profit before interest and tax	75.00	5.00	150.00
Add: Loss in Sale of Assets	3.00	-	18.00
Less: Non-operating income	(12.00)	(7.25)	(8.00)
Branded Earnings	66.00	78.00	160.00

(ii)Determine the brand value of D Ltd. 5 Marks

Particulars	2014	2015	2016
Inflation Adjustment Factor	1.09×1.15=1.25	1.15	1.00
Inflation Adjusted Earning as at 31.03.2016 (Rs. in lakhs)	82.50	89.70	160.00
Weight	1	2	3
Product	82.50	179.40	480.00
Weighted Average Earnings Before Tax [(82.50+179.40+480)÷(1+2+3)] (Rs. in lakhs)			123.65
Less: Taxes at 35%			(43.28)
Weighted Average Brand Earnings After Tax (Rs. in lakhs)			80.37
Capitalization Factor			14
Brand Value			Rs.1125.18 Lakhs

Note: Most recent year is given higher weight.

Problem 2

Cost = $300x - 10x^2 + \quad x^3$

(i) Calculate the Output at which Marginal Cost is minimum.	2 Marks

Answer: Cost = $300x - 10x^2 + \frac{1}{3}x^3$

Marginal Cost = $\frac{dc}{dx}$ = $300 - 20x + x^2$ (say, y)

In order that MC is minimum first derivate must be equal to zero and 2nd derivate must be positive.

So, $\frac{dy}{dx} = 2x - 20 \Rightarrow 2x = 20$

$x = 10$

$\frac{d^2y}{dx^2}$ = 2, which is positive. It is minimum at x = 10.

(ii) Compute Output at which Average Cost is minimum.	3 Marks

Answer:

Answer: Cost = $300x - 10x^2 + \frac{1}{3}x^3$

$\frac{dy}{dx} = -10 + \frac{2}{3}x = 0$

$\Rightarrow x = 30/2 = 15$

$\frac{d^2y}{dx^2} = \frac{2}{3} > 0$

So, Average Cost is minimum of output at x = 15.

(iii) Calculate Output at which Marginal Cost = Average Cost.	3 Marks

Answer:

Output at which Marginal Cost = Average Cost

$300 - 20x + x^2 = 300x - 10x^2 + \frac{1}{3}x^2$

$-20x + 10x + x^2 - \frac{1}{3}x^2 = 0$

$-10x + \frac{2}{3}x^2 = 0$

$(-30x - 2x^2)/3 = 0$

$2x^2 - 30x = 0$

$2x(x - 15) = 0$

$X - 15 = 0$

So, $x = 15$

Problem 3

A Ltd., is trying to buy B Ltd., B Ltd. is a small bio-technology firm that develops products that are licensed to major pharmaceutical firms. The development costs are expected to generate negative cash flows of Rs. 10 lakhs during the first year of the forecast period. Licensing fee is expected to generate positive cash flows of Rs.5 lakhs, Rs. 10 lakhs, Rs. 15 lakhs and Rs. 20 lakhs during 2-5 years respectively. Due to the emergence of competitive products, cash flows are expected to grow annually at a modest 5% after the fifth year. The discount rate for the first five years is estimated to be 15% and then drop to 8% beyond the fifth year.

Given: The discount rate @ 15% will be:

Year	1	2	3	4	5
Discount Rate	0.869	0.756	0.6575	0.572	0.497

(i) Calculate Total Present Value. 4 Marks

Answer:

Year	Cash flows (` In lakhs)	Discount rate @15%	Present Value (` in lakhs)
	(10)	0.869	(8.69)
	5	0.756	3.78

	10	0.6575	6.575
	15	0.572	8.58
	20	0.497	9.94
Total sum of present value			20.185

(ii) Compute the value of the firm. 4 Marks

Answer:
Terminal Value $_t$ = Cash Flow $_{t+1}$ / r-G_{stable}
Cash Flow $_{t+1}$ = Cash flow (1+g) = 20 (1+0.05) = Rs. 21 Lakhs
Terminal Value = Rs.21/(0.08-0.05) = Rs.700 Lakhs.
Present value of terminal value = Rs.700 x 0.497 = Rs.347.9 Lakhs
Value of the firm = Total sum of present value + Present value of terminal value
= Rs.20.185 + Rs. 347.9 = Rs. 368.085 Lakhs.

Problem 4

The following information is available of a concern; calculate E.V.A.:

Debt capital 12%	Rs.4,000 crores
Equity capital	Rs.1,000 crores
Reserve and Surplus	Rs.15,000 crores
Capital employed	Rs.20,000 crores
Risk-free rate	8%
Beta factor	1.05
Market rate of return	18%
Equity (market) risk premium	10%
Operating profit after tax	Rs.4,200 crores
Tax rate	30%

(i) Compute Cost of Equity Capital 4 Marks

Answer:
E.V.A. = NOPAT – COCE
NOPAT = Net Operating Profit after Tax
COCE = Cost of Capital Employed
COCE = Weighted Average Cost of Capital x Average
Capital Employed = WACC x Capital Employed
Debt Capital Rs.4,000 crores
Equity capital Rs.1,000 + Rs.15,000 = Rs.16,000 crores
Capital employed = Rs.4,000 + Rs.16,000 = Rs. 20,000 crores

Debt to capital employed = $\frac{4,000}{20,000}$ = 0.20

Equity to capital employed = $\frac{16,000}{20,000}$ = 0.20

Debt cost before tax	12%
Less: Tax (30% of 12%)	3.6%
Debt cost after Tax	8.4%

According to capital Asset Pricing Model (CAPM)
Cost of Equity Capital = Risk Free Rate + Beta x Equity Risk Premium
Or
= 9 + [1.05 x (18 - 8)]
= 9 + (1.05 x 10) = 19.5%

(ii) Calculate WACC. 2 Marks
Answer:

Answer:

WACC = Equity to CE
Cost of Equity capital +Debt to CE
Cost of Debt = 0.8
19.5% + 0.20
8.40% = 15.60% + 1.68% =17.28%

(i) Compute COCE 1 Mark

Answer:

COCE = WACC
Capital employed = 17.28%
Rs.20,000 crores =Rs.3,456 crores

(ii) Calculate EVA 1 Mark

Answer:

E.V.A = NOPAT – COCE = Rs. 4,200 – Rs. 3,456 =Rs.744 crores

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, Attend Webinar sessions**

02 **Solve Excercises given in Study Note**

03 **Assess Yourself**

04 **Appear For Examination**

FINISHED

SUBMISSIONS

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,

Passing the exam is a happy event. Congratulations on all that you have accomplished! There is no secret of success. It is the result of preparation, hard work and learning from failure. Well done! It is clear that the future holds great opportunities for you.

Those who could not pass, failing in an exam does not mean failing in life. All of us face failure at one time or another. Try to focus your attention on the importance of perseverance and mind it that dedication and determination plays the lead role in shaping a person's life.

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, Mock Test Papers (MTPs), Work Books, MCQs and we have conducted Webinar sessions.

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:

"You must be the Change you wish to see in the World",

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 link mentioned below :

https://icmai.in/studentswebsite

- Don't give up
- Don't give in
- Don't give out

You can win!

The Institute is pleased to inform that the University Grants Commission (UGC) Ministry of Education, Govt. of India has announced that CMA qualification be Considered equivalent to PG Degree.

GOOD LUCK

Be Prepared and Get Success;

Few Snapshots

Group Photo- MDP Kolkata during valedictory session on 27-Aug 21

As part of CAT & AAT Board ICAI initiative, team of delegates from Institute CMA P Raju Iyer, Vice President, CMA Rakesh Singh, Former President, CMA Vijender Sharma, Chairman PD, CMA Dr K Ch A V S N Murthy, Chairman RC & CC, Journal, CMA Chittaranjan Chattopadhyay, Chairman BFSI Board and CMA H Padmanabhan, Chairman CAT and AAT Board met Shri. A Namassivayam, Minister Puducherry-Home, Education, Industries & Commerce, Electricity, Sports, Sainik Welfare

As part of initiative of CAT and AAT Board ICAI our Institute CMA P Raju Iyer Vice President, CMA Rakesh Singh Former President, CMA Vijender Sharma, Chairman PD, CMA Chittaranjan Chattopadhyay, Chairman BFSI Board, CMA Dr K Ch A V S N Murthy, Chairman RC & CCC and CMA H Padmanabhan, Chairman CAT and AAT Board met Shri N. Rangaswamy, Honorable Chief Minister of Puducherry UT

CMA Chittaranjan Chattopadhyay Chairman BFSI Board, CMA Vijender Sharma and CMA H Padmanabhan met BANK top management Shri. P Suresh, Puducherry Head and handed over BFSI Publication after discussing scope for PCMAs and IPAs in Banking Industry

CMA Neeraj D. Joshi, Chairman, Management Accounting Committee and CMA (Dr.) Ashish P. Thatte, Chairman, Corporate Laws Committee had an opportunity to greet Dr. Bhagwat Kishanrao Karad, Hon'ble Union Minister of State for Finance on 29th July, 2021

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