ICMAI
THE INSTITUTE OF
COST ACCOUNTANTS OF INDIA
भारतीय लागत लेखाकार संस्थान
Statutory Body under an Act of Parliament
(Under the jurisdiction of Ministry of Corporate Affairs)
www.icmai.in

CMA STUDENT E-Bulletin

VOL 11 | NO. 08 | AUGUST 2026

An Initiative of Directorate of Studies

Behind every successful business decision, there is always a CMA

About the Institute

The Institute of Cost Accountants of India (ICMAI) is a statutory body set up under an Act of Parliament in the year 1959. The Institute as a part of its obligation, regulates the profession of Cost and Management Accountancy, enrols students for its courses, provides coaching facilities to the students, organizes professional development programmes for the members and undertakes research programmes in the field of Cost and Management Accountancy. The Institute pursues the vision of cost competitiveness, cost management, efficient use of resources and structured approach to cost accounting as the key drivers of the profession. In today's world, the profession of conventional accounting and auditing has taken a back seat and cost and management accountants increasingly contributing towards the management of scarce resources like funds, land and apply strategic decisions. This has opened up further scope and tremendous opportunities for cost accountants in India and abroad.

The Institute is headquartered in New Delhi having four Regional Councils at Kolkata, Delhi, Mumbai and Chennai, 113 Chapters in India and 11 Overseas Centres. The Institute is the largest Cost & Management Accounting body in the world with about 1,00,000^{+} qualified professionals and over 6,00,000^{+} students pursuing the CMA Course. The Institute is a founder member of International Federation of Accountants (IFAC), Confederation of Asian and Pacific Accountants (CAPA) and South Asian Federation of Accountants (SAFA). The Institute is also an Associate Member of ASEAN Federation of Accountants (AFA) and member in the Council of International Integrated Reporting Council (IIRC), UK.

Vision Statement

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

Mission Statement

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

Institute Motto

असतोमा सद्गमय तमसोमा ज्योतिर् गमय मृत्योर्मामृतं गमय ॐ शान्ति शान्ति शान्तिः	From ignorance, lead me to truth From darkness, lead me to light From death, lead me to immortality Peace, Peace, Peace

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CHAIRMAN'S COMMUNIQUE

Dear CMA Students,

It gives me immense pleasure to connect with you through the August 2026 issue of the CMA Student E-Bulletin. As the Chairman of the Training & Educational Facilities Committee of ICMAI, I am excited to share the latest developments and initiatives that aim to enhance your learning experience and professional growth.

At ICMAI, our commitment to excellence in education and training remains unwavering. We continuously strive to provide you with the best resources, state-of-the-art facilities, and cutting-edge training programs that will prepare you to excel in the field of cost and management accounting. Your success is our primary motivation, and we are dedicated to supporting you every step of the way.

In today's digital age, leveraging technology to facilitate learning is paramount. We have introduced several innovative learning platforms to ensure that you have access to high-quality education regardless of your location. Our online classes, interactive webinars, and virtual workshops provide you with the flexibility to learn at your own pace while maintaining the highest standards of education.

In addition to theoretical knowledge, practical skills are crucial for your professional development. We have designed a variety of skill development programs that focus on real-world applications and industry-relevant practices. These programs include case studies, simulation exercises, and hands-on training sessions that bridge the gap between academic knowledge and practical implementation.

Our collaborations with leading organizations and industry experts provide you with invaluable insights and opportunities to apply your knowledge in real-world scenarios. Through internships, live projects, and guest lectures, you can gain practical experience and understand the nuances of the industry. These collaborations also open doors to networking opportunities that can be instrumental in your career growth.

At ICMAI, we believe in the holistic development of our students. Alongside academic excellence, we emphasize the importance of soft skills such as communication, leadership, and teamwork. Our comprehensive training programs include workshops and seminars focused on developing these essential skills, ensuring that you are well-rounded professionals ready to take on leadership roles.

I am confident that the initiatives and programs we have implemented will significantly enhance your learning experience and prepare you for a successful career. I encourage you to take full advantage of these opportunities and remain dedicated to your goals.

I extend my best wishes to all of you. Your hard work, determination, and passion are the driving forces behind our efforts. Let us continue to work together to achieve excellence and elevate the standards of the cost and management accounting profession.

Warm regards,

CMA Vinayranjan P.

Chairman, Training & Educational Facilities Committee, ICMAI

CMA FOUNDATION COURSE

Syllabus 2022

Topic

Fundamentals of Business Laws -

Module 2: Indian Contracts Act, 1872

Business Communication -

Module 5: Business Communication

FOUNDATION

Paper-1

Fundamentals of Business Laws and Business Communication (FBLC)

SECTION – A: FUNDAMENTALS OF BUSINESS LAWS

1. A offers to sell his car to B. Before B communicates acceptance, B receives reliable information that A has died. B nevertheless sends an acceptance. Which of the following is correct?
   a) A valid contract is formed
   b) The offer is revoked due to A's death known to B before acceptance
   c) The legal heirs are bound by the offer
   d) The contract is voidable
2. A debtor owes ₹1,00,000 to a creditor. The creditor voluntarily accepts ₹80,000 in full satisfaction of the debt. This is known as:
   a) Novation
   b) Rescission
   c) Remission
   d) Alteration
3. A agrees to sell a painting to B. Before delivery, the painting is accidentally destroyed without the fault of either party. The contract is:
   a) Valid and enforceable
   b) Void due to destruction of the subject matter
   c) Voidable at B's option
   d) Illegal
4. Under the Indian Contract Act, consideration may be:
   a) Past only
   b) Present only
   c) Future only
   d) Past, present, or future
5. A agrees to indemnify B against any loss arising from a fire in B's warehouse. The agreement is made orally. Later, a fire occurs and B suffers a loss. Can B enforce the agreement?
   a) No, because a contract of indemnity must always be in writing
   b) Yes, because an oral contract of indemnity is valid if the essentials of a contract are present
   c) No, because indemnity requires registration
   d) Yes, only if witnessed by two persons
6. A person accepts goods knowing they were delivered by mistake and refuses either to return them or pay for them. He is liable because:
   a) He committed fraud
   b) The law imposes an obligation to prevent unjust enrichment
   c) The delivery amounts to a gift
   d) The contract is implied by writing
7. A promise to contribute money for a charitable purpose is generally:
   a) Always enforceable
   b) Enforceable only if accepted
   c) Not enforceable unless supported by consideration or other legal grounds
   d) Illegal
8. A contract entered into with a person of unsound mind during a period when he is incapable of understanding the agreement is:
   a) Void
   b) Voidable
   c) Valid
   d) Illegal
9. The object of awarding nominal damages is to:
   a) Punish the defaulting party
   b) Compensate for substantial loss
   c) Recognize the infringement of a legal right where no actual loss is proved
   d) Prevent future contracts
10. A promises to deliver machinery to B in exchange for B's old machinery plus ₹2 lakh. This is an example of:
    a) Agreement without consideration
    b) Consideration consisting partly of an act and partly of money
    c) Gratuitous promise
    d) Quasi-contract
11. If a contract contains reciprocal promises and one party prevents the other from performing, the affected party:
    a) Must still perform his obligation
    b) May treat the contract as voidable and claim compensation
    c) Can only seek specific performance
    d) Has no legal remedy

12. A person who supplies necessaries to a person incapable of contracting is entitled to:
    a) Recover the amount personally from that person
    b) Recover only from the incapable person's property
    c) Recover from the Government
    d) Recover from the guardian personally in every case
13. A and B enter into an agreement believing a cargo ship is on its way to India. Unknown to both, the ship had already sunk before the agreement. The agreement is:
    a) Valid
    b) Void due to bilateral mistake
    c) Voidable
    d) Illegal
14. Which of the following best describes an executed contract?
    a) A contract yet to be performed by both parties
    b) A contract fully performed by both parties
    c) A contract that is voidable
    d) A contingent contract
15. A principal is bound by the acts of an agent acting within:
    a) Personal discretion only
    b) Actual authority (whether express or implied)
    c) Express authority only
    d) Judicial authority only
16. Which of the following is not an essential element of a valid contract?
    a) Lawful object
    b) Competency of parties
    c) Social relationship between parties
    d) Free consent
17. A contract in which one party has performed his obligation while the other has yet to perform is called:
    a) Executed contract
    b) Unilateral contract
    c) Void contract
    d) Contingent contract
18. An agreement whose object or consideration is forbidden by law is:
    a) Void only
    b) Void and illegal
    c) Voidable
    d) Valid until challenged
19. Which of the following is an example of an implied contract?
    a) A written employment agreement
    b) Purchasing goods from a self-service supermarket and paying at the counter
    c) A registered lease deed
    d) A notarized guarantee agreement
20. The maxim "Consensus ad idem" refers to:
    a) Equality before law
    b) Meeting of the minds upon the same thing in the same sense
    c) Performance of reciprocal promises
    d) Compensation for breach
21. In a contract of guarantee, the creditor gives additional time to the principal debtor without the surety's consent. The surety is generally:
    a) Always liable
    b) Discharged from liability
    c) Liable only for half the debt
    d) Liable only if the principal defaults again
22. A bailee mixes the bailor's goods with his own goods without the bailor's consent, and the goods cannot be separated. The bailee must:
    a) Return only his own goods
    b) Bear the loss and compensate the bailor
    c) Become the owner of all goods
    d) Sell all goods and divide the proceeds equally
23. A principal, after becoming aware of all material facts, expressly approves an unauthorized act of his agent. The approval:
    a) Creates a new agency from that date only
    b) Operates retrospectively as if authority originally existed
    c) Makes the contract void
    d) Is ineffective unless registered

24. A contract where the promisor undertakes an obligation only on the occurrence or non-occurrence of a collateral event is called:

    a) Void contract

    b) Contingent contract

    c) Quasi-contract

    d) Executed contract

25. A customer receives a reply to his complaint that is factually correct but fails to address the issue raised in the complaint. Which principle of effective business communication has been violated?

    a) Completeness

    b) Courtesy

    c) Concreteness

    d) Clarity

26. During a business presentation, the presenter avoids reading directly from slides and instead maintains eye contact with the audience while explaining the content. This primarily improves:

    a) Semantic accuracy

    b) Audience engagement through effective non-verbal communication

    c) Formality of communication

    d) Written communication skills

27. A customer complains about receiving a damaged product. Before suggesting a replacement, the customer service executive carefully understands the customer's inconvenience and offers a solution that best meets the customer's needs. Which principle of effective business communication is best demonstrated?

    a) Consideration

    b) Concreteness

    c) Conciseness

    d) Correctness

28. Which of the following is the most suitable communication channel for informing all employees immediately about an unexpected office closure due to a natural disaster?

    a) Annual Report

    b) Internal Notice Board only

    c) Instant SMS/Official Mobile Alert and Email

    d) Printed Circular sent by post

29. A speaker frequently uses filler words such as "um", "you know", and "actually" during a business presentation. These fillers mainly affect:

    a) Courtesy

    b) Fluency and professionalism of oral communication

    c) Feedback

    d) Confidentiality

30. A multinational company encourages employees to ask questions after every training session to ensure concepts have been understood correctly. This practice mainly strengthens:

    a) Encoding

    b) Feedback and two-way communication

    c) Grapevine communication

    d) Upward communication only

Answer:

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
b	c	b	d	b	b	c	a	c	b	b	b	b	b	b
16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
c	b	b	b	b	b	b	b	b	a	b	a	c	b	b

Topic

Fundamentals of Financial Accounting -

Module 1: Accounting Fundamentals

Fundamentals of Cost Accounting -

Module 4: Fundamentals of Cost Accounting

FOUNDATION

Paper-2

Fundamentals of Financial and Cost Accounting (FFCA)

FUNDAMENTALS OF FINANCIAL AND COST ACCOUNTING

Sl. No.	Questions	Alternative Answers ('tick' the correct one)			
		A	B	C	D
1	Making entries from Journal to Ledger is called	Recording	Entering	Posting	Ledgering
2	From the balances of which accounts net profit/loss can be ascertained	Real	Nominal	Personal	Ledger Balance
3	Classification and condensation are to be done in	Journal	Ledger	Trial Balance	Balance Sheet
4	In which Account a Furniture Dealer will Debit for purchase of Furniture	Furniture Account	Purchases Account	Revenue Account	Creditor Account
5	Premia paid on Life Insurance Policy of the proprietor will be debited to	Capital Account	Drawings Account	Premium Expense Account	Bank Account
6	In which Account Pre-paid insurance will be credited ?	Insurance Account	Pre-paid Insurance A/C	Debtors Account	Creditors Account
7	Loss of goods by fire should be credited to	Capital Account	Loss of Goods by Fire A/C	Purchases Account	Drawings Account
8	In which account excess of liabilities over asset in the opening entry will be debited ?	Capital Reserve Account	Asset Account	Goodwill Account	Liabilities Account
9	Discount allowed to a Debtor is credited to -	Discount Allowed A/C	Discount Received A/C	Debtor Account	Cash Book A/C
10	Cash Discount received from a Creditor is Debited to-	Purchases Account	Cash Account	Discount Account	Creditors Account
11	Discount recorded in Debit side of a Cash Book is -	Discount Received	Discount Allowed	Trade Discount Received	Trade Discount Allowed
12	When a Suspense Account is opened	Bal. transfer from Ledger	Final Account is prepared	Something is doubtful	Trial Balance not agreed
13	What is the nature of Suspense Account	Real Account	Personal Account	Nominal Account	None of these
14	Charging Depreciation is -	Compulsory	Voluntary	Conditional	For Tax purposes only
15	Loss on sale of Asset is debited to -	Capital Reserve Account	Profit & Loss Account	Bank Account	Asset Account
16	Straight Line Method depreciation is calculated on -	Market value of Asset	Written Down value	Original Cost of Asset	Original Cost less Scrap
17	In which account probable non-recovery of debt will be credited-	Bad Debt Account	Creditors Account	Debtors Account	Bad & Doubtful Debt Provision A/c
18	Bad Debt is actually a type of -	Income	Asset	Liability	Loss
19	Recovery of bad debt is credited to -	Bad Debt Account	Provision for Bad Debt A/C	Profit & Loss A/C	None of these
20	Type of expenditure to give benefit for more than one accounting period is	Capital expenditure	Revenue Expenditure	Deferred Revenue Expenditure	Long term Expenditure

Sl. No.	Questions	Alternative Answers ('tick' the correct one)			
		A	B	C	D
21	Licence Fees for importing a Machine is debited -	Licence Fees Account	Machinery Account	Import Expense A/C	General Expense A/C
22	Which inventory valuation method assumes materials issued first are the oldest purchases?	LIFO	FIFO	Weighted Average	Standard Cost
23	Idle Time Cost due to machine breakdown is classified as:	Abnormal Cost	Direct Cost	Normal Cost	Part of total cost
24	Cost Unit means:	Unit of product or service for which cost is computed	Amount for the Unit Cost	Cost Measurement	No. of pieces
25	Which one is a variable cost?	Factory Rent	Depreciation under SLM	Direct Materials	Insurance Premia
26	Process Costing is most appropriate for:	Shipbuilding	Printing Press	Oil Refinery	Housing Project
27	Cost Sheet is prepared mainly to:	Ascertain Costing Profit	Ascertain cost of Production	Ascertain cost efficiency	Ascertain GST
28	Which cost remains constant per unit?	Fixed Cost	Variable Cost	Step Cost	Breakeven Cost
29	Standard Costing is mainly a technique of -	Cost Reduction	Cost Behaviour	Cost Control	Cost Comparison
30	Break-even Point occurs where:	Sales = Variable Cost	Fixed Cost = Variable Cost	Sales = Profit	Total Revenue = Total Cost

Answer:

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
C	B	B	B	B	A	B	C	C	D	B	D	D	B	B
16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
D	D	D	D	A	B	A	A	A	C	C	B	B	C	D

Topic

Fundamentals of Business Mathematics -

Module 1: Arithmetic

Fundamentals of Business Statistics -

Module 2: Algebra

Module 5: Measures of Central Tendency and Dispersion

FOUNDATION

Paper-3

Fundamentals of Business Mathematics and Statistics (FBMS)

FUNDAMENTALS OF BUSINESS MATHEMATICS AND STATISTICS

In this issue we will carry out MCQs on Arithmetic and Measures of Central Tendency and Dispersion--Refer Module 1 and Module 5 of Study guide

1. When the number 418 in decreased in the ratio of 19: 16, the new number is

   (a) 352

   (b) 325

   (c) 496

   (d) 469

2. For the ratio X : Y

   (a) The duplicate ratio is 2X : 2Y

   (b) The duplicate ratio is (X/2) : (Y/2)

   (c) The duplicate ratio is $(X^2) : (Y^2)$

   (d) The duplicate ratio is $\sqrt{X} : \sqrt{Y}$

3. For the ratio X : Y, Sub triplicate ratio is

   (a) $\sqrt[3]{X} : \sqrt[3]{Y}$

   (b) $X^3 : Y^3$

   (c) 3X : 3Y

   (d) $\sqrt[1/3]{X} : \sqrt[1/3]{Y}$

4. If $\frac{1 + x + x^2}{1 - x + x^2} = \frac{62(1+x)}{63(1-x)}$ then value of x is

   (a) 1/3

   (b) 1/5

   (c) 1/4

   (d) 1/9

5. In a fraction $\frac{a}{b}$

   (a) The numerator a is called the antecedent of the ratio and denominator b is called the consequent of the ratio

   (b) The numerator a is called the consequent of the ratio and denominator b is called the antecedent of the ratio

   (c) The antecedent a is called the numerator of the ratio and consequent b is called the denominator of the ratio

   (d) The consequent a is called the numerator of the ratio and antecedent b is called the denominator of the ratio

6. If A varies as B and C jointly while B varies as D^2 and C varies inversely as A then

   (a) $A \propto D^2$

   (b) $A \propto \sqrt{D}$

   (c) $AD \propto BC$

   (d) $A \propto D$

7. If (x - 9) : (3x + 6) is the duplicate ratio of 4 : 9, the value of is

   (a) 1

   (b) 25

   (c) 12

   (d) 9

8. The number which has the same ratio with $\frac{4}{9}$ as $\frac{2}{11}$ has with $\frac{7}{33}$ is

   (a) $\frac{9}{22}$

   (b) $\frac{7}{21}$

   (c) $\frac{8}{21}$

   (d) $\frac{3}{11}$

9. What number must be added to each of the numbers 8, 13 and 20 so that the resulting numbers may be in continued proportion?

   (a) 4

   (b) 4.50

   (c) 5

   (d) 6.50

10. A ratio of greater inequality

    (a) is increased by adding the same positive number to both its antecedent and consequent

    (b) is increased by multiplying the same positive number to both its antecedent and consequent

(c) is diminished by adding the same positive number to both its antecedent and consequent

(d) is diminished by multiplying the same positive number to both its antecedent and consequent

11. If $A \propto BC$ and $B \propto CA$,then

(a) A is a constant

(b) B is a constant

(c) C is a constant

(d) $AB \propto C^2$

12. If $A \propto B$ and $C \propto D$, then

(a) $\frac{A}{C} \propto \frac{D}{B}$

(b) $\frac{A}{C} \propto \frac{B}{D}$

(c) $\frac{C}{A} \propto \frac{B}{D}$

(d) $\frac{C}{A} \propto \frac{D}{B}$

13. The marks secured by some students of a class are given below.

Marks	20	21	22	23	24	25
No of students	4	2	7	1	3	1

The harmonic mean is

(a) 20.13

(b) 16

(c) 18.75

(d) 21.9

14. The average weight of the following distribution is 58.5 kg

Weight in Kg	50	55	60	X+12.5	70	Total
Number of men	1	4	2	2	1	10

The value of x is

(a) 45

(b) 52

(c) 50

(d) 29

15. Cumulative frequency distribution of marks obtained by 22 students is

Marks below 10	3
Marks below 20	8
Marks below 30	17
Marks below 40	20
Marks below 50	22

The mode of the distribution is

(a) 24

(b) 22

(c) 21

(d) 20

16. If for a distribution mean =100 and s.d s = 10 then

(a) 95% of the observations will lie between 80 and 120

(b) 68% of the observations will lie between 85 and 115

(c) Practically all observation will lie between 60 and 140

(d) The estimated range of the distribution is 40

17. For a symmetrical bell shaped frequency distribution which one of the following is correct?

(a) 70% of the observations will lie within plus and minus 1 standard deviations

(b) 93% of the observations will lie within plus and minus 2 standard deviations

(c) 95% of the observations will lie within plus and minus 3 standard deviations

(d) Mean, median, Mode all are equal

18. The hourly wages for a sample of part-time employees at home depot are R2, R3, R6, R8 and R9. Sample variance is

(a) 5.6

(b) 6

(c) 8

(d) 9.3

19. In a sample containing 10 data the arithmetic mean of the squared deviations of individual items from mean is called

    (a) Variance

    (b) Standard deviation

    (c) Mean deviation

    (d) Kurtosis

20. Refer the following distribution:

Class Interval	0 - 500	500 - 1000	1000 - 1500	1500 - 2000	2000 - 3000
Frequency	90	218	86	41	15

    The standard deviation of the distribution is

    (a) 134.287

    (b) 615.871

    (c) 872

    (d) 519.564

21. To ascertain the size of shoes sold out in largest number from a shop the average employed will be

    (a) Median

    (b) Mode

    (c) Average Mean

    (d) Harmonic Mean

22. The arithmetic mean hourly output in two manufacturing plant A and B is 50. Then which one of the following statement is correct?

    (a) Based on the two equal means we could conclude that the distributions of the hourly outputs are identical in two plants

    (b) Based on the two equal means only we cannot conclude on pattern of distributions of hourly outputs unless computing respective medians

    (c) Based on the two equal means only we cannot conclude on pattern of distributions of hourly outputs unless computing respective variances

    (d) Based on the two equal means only we could conclude that the distributions of hourly outputs have two equal mode

23. The analysis of the results of a budget survey of 150 families gave an average monthly expenditure of ₹120 on food items with a standard deviation of ₹15. After the analysis was completed it was noted that figure recorded for one household was wrongly taken as ₹15 instead of ₹105. The correct value of the average expenditure is

    (a) ₹90.54

    (b) ₹150

    (c) ₹130.8

    (d) ₹120.6

24. Which of the following central tendency is most appropriate when total time taken is fixed but the speeds to be averaged is varying

    (a) Harmonic Mean

    (b) Arithmetic Mean

    (c) Geometric Mean

    (d) Weighted Mean

25. Standard deviation of two series of observations X and Y are respectively 7.51 and 10.47. Both the series have same mean. Which one of the following is correct?

    (a) Series X has more item compared to Series Y

    (b) Data in series X are more concentrated around mean as s.d. of X < s.d. of Y

    (c) Data in series Y are more concentrated around mean as s.d. of Y > s.d. of X

    (d) Series Y has more item compared to Series X

26. For a group containing 100 observations the arithmetic mean and standard deviations are 8 and . For 50 observations selected from these 100 observations the mean and the standard deviation are 10 and 2 respectively. The standard deviation of the other half is

(a) 8.2

(b) 3

(c) 4

(d) 5.5

27. When it is desired that the sum of deviations from the mean should be least, which of the following central tendency measure is appropriate

(a) Mean

(b) Mode

(c) Median

(d) Weighted Average

28. If two variables x and y are related by 2x+3y–7=0 and the mean and Mean deviation about mean of x are 1 and 0.3 respectively, then the coefficient of mean deviation of y about mean is

(a) -5

(b) 12

(c) 50

(d) 4

29. Coefficient of Standard deviation is equal to

(a) Standard deviation / AM

(b) AM/ Standard deviation

(c) Standard deviation / GM

(d) None

30. Quartiles can be determined graphically using

(a) Histogram

(b) Frequency polygon

(c) Ogive

(d) Pie chart

Answer:

1	a	
2	c	
3	a	
4	b	$\frac{1+x+x^2}{1-x+x^2}=\frac{62(1+x)}{63(1-x)}$ or, $\frac{(1+x+x^2)(1-x)}{(1-x+x^2)(1+x)}=\frac{62}{63}$ or, $\frac{1-x^3}{1+x^3}=\frac{62}{63}$ Do componendo dividendo & hence the result
5	a	
6	d	
7	b	$\frac{(4)^2}{(9)^2}=\frac{x-9}{3x+6}$ & hence the answer
8	c	
9	b	
10	c	
11	c	
12	b	
13	d	
14	c	
15	a	
16	a	95% of observation will lie plus minus 2 s.d. i.e. between 100 - 2*10 to 100*2.10 i.e. from 80 to 120
17	d	
18	d	Variance of a sample = $\frac{\sum(x-\bar{x})^2}{n-1}$
19	a	
20	d	
21	b	
22	c	
23	d	
24	a	
25	b	
26	b	
27	c	
28	b	
29	a	
30	c	

Suggestions:

The study guide are to be studied thoroughly. Supplementary readings could be made from other resources. In this issue MCQs are based on basic concepts taught in the respective modules/sub modules of the study guide. Students should try to solve individual questions with expertise developed after studying guide book to understand the correct answer of each question. Formula used here are all covered in study guide.

Best Wishes.

Topic

Fundamentals of Business Economics -

Module 1 : Basic Concepts

Module 2 : Forms of Market

Module 3 : Money and Banking

Fundamentals of Management -

Module 5: Fundamentals of Management

FOUNDATION

Paper-4

Fundamentals of Business Economics and Management (FBEM)

FUNDAMENTALS OF BUSINESS ECONOMICS AND MANAGEMENT

Let us start our usual mock test.

I. Choose the correct answer:

1. Who was the proponent of the scarcity definition of economics?
   A. Samuelson
   B. Robbins
   C. Pigou
   D. Marshall
2. Who invented "Multiplier theory"?
   A. Schumpeter
   B. Samuelson
   C. Keynes
   D. None of the above
3. If the level of expenditure on a commodity remains the same, even if the price of it falls, the price elasticity of demand will be
   A. Greater than unity
   B. Less than unity
   C. Equal to unity
   D. None of the above
4. A point to the left of the mid point of a linear demand curve will have price elasticity of demand which is
   A. Relatively elastic
   B. Relatively inelastic
   C. Unit elastic
   D. None of the above
5. Demand for durable goods usually remains
   A. Relatively elastic
   B. Relatively inelastic
   C. Unitary elastic
   D. None of the above
6. The price elasticity of demand for salt is
   A. Elastic
   B. Perfectly elastic
   C. Inelastic
   D. None of the above
7. When price elasticity of demand is infinity, then MR will be
   A. Greater than price
   B. Equal to price
   C. Less than price
   D. None of the above
8. Law of increasing returns to scale is a
   A. Long run phenomenon
   B. Medium run phenomenon
   C. Short run phenomenon
   D. None of the above
9. As output rises, AFC
   A. Also rises
   B. First falls then rises
   C. Falls but it cannot be zero
   D. None of the above
10. When AVC is rising then
    A. SMC > AVC
    B. SMC < AVC
    C. SMC = AVC
    D. None of the above
11. When AVC curve is rising
    A. SMC curve will also be rising
    B. SMC curve will be falling
    C. SMC curve will be parallel to x-axis
    D. Nothing can be predicted
12. Profit will be maximum when
    A. AR = MR
    B. MR curve cuts the AR curve from below
    C. Both A and B
    D. None of the above
13. Internal economies of scale occurs when
    A. LAC curve sloping downward
    B. SAC curve sloping downward
    C. LAC curve sloping upward
    D. SAC curve sloping upward

14. External economies of scale occurs when
    A. LAC curve shifts downward
    B. SAC curve shifts downward
    C. LAC curve shifts upward
    D. SAC curve shifts upward
15. The principal goal of a monopoly firm is assumed to be
    A. Sales maximization
    B. Revenue maximization
    C. Profit maximization
    D. None of the above
16. Product differentiation is the other name of
    A. Monopoly
    B. Discriminating monopoly
    C. Monopolistic competition
    D. None of the above
17. Kinked demand curve is related to
    A. Oligopoly
    B. Monopoly
    C. Monopolistic competition
    D. None of the above
18. Under perfect competition, a firm faces a demand curve which is
    A. Downward sloping
    B. Parallel to the x- axis
    C. Upward rising
    D. None of the above
19. What is the name of the central bank of England?
    A. Central bank of England
    B. Bank of London
    C. Bank of England
    D. None of the above
20. Inflation can be controlled if
    A. Bank rate is increased
    B. Govt. bond is sold in the open market
    C. CRR is increased
    D. All the three above
21. The narrow money in an economy is denoted by
    A. M4
    B. M3
    C. M1
    D. None of the above
22. The final step in decision making process is
    A. Selection of an alternative
    B. Developing alternative
    C. Evaluation of alternative
    D. Implementation and follow up of decision
23. Free-rein Leadership is also known as
    A. Laissez Faire leadership
    B. Participative leadership
    C. Authoritarian leadership
    D. None of the above
24. Selection is a process of rejection hence it is a
    A. Positive process
    B. Negative process
    C. either A or B
    D. none of the above
25. T-group training is also called
    A. Class room training
    B. Apprenticeship training
    C. Internship training
    D. Sensitivity training
26. Introduction of a person to a job is called
    A. Induction
    B. Placement
    C. Orientation
    D. None of the above
27. Vestibule training is considered as a part of
    A. Off-the-job training
    B. On-the-job training
    C. Both A and B
    D. None of the above

28. Who takes the initiative in formulating major objectives, strategies, policies

A. Middle management

B. Top management

C. Lower management

D. All of the above

29. Which of the following are called standing plans?

A. Policies

B. Procedures

C. Rules

D. All of the above

30. Carrot and stick approach to motivation is adopted under which system?

A. Exploitative Autocratic

B. Benevolent Autocratic

C. Consultative

D. Democratic

Answer:

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
B	C	C	A	B	C	B	A	C	A	D	C	A	A	C
16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
C	A	B	C	D	C	D	A	B	D	A	A	B	D	B

So friends,

I asked you to go through the "straight line" chapter of co-ordinate geometry. I hope all of you have followed my instruction. So this mock test will be a cake-walk for you. Please maintain a record of your performance in all the mock tests. That will indicate your progress in this paper. Of course you should not consult the KEY before you finish off solving the test paper.

Wish you all the best!!!

CMA INTERMEDIATE COURSE

Syllabus 2022

Topic

Module 5: Indian Partnership Act, 1932

INTERMEDIATE

Group I - Paper-5

Business Laws and Ethics (BLE)

Dissolution of Firms under the Indian Partnership Act, 1932

Introduction

Partnership represents one of the oldest and most widely adopted forms of business organization in India. Small and medium enterprises often prefer this structure due to its simplicity, flexibility, and ease of formation. The relationship among partners is based on mutual trust, confidence, and the principle of uberrimae fidei (utmost good faith). Nevertheless, business relationships may not persist indefinitely. Changes in business objectives, financial difficulties, retirement or death of partners, or disputes among partners may render continuation of the partnership impossible or undesirable. In such situations, the law provides a structured mechanism for terminating the partnership.

The Indian Partnership Act, 1932, comprehensively governs the dissolution of firms through Sections 39 to 55. These provisions specify the circumstances under which a firm may be dissolved, the rights and obligations of partners after dissolution, and the manner in which the firm's assets and liabilities should be settled. The Act seeks to protect not only the interests of partners but also those of creditors and third parties who have dealt with the firm.

Dissolution constitutes a critical stage in the life cycle of a partnership, as it determines the discharge of business obligations and the distribution of remaining assets. Judicial decisions have further clarified statutory provisions, thereby promoting fairness and legal certainty in the dissolution process.

Meaning of Dissolution of a Firm

Section 39 of the Indian Partnership Act defines dissolution of a firm as the dissolution of the partnership between all partners of the firm. Dissolution signifies the complete termination of the legal relationship among all partners and brings the business of the firm to an end. After dissolution, the firm ceases to exist except for activities necessary to wind up its affairs.

Distinguishing between dissolution of partnership and dissolution of firm is essential. Dissolution of partnership refers to a change in the relationship among partners resulting from the admission, retirement, death, or insolvency of a partner. In these instances, the business may continue with the remaining or newly admitted partners, leading to reconstitution of the firm. Conversely, dissolution of the firm results in complete closure of the business and termination of the partnership among all partners.

This distinction is significant, as every dissolution of a firm involves dissolution of partnership, whereas not every dissolution of partnership necessarily results in dissolution of the firm.

Modes of Dissolution of a Firm

The Indian Partnership Act recognizes several modes by which a firm may be dissolved, depending on the circumstances.

Dissolution by Agreement (Section 40)

The simplest method of dissolution occurs through mutual agreement among all parties. As a partnership formed by agreement, the partners may unanimously decide to terminate the business whenever they deem appropriate.

Dissolution by agreement commonly occurs when:

- the business objectives have been achieved;
- partners wish to pursue separate ventures;
- persistent disagreements affect business operations; or
- the firm is no longer commercially viable.

A written dissolution agreement is generally prepared, specifying the date of dissolution, the settlement of liabilities, the realization of assets, and the distribution of remaining property. Although the Act does not mandate registering the dissolution agreement, documenting its terms serves to minimize future disputes.

Compulsory Dissolution (Section 41)

Certain circumstances result in compulsory dissolution by operation of law.

A firm is compulsorily dissolved if:

- all partners or all except one become insolvent; or
- the business of the firm becomes unlawful due to changes in law.

For example, if legislation prohibits a particular business activity conducted by the firm, continuation of the partnership becomes illegal, thereby necessitating dissolution.

Compulsory dissolution reflects the principle that a partnership cannot continue if its business becomes unlawful or if there are insufficient legally competent partners to conduct it.

Dissolution on the Happening of Certain Contingencies (Section 42)

Unless otherwise agreed by the partners, a firm may dissolve upon the occurrence of specified events, including:

- expiry of the fixed duration for which the partnership was constituted;
- completion of a specific venture or undertaking;

- death of a partner; or
- insolvency of a partner.

For instance, if a partnership is established specifically to construct a residential complex, the firm automatically dissolves upon completion of the project unless the partners agree to continue the business.

Many modern partnership deeds expressly provide that the firm shall continue despite the death or retirement of a partner, thereby avoiding automatic dissolution.

Dissolution by Notice (Section 43)

Where the partnership is at will, any partner may dissolve the firm by giving written notice to the other partners of the intention to dissolve. The dissolution becomes effective from:

- the date mentioned in the notice; or
- if no date is specified, the date on which the notice is communicated.

This provision recognizes the voluntary nature of partnerships at will and prevents partners from being compelled to remain in a business relationship against their will.

Dissolution by the Court (Section 44)

The Act empowers the court to dissolve a firm in circumstances where continuation of the partnership becomes impracticable or inequitable. The court may order dissolution on grounds such as:

- insanity of a partner;
- permanent incapacity affecting business performance;
- misconduct likely to prejudice the firm's business;
- persistent breach of the partnership agreement;
- transfer of a partner's entire interest;
- continuous business losses; or
- any other circumstance making it just and equitable to dissolve the firm.

The "just and equitable" ground provides courts with considerable flexibility to grant relief when mutual trust has irretrievably broken down.

Judicial Perspectives

Case Study: Blisset v. Daniel (1853)

Case Background

A majority of partners attempted to expel another partner from the firm without exercising their powers in good faith.

Court Decision

The court held that powers granted under the partnership agreement must be exercised bona fide and for the benefit of the partnership rather than for personal advantage.

Significance

Although the case primarily concerned expulsion, it established the broader principle that partnership powers, including decisions leading to dissolution, must be exercised in good faith.

Case Study: Garner v. Murray (1904)

Case Background

After the dissolution of the partnership, one partner became insolvent before contributing his share of the firm's losses. The remaining partners subsequently disputed the allocation of the resulting deficiency.

Court Decision

The court determined that, unless otherwise stipulated, the deficiency resulting from the insolvent partner must be borne by the solvent partners in proportion to their last agreed capital balances.

Significance

This landmark decision established a significant rule for the settlement of accounts following dissolution. Although originating from English law, it has been widely cited in discussions of equitable settlement of partnership accounts.

Settlement of Accounts (Section 48)

Section 48 outlines a systematized procedure for the fair distribution of assets. The sequence prescribed by the Act is:

Losses, including capital deficiencies, are first paid out of profits, then out of capital, and finally by partners individually according to their profit-sharing ratio.

The firm's assets, including additional contributions made by partners, are applied in the following order:

- payment of external debts;
- repayment of advances made by partners distinct from capital;
- return of partners' capital contributions;
- distribution of any remaining surplus among partners according to the agreed profit-sharing ratio.

This statutory order protects and safeguards the interests of creditors and ensures the protection of partners.

Rights and Liabilities after Dissolution

Dissolution does not result in the immediate termination of all rights and liabilities.

Partners retain the authority to perform acts necessary for winding up the firm's affairs and completing unfinished transactions. This authority persists until the business is fully wound up.

Partners also remain liable to third parties for acts conducted prior to public notice of dissolution unless proper notice is provided. Therefore, issuing public notice holds considerable legal significance.

Each partner retains the right to demand proper realization of assets and equitable settlement of accounts. Partners are also entitled to have partnership property applied exclusively to the payment of partnership liabilities before any distribution among themselves.

Goodwill on Dissolution

Goodwill encompasses the firm's reputation and accumulated customer loyalty. It is recognized as a partnership asset and may be sold upon dissolution.

Unless otherwise agreed, the purchaser of goodwill acquires the right to represent themselves as continuing the former business and may use the firm's name. Partners may, however, agree to reasonable restrictions to prevent former partners from competing in ways that diminish the value of the goodwill sold.

The treatment of goodwill during dissolution underscores its increasing commercial significance, especially within professional firms and service-based enterprises.

Practical Importance of Dissolution Provisions

The statutory provisions governing dissolution promote certainty and fairness in commercial relationships. These provisions reduce prolonged disputes among partners by prescribing clear procedures for termination, settlement of liabilities, and distribution of assets.

In the contemporary business environment, partnerships frequently operate in sectors such as professional services, consultancy, retail trade, and family businesses. Effective dissolution provisions help preserve commercial confidence by ensuring that creditors are paid, partners receive their legitimate shares, and business obligations are discharged in an orderly manner.

Furthermore, comprehensive partnership agreements include provisions on dissolution, asset valuation, dispute resolution, and continuation clauses, thereby significantly reducing litigation and facilitating smoother business exits.

Conclusion

The provisions of the Indian Partnership Act, 1932, concerning dissolution, establish a comprehensive legal framework for terminating partnerships in an orderly and equitable manner. By recognizing multiple modes of dissolution, prescribing a clear mechanism for settlement of accounts, and safeguarding the interests of partners and creditors, the Act ensures that the termination of a partnership does not result in unnecessary legal uncertainty.

Judicial decisions such as Garner v. Murray and Blisset v. Daniel have further reinforced these statutory principles by emphasizing fairness, good faith, and equitable distribution of liabilities. In an increasingly dynamic business environment, the law governing dissolution continues to play a crucial role in facilitating responsible business exits and maintaining confidence in commercial transactions.

Dissolution and Winding-up of Limited Liability Partnerships under the Limited Liability Partnership Act, 2008

Introduction

The enactment of the Limited Liability Partnership (LLP) Act, 2008, represented a pivotal development in Indian business law. Before this legislation, entrepreneurs were limited to traditional partnership firms, which imposed unlimited personal liability, or companies, which entailed complex regulatory and compliance obligations. The Government of India addressed the need for a flexible, legally secure business structure by introducing the LLP model, which combines the operational flexibility of partnerships with the limited liability benefits of companies.

Although an LLP is designed to have perpetual succession, situations such as financial distress, failure to fulfill business objectives, partner disputes, or regulatory non-compliance may require its closure. The Limited Liability Partnership Act, 2008, along with the Limited Liability Partnership (Winding up and Dissolution) Rules, 2012, establishes a comprehensive legal framework to govern the dissolution and winding-up of LLPs, thereby ensuring an orderly business exit.

The dissolution provisions are designed to safeguard the interests of partners, creditors, employees, regulators, and other stakeholders, while ensuring that the LLP terminates its operations transparently and in compliance with legal requirements.

Meaning of Dissolution and Winding-up

Although the terms 'winding-up' and 'dissolution' are frequently used interchangeably, they denote distinct legal stages in the process of closing an LLP.

Winding-up is the legal process by which the affairs of an LLP are brought to an end. During this stage, the assets of the LLP are realized, liabilities are discharged, pending claims are settled, and any surplus is distributed among the partners in accordance with the LLP Agreement or applicable legal provisions.

Dissolution, on the other hand, is the final legal event that terminates the existence of the LLP. Once dissolved, the LLP ceases to exist as a separate legal entity and cannot carry on any business activities.

Therefore, winding up constitutes the procedural phase, while dissolution is the legal outcome following the completion of that process.

Legal Framework Governing Dissolution

The provisions relating to dissolution are primarily contained in Chapter XIII of the Limited Liability Partnership Act, 2008, read together with the Limited Liability Partnership (Winding up and Dissolution) Rules, 2012.

The legal framework aims to:

- ensure equitable settlement of liabilities;
- protect the interests of creditors;
- prevent fraudulent closure of business;
- provide certainty regarding distribution of assets; and
- facilitate an orderly exit from commercial activities.

In contrast to traditional partnership firms, LLPs have a distinct legal identity, which makes the winding-up process more structured and more akin to the procedures applicable to companies.

Modes of Dissolution of an LLP

An LLP may be dissolved through various legal mechanisms, contingent upon its financial condition and operational status.

Voluntary Winding-up

Voluntary winding-up is a prevalent method of closure, wherein the partners collectively resolve to discontinue the LLP's business operations.

Such a decision may arise due to:

- completion of business objectives;
- prolonged inactivity;
- retirement of key partners;
- commercial unviability; or
- strategic restructuring.

Prior to commencing voluntary winding-up, partners are generally required to pass a resolution in accordance with the LLP Agreement. The LLP must also ensure that all liabilities are either discharged or that suitable arrangements for their settlement have been established.

This approach allows partners to conclude business operations efficiently and avoid protracted litigation.

Winding-up by the Tribunal

The National Company Law Tribunal (NCLT) may order the winding-up of an LLP under circumstances prescribed by law. The Tribunal may intervene when the continuation of the LLP contravenes legal or public interests. Judicial oversight ensures fairness, especially in cases where creditors or stakeholders could be adversely affected.

Grounds for Winding-up by the Tribunal

The Tribunal may order winding-up under several circumstances, including:

- where the LLP resolves that it should be wound up by the Tribunal;
- where the LLP has acted against the sovereignty and integrity of India, the security of the State, or public order;
- where the LLP has failed to file its Statement of Account and Solvency or Annual Returns for the prescribed period;
- where the number of partners falls below the statutory minimum for more than six months; or
- where the Tribunal considers that it is just and equitable to wind up the LLP.

The 'just and equitable' ground grants the Tribunal discretion in cases where the continuation of the LLP is impracticable, such as in instances of deadlock, loss of mutual confidence, or other exceptional circumstances.

Role of the Liquidator

Once winding-up commences, a Liquidator may be appointed to administer the process. The Liquidator performs several important functions, including:

- taking custody of the LLP's assets;
- preparing an inventory of properties;
- realizing assets;
- settling liabilities;
- verifying creditors' claims;
- maintaining proper accounts; and
- distributing any remaining surplus among partners.

The Liquidator serves as an impartial officer tasked with ensuring compliance with statutory requirements and safeguarding the interests of all stakeholders throughout the winding-up process.

Settlement of Assets and Liabilities

One of the primary objectives of winding up is the equitable settlement of financial obligations.

The realization of assets follows a systematic approach. Assets of the LLP are sold, and the proceeds are utilized for:

- payment of costs and expenses of winding-up;
- discharge of debts owed to creditors;
- payment of statutory liabilities;
- repayment of loans advanced by partners, where applicable; and
- distribution of any remaining surplus among partners according to the LLP Agreement.

This structured approach reduces the likelihood of disputes and ensures that creditors are prioritized before partners receive any residual assets.

Rights and Liabilities of Partners during Winding-up

Although partners in an LLP enjoy limited liability during the ordinary course of business, certain responsibilities continue during winding-up. Partners are expected to cooperate with the Liquidator by providing books of account, financial records, statutory documents, and any other information necessary to complete the winding-up process.

Where partners have acted honestly and within the scope of the LLP Agreement, their liability ordinarily remains limited to their agreed contribution. However, limited liability does not extend to acts involving fraud, deliberate misconduct, or wrongful concealment of assets.

Fraudulent Conduct and Personal Liability

One key feature of the LLP Act is that limited liability is not absolute. Where business has been carried on with intent to defraud creditors or for any fraudulent purpose, the persons responsible may become personally liable without limitation.

Practical Illustration

Suppose the designated partners of an LLP deliberately obtain loans by submitting manipulated financial statements while secretly transferring business assets to another entity. When creditors initiate recovery proceedings, the investigation reveals fraudulent conduct.

In such circumstances, the Tribunal may impose unlimited personal liability upon the partners responsible for the fraud, despite the LLP ordinarily providing limited liability.

This provision serves to deter. The LLP structure fosters corporate governance.

Striking Off and Dissolution

Apart from winding up, the Registrar may remove the name of an LLP from the register where it has ceased carrying on business and satisfies the prescribed legal requirements.

Striking off is typically applicable to LLPs that are inactive and free of outstanding liabilities. It provides a relatively straightforward method for closing dormant entities. However, where liabilities exist or disputes remain unresolved, winding up remains the appropriate legal mechanism. Therefore, striking off and winding up fulfill distinct legal functions, although both processes ultimately result in the dissolution of the LLP.

Judicial Perspective

Case Study: Registrar of Companies v. Independent Infrastructure LLP

Case Background

An LLP persistently failed to file statutory returns and financial statements for several consecutive years. Despite repeated notices from the Registrar, the LLP neither complied with the filing requirements nor regularized its statutory defaults.

Tribunal's Decision

The Tribunal observed that continuous non-compliance with mandatory statutory obligations defeated the objective of maintaining transparency and accountability in business organizations. Appropriate action was directed under the provisions governing winding-up and regulatory compliance.

Significance

The case illustrates that statutory compliance is an essential responsibility of LLPs. Limited liability does not exempt business organizations from complying with legal filing requirements, and persistent default may ultimately lead to regulatory action, including winding up.

Importance of Dissolution Provisions in Modern Business

The legal framework for dissolution is instrumental in fostering confidence among investors, creditors, and business partners.

An orderly winding-up process ensures that business failures do not generate undue uncertainty or compromise stakeholder rights. Additionally, it encourages entrepreneurship by assuring business owners that LLP closures are governed by transparent legal procedures.

Within India's rapidly growing start-up ecosystem, numerous enterprises select the LLP structure for its combination of managerial flexibility and limited liability. Equally significant is the presence of a well-defined exit mechanism for situations in which business objectives are met or commercial conditions change.

Moreover, the focus on accountability, statutory compliance, and safeguards against fraudulent conduct enhances corporate governance and bolsters the credibility of LLPs as a preferred business structure.

Conclusion

The provisions regulating the dissolution and winding-up of Limited Liability Partnerships under the LLP Act, 2008, establish a comprehensive legal framework for the orderly closure of business entities. By differentiating between winding-up and dissolution, outlining clear procedures for liability settlement, protecting creditors, and enforcing accountability for fraudulent conduct, the Act achieves a balance between entrepreneurial flexibility and legal responsibility.

The LLP structure has emerged as one of the most preferred business models for professionals, start-ups, and small enterprises because it combines operational freedom with limited liability. Equally significant is the statutory mechanism for winding up, which ensures that business closures are conducted transparently, fairly, and in accordance with law. As India's business environment continues to evolve, the legal provisions governing dissolution will remain essential for promoting responsible business practices, safeguarding stakeholder interests, and strengthening confidence in the LLP form of organization.

Topic

Module 1:
Accounting
Fundamentals

INTERMEDIATE

Group I - Paper-6

Financial Accounting
(FA)

Capital and Revenue Transactions, Adjustment Entries and Rectification of Errors

Capital and Revenue Transactions

Capital and Revenue Transactions are two fundamental concepts in accounting that distinguish between different types of expenditures and receipts. They help in understanding how different financial activities impact a company's financial statements.

Capital Transactions

Capital Expenditure: These are expenses incurred to acquire or improve fixed assets (e.g., purchasing machinery, buildings, vehicles). Such expenses provide benefits over a long period and are capitalized, i.e., added to the cost of the asset on the balance sheet.

Examples:

- Purchase of land, building, or machinery.
- Installation costs for new equipment.
- Legal fees for purchasing property.

Capital Receipts: These are funds received that either reduce liabilities or increase the owner's equity without impacting the company's profit or loss. They are not generated from the day-to-day business activities.

Examples:

- Sale of fixed assets.
- Issue of shares or debentures.
- Loans received from banks or financial institutions.

Revenue Transactions

Revenue Expenditure: These are the costs incurred in the ordinary course of business to maintain daily operations. These expenses provide benefits for a short term, typically within a single financial year, and are charged to the profit and loss account.

Examples:

- Wages and salaries.
- Rent, utilities, and insurance.
- Repairs and maintenance.

Revenue Receipts: These are incomes generated from the core business activities, typically recurring in nature. They contribute directly to the profit of the business.

Examples:

- Sales revenue from goods and services.
- Interest received on investments.
- Commission received.

Differences between capital expenditure and revenue expenditure

Criteria	Capital Expenditure	Revenue Expenditure
Nature	Incurred to acquire or improve long-term assets.	Incurred for day-to-day operations.
Purpose	Aimed at increasing earning capacity or extending asset life.	Aimed at maintaining earning capacity and daily functions.
Treatment in Financial Statements	Capitalized and shown as an asset on the balance sheet.	Expensed in the income statement (profit and loss account).
Recurrence	Typically non-recurring, it involves large sums.	Recurring involves regular and smaller amounts.
Impact on Financial Statements	Affects both the balance sheet and the income statement through depreciation.	Directly impacts the income statement by reducing profit.
Examples	Purchase of machinery, construction of a building.	Payment of wages, rent, repairs, and utilities.
Long-Term vs. Short-Term Impact	Provides long-term benefits, often over several years.	Provides short-term benefits within the current year.
Depreciation	Subject to depreciation over the useful life of the asset.	Not subject to depreciation; fully expensed in the current year.
Impact on Profitability	Initially reduces cash flow but spreads the cost over time.	Directly reduces profits in the year incurred.
Example Scenarios	Buying a new factory, installing new equipment.	Routine maintenance, office supplies, utility bills.

Differences between capital receipts and revenue receipts

Criteria	Capital Receipts	Revenue Receipts
Nature	Non-recurring receipts that affect liabilities or equity.	Recurring receipts from normal business operations.
Source	Derived from non-operational activities like financing.	Generated from operational activities like sales.
Impact on Financial Statements	Recorded on the balance sheet.	Recorded on the income statement (profit and loss account).
Recurrence	Typically non-recurring.	Regular and recurring.
Impact on Capital Structure	Affects capital structure (increases equity or liabilities).	No impact on capital structure.
Examples	Sale of fixed assets, issue of shares, and loans received.	Sales revenue, interest earned, commission received.
Long-Term vs. Short-Term Impact	Long-term impact, linked to investment/ financing activities.	Short-term impact, related to the current period's earnings.
Repayment or Obligation	May involve future obligations (e.g., loan repayment).	No repayment obligation.
Tax Treatment	May not be taxable, subject to specific rules.	Fully taxable as business income.
Example Scenarios	Selling land, borrowing from a bank, issuing shares.	Income from sales, interest on deposits, and rent received.

Adjustment Entries and Rectification of Errors

Adjustment Entries

Adjustment entries are made at the end of an accounting period to update the accounts before financial statements are prepared. They ensure that revenues and expenses are recorded in the period they occur, regardless of when the cash is received or paid.

Key Types of Adjustment Entries:

1. **Accrued Revenues:** Revenue earned but not yet received or recorded.
   - Example: Interest receivable.
2. **Accrued Expenses:** Expenses incurred but not yet paid or recorded.
   - Example: Salaries payable.
3. **Prepaid Expenses:** Payments made in advance for expenses that have not yet been incurred.
   - Example: Prepaid rent.
4. **Unearned Revenues:** Cash received before revenue is earned.
   - Example: Advance payments from customers.
5. **Depreciation:** Allocation of the cost of a tangible fixed asset over its useful life.
   - Example: Depreciation on machinery.

Rectification of Errors

Rectification of errors involves correcting mistakes in financial records. Errors can occur due to omission, incorrect recording, or misclassification of transactions.

Types of Errors:

1. **Errors of Omission:** A transaction is completely omitted from the books.
   - **Example:** Forgetting to record a purchase.
   - **Rectification:** Record the omitted entry in the relevant accounts.
2. **Errors of Commission:** A transaction is recorded but with the wrong amount or in the wrong account.
   - **Example:** Recording Rs.500 as Rs.50.
   - **Rectification:** Correct the amount or the account in which the entry was made.
3. **Errors of Principle:** A transaction is recorded in violation of accounting principles.
   - **Example:** Treating revenue expenditure as capital expenditure.
   - **Rectification:** Reverse the incorrect entry and record it correctly.
4. **Compensating Errors:** Two or more errors that cancel each other out.
   - **Example:** Understating income by Rs.200 and overstating expenses by Rs.200.
   - **Rectification:** Identify and correct each error separately.

5. **Errors of Duplication:** Recording the same transaction more than once.
   - **Example:** Entering a purchase invoice twice.
   - **Rectification:** Reverse the duplicated entry.

Methods of Rectification:

1. **Before Preparation of Trial Balance:** Correct the error directly in the ledger accounts.
2. **After Preparation of Trial Balance:** Use a Suspense Account to temporarily hold discrepancies until they are resolved.

Importance of Adjustment Entries

Adjustment entries are crucial for accurate financial reporting and ensuring compliance with accounting principles. Here's why they are important:

1. **Accurate Financial Statements:** Adjustment entries ensure that revenues and expenses are recognized in the correct accounting period, providing a true and fair view of the financial position.
2. **Compliance with Accounting Standards:** These entries are necessary to adhere to the Matching Principle (matching revenues with related expenses) and the Accrual Principle (recording transactions when they occur, not when cash is received or paid).
3. **Reflect True Profit or Loss:** Adjustments for accrued expenses, prepaid expenses, depreciation, and provisions help calculate the actual profit or loss for the accounting period.
4. **Preparation for Audit:** Adjustment entries help ensure that the books of accounts are accurate, reducing discrepancies during audits.
5. **Improved Decision-Making:** Adjusted financial statements provide stakeholders with accurate data for making informed decisions.
6. **Legal and Tax Compliance:** Proper adjustments ensure that income and expenses are reported accurately, aiding in compliance with tax laws and regulations.

Importance of Rectification of Errors

Rectification of errors is vital to maintain the integrity and reliability of financial records. Here's its importance:

1. **Correct Representation of Financial Data:** Rectifying errors ensures that the financial statements reflect the true financial position of the business.
2. **Maintaining Trustworthiness:** Accurate books of accounts enhance the credibility of the business among stakeholders, investors, and regulatory authorities.
3. **Facilitating Audit Process:** Errors in financial records can complicate audits. Rectification ensures smooth audits by presenting accurate data.
4. **Compliance with Laws and Standards:** Correcting errors helps in adhering to accounting standards and legal requirements, avoiding penalties or legal complications.
5. **Avoidance of Misinterpretation:** Financial errors can mislead management and stakeholders, resulting in poor decisions. Rectification prevents such issues.
6. **Reduction of Financial Risks:** Errors, if uncorrected, can escalate over time, causing larger discrepancies. Rectification mitigates such risks.
7. **Smooth Preparation of Future Accounts:** Correcting errors in the current period ensures that opening balances for the next period are accurate.
8. **Transparency and Accountability:** Identifying and rectifying errors fosters transparency and accountability in accounting practices.

Questions:

1. Which of the following is a capital expenditure?
   A) Payment of salaries
   B) Purchase of machinery
   C) Repair of machinery
   D) Rent for the office building
2. Which of the following is considered a revenue receipt?
   A) Loan from a bank
   B) Sale of old furniture
   C) Revenue from sales
   D) Issue of shares
3. Which of the following would be recorded as a capital receipt?
   A) Cash sales
   B) Loan from a bank
   C) Rent received
   D) Interest received on investments
4. Revenue expenditure is typically incurred for which of the following?
   A) Acquiring new machinery
   B) Day-to-day operations
   C) Purchasing land
   D) Constructing a new building

5. Which of the following is NOT a characteristic of capital expenditure?
   A) Long-term benefit
   B) Non-recurring in nature
   C) Expensed in the profit and loss account
   D) Increases the earning capacity of the business
6. Which of the following is an example of an accrued expense?
   A) Prepaid Rent
   B) Unearned Revenue
   C) Salaries Payable
   D) Depreciation Expense
7. If a transaction is completely omitted from the books, it is an error of:
   A) Commission
   B) Principle
   C) Omission
   D) Compensating
8. Which of the following errors will not affect the Trial Balance?
   A) Posting to the wrong account
   B) Omitting an entry in the ledger
   C) Entering a debit as a credit
   D) Adding up the ledger incorrectly
9. The process of distributing the cost of a tangible asset over its useful life is known as:
   A) Amortization
   B) Depreciation
   C) Accrual
   D) Prepayment
10. A customer paid in advance for services, but the services have not yet been provided. This should be recorded as:
   A) Revenue
   B) Expense
   C) Asset
   D) Liability

Answer:

1	2	3	4	5	6	7	8	9	10
B	C	B	B	C	C	C	A	B	D

Topic

Module 1: Basics of Income Tax Act

INTERMEDIATE

Group I - Paper-7A

Direct Taxation (DT)

Agricultural Income

While Section 10(1) of the Income Tax Act, 1961, broadly exempts agricultural income from taxation to support India's agrarian economy, applying this exemption requires careful scrutiny. The precise definition of 'agricultural income' under Section 2(1A) involves complex statutory rules, judicial precedents, and specific operational conditions that dictate its ultimate tax treatment.

Meaning

Agricultural income means -

a. Any rent or revenue derived from land, which is situated in India & is used for agricultural purposes;

b. Any income derived from such land by agricultural operations#;

c. Any income derived from such land by the cultivator by processing the agricultural produce raised or by the receiver of rent in kind by processing the agricultural produce received; so as to render it fit for sale in the market.

d. Any income derived from such land on sale made by the cultivator of the agricultural produce raised, or by the receiver of rent in kind of the agricultural produce received, without carrying on any process, other than the process required to render it fit for the market.

e. Any income derived from a building subject to the fulfilment of the following conditions

- The building should be occupied by the cultivator or receiver of rent in kind.
- The building should be on or in the immediate vicinity of the land, situated in India and used for agricultural purposes.
- The building should be used as a dwelling house, a storehouse, or another outbuilding.
- The land is either situated in a rural area or assessed for land revenue.

#Agricultural operation means:

- **Basic Operation:** It means application of human skill & labour upon the land, prior to germination. E.g., tilling of land, sowing of seeds, planting, irrigation, etc.
- **Subsequent Operation:** It means operations that foster the growth and preserve the produce, for rendering the produce fit for sale in the market, and which are performed after the produce sprouts from the land. E.g. pruning, cutting, harvesting, etc.

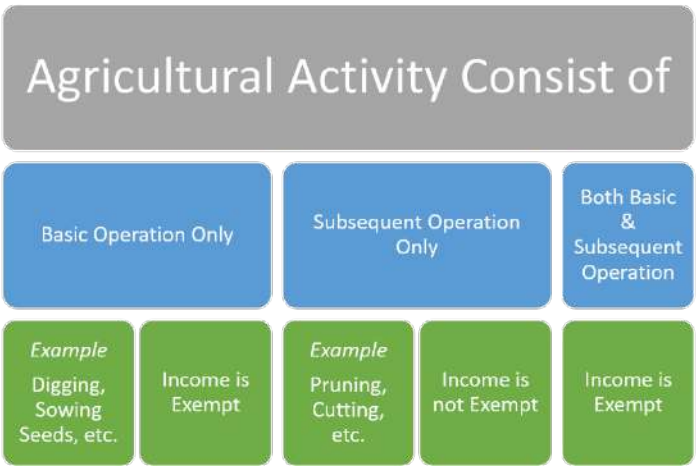
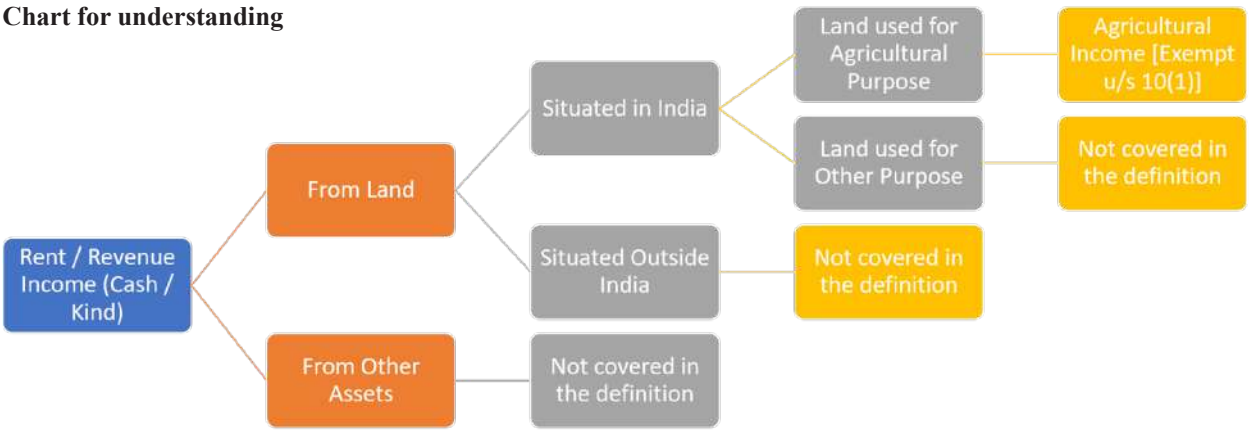


Chart for understanding



Treatment of Partly Agricultural & Partly Non-Agricultural Income

Nature of Business	Agricultural Income	Non-Agricultural Income
Growing & manufacturing tea	60%	40%
Growing & manufacturing rubber	65%	35%
Coffee grown and cured by the seller	75%	25%
Coffee is grown, cured, roasted and ground by the seller	60%	40%

Any Other Case: The assessee must prepare two statements of income (one for agro-business, one for non-agro-business). For computing agricultural income, the market value of the agricultural produce utilised as raw material is treated as revenue for the agro-business and as a deductible expenditure for the non-agro-business.

Impact of Agricultural Income on Tax Computation (Partial Integration)

Conditions:

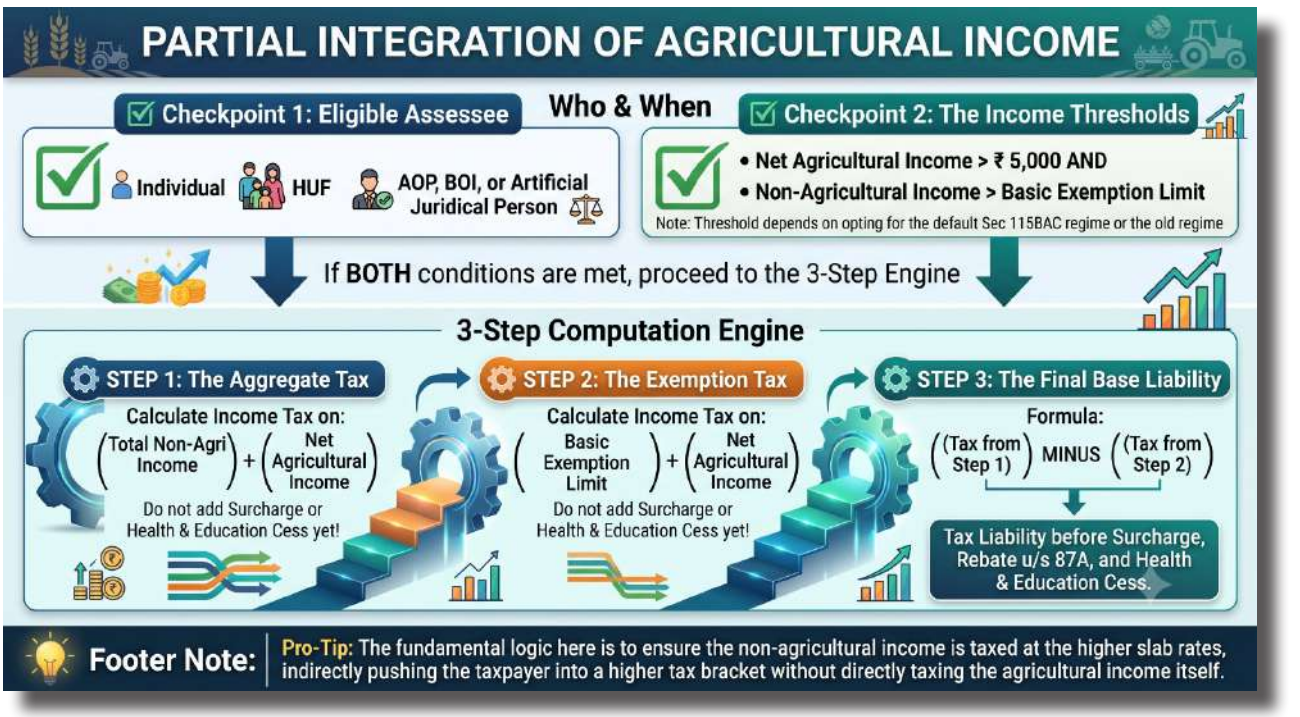
1. The assessee is an individual, HUF, a BOI, an AOP, or an artificial juridical person.
2. The assessee has non-agricultural income exceeding the basic exemption limit (as per the regime opted by the assessee)
3. The agricultural income of the assessee exceeds ₹ 5,000.

Treatment

Step 1: Compute income tax (before rebate, surcharge and cess) on the total income of the assessee, including agricultural income.

Step 2: Compute income tax on (Agricultural income + Basic Exemption Limit), before rebate, surcharge and cess

Step 3: Tax liability before rebate, surcharge and cess = (Tax as per Step 1) - (Tax as per Step 2)



➢ This method is not applicable in the case of a company and firm

State -vs.- Central Jurisdiction

In this context, it is worthwhile to note that the taxation of agricultural income falls under state jurisdiction due to the devolution of powers from the central government to states as per the Constitution. Each state has the authority to levy taxes on agricultural activities within its boundaries, although most states prefer to align with the central exemption to avoid administrative complexities and support the agricultural sector.

Choose the correct option.

1. Which of the following is an agricultural income?
   (a) Dividend paid by a company to its shareholders out of agricultural income
   (b) Share of Profit of a Partner from a firm engaged in an agricultural operation
   (c) Income from the supply of water by an assessee from a tank in agricultural land
   (d) Interest received by a money lender in the form of agricultural produce
2. Which of the following incomes received by an assessee are exempt under section 10 of the Income-tax Act, 1961?
   (a) Agricultural Income
   (b) Salary of a partner from a firm
   (c) Salary received by a member of a ship's crew
   (d) Cash gift of ₹ 5,00,000 received from a friend
3. In case of an individual or HUF, agricultural income is –
   (a) Exempted
   (b) Exempted but included in the total income for the rate purpose
   (c) Fully taxable, provided it is earned from India
   (d) Taxable at a flat rate of 10%
4. In case of an assessee engaged in the business of manufacturing of tea, his agricultural income is –
   (a) 60% of the total receipts of the business
   (b) 60% of income of the business
   (c) Nil
   (d) 40% of income of the business
5. Remuneration to a partner of a firm engaged in the business of growing and manufacturing rubber in India is –
   (a) Partly agricultural income and partly non-agricultural income
   (b) Agricultural income
   (c) Non-Agricultural income
   (d) Exempted income
6. Out of the following, which activity shall be considered as an agricultural activity?
   (a) Subsequent operation on the agricultural land
   (b) Basic operation on the agricultural land
   (c) Marketing operation of the agricultural produce
   (d) None of the above
7. Agricultural income is exempt u/s _____ of the Indian Income-tax Act, 1961.
   (a) 10(1)
   (b) 2(1A)
   (c) 10(2A)
   (d) 10A
8. Income from saplings shall be considered as _____ .
   (a) Agricultural Income
   (b) Business Income
   (c) Partly agricultural income and partly business income
   (d) Income from other sources
9. Which of the following is not an agricultural income?
   (a) Rent received from a land situated in India for agricultural purposes
   (b) Income derived from agricultural produce
   (c) Income derived from land being let out for the marriage of a farmer
   (d) Income from the production of tea leaves
10. Mr X is engaged in growing and manufacturing tea in India. His income from this activity is ₹ 1,40,000. His agricultural income will be –
   (a) ₹ 70,000
   (b) ₹ 84,000
   (c) ₹ 1,40,000
   (d) ₹ 56,000

Answer:

1	2	3	4	5	6	7	8	9	10
B	a	b	b	a	b	a	a	c	b

Topic

Module 5:
Goods and Services Tax (GST) Laws

INTERMEDIATE

Group I - Paper-7B

Indirect Taxation (IDT)

Time of Supply

The precise determination of the 'Time of Supply' serves as the ignition switch for GST liability. It is the chronological point where a transaction legally matures into a taxable event, dictating the crucial deadlines for discharging tax obligations and filing periodic returns. Given the bifurcated legislative treatment of goods and services under Sections 12 and 13 of the CGST Act, alongside highly nuanced provisions for reverse charge mechanisms and tax rate transitions, learning these statutory triggers is indispensable for both compliance accuracy and professional examination success.

Time of Supply of Goods – Forward Charge [Sec. 12(2)]

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

a. the date of issue of the invoice by the supplier; or

b. the last date on which he is required to issue the invoice with respect to the supply u/s 31; or

Taxpoint

A registered person supplying taxable goods shall issue a tax invoice, before or at the time of:

Where the supply involves the movement of goods	Removal of goods for supply to the recipient
Where the supply does not involve the movement of goods	Delivery of goods or making them available to the recipient

In a nutshell, in the case of the supply of goods, the time of supply is as follows:

Time of Supply of Goods in case of reverse charge [Sec. 12(3)]

In case of supplies in respect of which tax is paid or liable to be paid on a reverse charge basis, the time of supply shall be the earliest of the following dates:

a. the date of the receipt of goods; or

b. the date of payment as entered in the books of account of the recipient; or

c. the date on which the payment is debited in his bank account; or

d. the date immediately following 30 days from the date of issue of invoice or any other document, by whatever name called, in lieu thereof by the supplier.

Taxpoint:

- Where it is not possible to determine the time of supply as per the aforesaid rule, the time of supply shall be the date of entry in the books of account of the recipient of supply.
- In case of reverse charge, to determine the time of supply, the payment date is relevant.

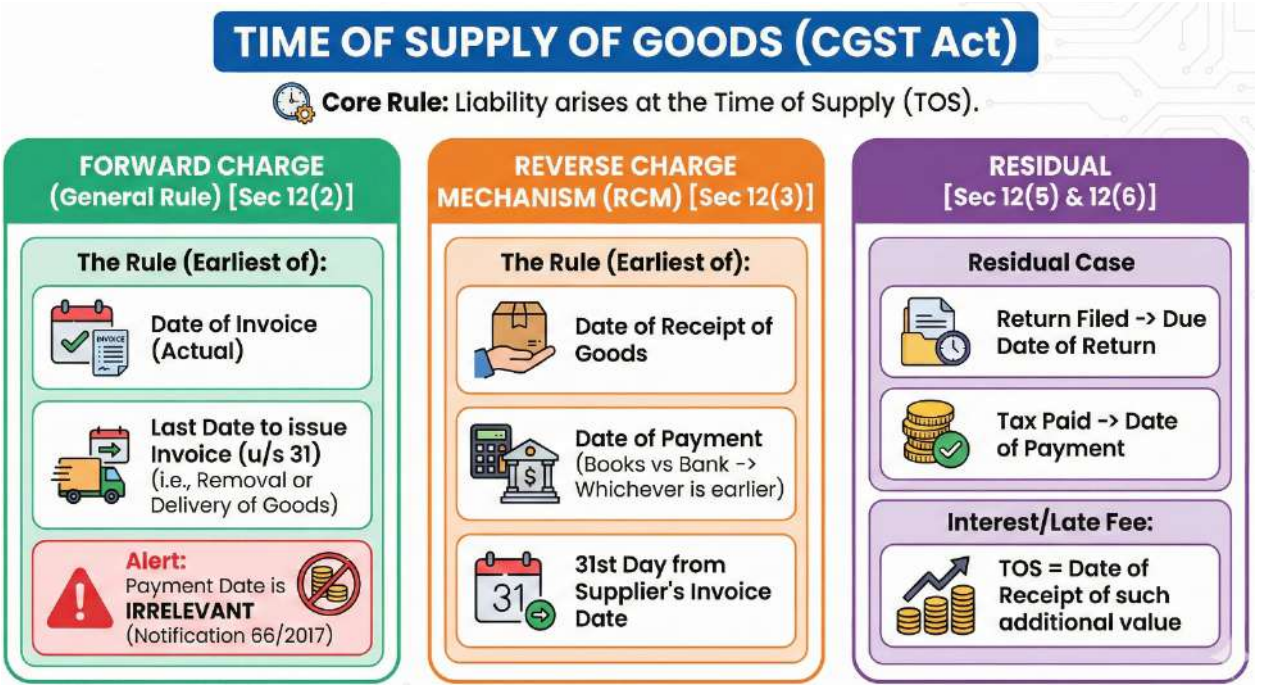
Time of Supply of goods in residual cases [Sec. 12(5)]

Where it is not possible to determine the time of supply under any of the aforesaid provisions, the time of supply shall be:

Where a periodical return has to be filed	The date on which such a return is to be filed
In any other case	The date on which the tax is paid.

Time of Supply in case of enhancement in value on account of interest, late fee, etc. [Sec. 12(6)]

The time of supply to the extent it relates to an addition in the value of supply by way of interest, late fee or penalty for delayed payment of any consideration shall be the date on which the supplier receives such addition in value.



Time of Supply of Services – Forward Charge [Sec. 13(2)]

The time of supply of services shall be the earliest of the following dates, namely:

Situation	Time of Supply
If the invoice is issued within the period prescribed u/s 31	a. The date of issue of the invoice by the supplier; b. The date of receipt of payment - whichever is earlier
If the invoice is not issued within the period prescribed u/s 31	a. The date of provision of service; b. The date of receipt of payment - whichever is earlier
In any other case	The date on which the recipient shows the receipt of services in his books of account

Taxpoint

- "The date of receipt of payment" shall be the date on which the payment is entered in the books of account of the supplier or the date on which the payment is credited to his bank account, whichever is earlier.
- The supply shall be deemed to have been made to the extent it is covered by the invoice or, as the case may be, the payment.
- Where the supplier of taxable service receives an amount up to ₹ 1,000 in excess of the amount indicated in the tax invoice, the time of supply to the extent of such excess amount shall, at the option of the said supplier, be the date of issue of the invoice relating to such excess amount.
- Time limit for issuance of invoice u/s 31 r.w. r. 47 is a general scenario: Within 30 days from the date of the supply of service (45 days in case of insurance/banking company or a financial institution, including NBFC)

Time of Supply of Services – Reverse Charge [Sec. 13(3)]

In case of supplies in respect of which tax is paid or liable to be paid on a reverse charge basis, the time of supply shall be the earlier of the following:

a. the date of payment as entered in the books of account of the recipient; or

b. the date on which the payment is debited in his bank account; or

c. the date immediately following 60 days from the date of issue of the invoice or any other document, by whatever name called, in lieu thereof by the supplier, in cases where the invoice is required to be issued by the supplier.

d. the date of issue of the invoice by the recipient, in cases where the invoice is to be issued by the recipient, the date of issue of the invoice by the recipient

Taxpoint

- Where it is not possible to determine the time of supply as per the aforesaid rule, the time of supply shall be the date of entry in the books of account of the recipient of supply.
- In case of supply by associated enterprises, where the supplier of service is located outside India, the time of supply shall be the date of entry in the books of account of the recipient of supply or the date of payment, whichever is earlier.

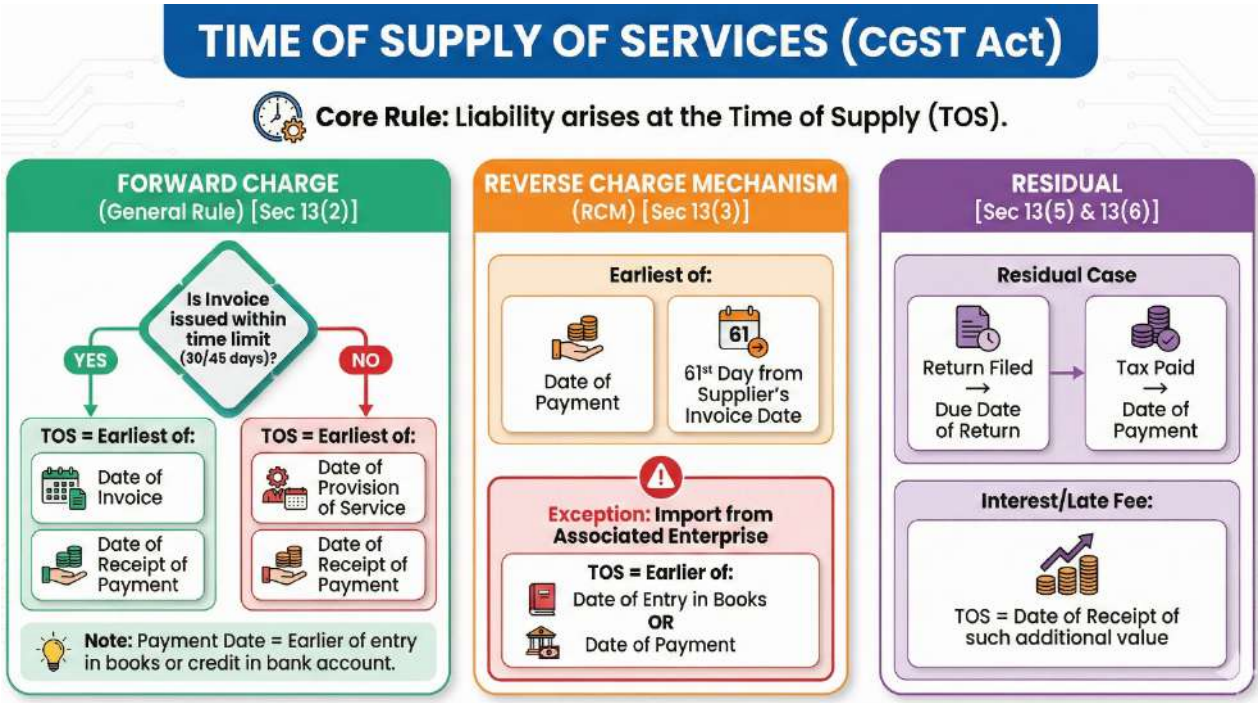
Time of Supply of Services – Residual Cases [Sec. 13(5)]

Where it is not possible to determine the time of supply of service under any of the aforesaid provisions, the time of supply shall be:

Where a periodical return has to be filed	The date on which such a return is to be filed
In any other case	The date on which the tax is paid.

Time of Supply in case of enhancement in value on account of interest, late fee, etc. [Sec. 13(6)]

The time of supply to the extent it relates to an addition in the value of supply by way of interest, late fee or penalty for delayed payment of any consideration shall be the date on which the supplier receives such addition in value.



Change in rate of tax in respect of supply of goods or services [Sec. 14]

The time of supply, where there is a change in the rate of tax in respect of goods or services or both, shall be determined in the following manner

Invoice issued	Payment received	Time of Supply	Applicable Rate
A. *Where the goods or services or both have been supplied before the change in the rate of tax*			
After	After	a. Date of receipt of payment; or b. Date of issue of invoice - whichever is earlier	New Rate

Invoice issued	Payment received	Time of Supply	Applicable Rate
Before	After	Date of issue of invoice	Old Rate
After	Before	Date of receipt of payment	Old Rate
B. *Where the goods or services or both have been supplied after the change in the rate of tax*			
Before	After	Date of receipt of payment	New Rate
Before	Before	a. Date of receipt of payment; or b. Date of issue of invoice - whichever is earlier	Old Rate
After	Before	Date of issue of invoice	New Rate

Taxpoint:

Rate applicability rule: There are three events, viz. (a) supply; (b) issuance of invoice; (c) receipt of payment. Out of these 3 events, at least two events occur after the change in the rate of tax; the new rate is applicable. On the other hand, any of the 2 events occurred before change of rate of tax, old rate is applicable.

Quick Summary

Scenario	Time of Supply
Goods (Forward Charge)	Earlier than the Invoice or the Due date of the invoice
Goods (Reverse Charge)	Earliest of receipt of goods, payment, or the 31st day
Services (Forward Charge)	Earlier of Invoice (if issued within time), else date of provision of service or Payment
Services (Reverse Charge)	Earliest of payment date, bank debit, or 61st day
Rate Change	2 out of 3 events, i.e., invoice issue, receipt of payment, supply, after rate change → New rate applies

Conclusion

In GST, accurately locking in the time of supply is non-negotiable to ensure statutory compliance and to circumvent penal interest. While the baseline rules often revolve around the issuance of an invoice or the receipt of payment, the law is tested on its exceptions—ranging from 31st/61st-day milestones under the reverse charge mechanism to the 'two-event' threshold required during a change in the rate of tax. A comparative grasp of these provisions and their respective deviations will ensure accuracy in both academic assessments and future professional advice.

Topic

Module 4:
Cost Book Keeping

INTERMEDIATE

Group I - Paper-8

Cost Accounting (CA)

Integrated Accounting

The main purpose of financial accounting is to ascertain financial position of any business at the end of any accounting period , whereas the purpose of cost accounting is to ascertain the cost of a product and record the transections related to costs only . Integrated Accounting is a single set of accounts system , which provides both financial and cost accounting information required for management information system. Maintenance of two separate sets of books cause duplication of records of certain items , once in financial books and again in cost books . Maintenance of two sets of books enhances cost. Again when transactions are not large , maintenance of two sets of accounts separately is an unnecessary voluminous task.

As for example :--

For Material purchase on credit.

In Financial Accounts –

Purchase A/c ..... Dr

To Creditors A/c

In Cost Accounts :--

Stores Ledger Control A/c ..... Dr

To Cost Ledger Control A/c

In Integral Accounts

Stores Ledger Control A/c ..... Dr

To Creditors A/c

For Production wages --

In Financial Accounts--

Wages A/c. ..... Dr

To Cash

In Cost Accounts--

Wages Clearance A/c .....Dr

To Cost Ledger Control A/c

In integrated Account --

Wages Clearance A/c. ..... Dr

To Cash A/c

For Production Overhead incurred --

In Financial Accounts--

Production Expenses A/c. ..... Dr

To Cash A/c

In Cost Accounts--

Production Overhead A/c ..... Dr

To Cost Ledger Control A/c

In Integrated Account --

Production Overhead A/c. ..... Dr

To Cash A/c.

For Cash Sales--

In Financial Accounts--

Cash A/c. ..... Dr

To Sales A/c

In Cost Accounts--

Cost Ledger Control A/c ..... Dr

To Sales A/c

In Integrated Accounts--

Cash A/c ..... Dr

To Sales A/c

It may be observed that the Cost Ledger Control A/c has been eliminated in the integrated accounting system.In short this system records the essential points of both cost and financial accounting viz. Stores and Creditors, Wages and Cash, Overhead and Cash, and Debtors and Sales have been recorded in Integrated Accounts.

Reconciliation of Cost Accounts and Financial Accounts

This chapter is important for most of the students related to this subject. Transactions exclusively relevant to Cost Accounts and Financial Accounts are to be identified and to be considered in the reconciliation statement. The amount of difference in items of costs or incomes appearing in both sets are to be identified and to be considered while preparing reconciliation statement. For instance, if profit shown in the cost edger is taken first and the amount that gives rise to differences are added or deducted from it, the resultant figure shoul agree with the profit shown in financial ledger.

Reasons for Difference in Profit--

A. Under or over absorption of overhead.

B. Adoption of different methods of valuation of stock.

C. Items purely of financial accounts.

D. Items purely of cost accounts.

E. Appropriation of profit not dealt with in the cost Accounts.

F. Others.

Now we can go through a detailed study of the above reasons for variation of profits:

(a) Under or over absorption:

In cost accounts in order to ascertain unit cost of a product predetermined rates are charged in respects of overhead. The basis normally used are percentage on prime cost, rate per unit, percentage of direct wages, rate per labour of machine hour. When overhead is recovered on predetermined rates it may not exactly agree with overheads actually incurred during a period. The difference between overhead 'incurred' and the overhead 'recovered' is known as over/under absorption of overhead. In case of under absorption the costing profit will be higher than financial profit and in case of over absorption costing profit will be lower than the financial profit. Now in order to reconcile costing profit with financial profit two adjustments are necessary with financial profit:

(1) In case of under absorption of overhead, the amount of under absorption overhead will have to be added back to financial profit and

(2) In case over absorption of overhead, the amount of over absorption overhead will have to be deducted from financial profit.

(b) Adoption of different methods of valuation of Stock:

In financial accounts the stock is valued based on the principal of "Cast or Market Value, whichever is lower". But in cost accounts the stock of raw materials are valued on the basis of FIFO, LIFO or other methods of pricing issues, WIP may be valued at prime cost or prime cost plus variable cost or prime cost plus variable and fixed overhead. Thus the stock valuation under two sets of accounts will be different and, as such, reconciliation is necessary. This reconciliation will be easier if the following principles are followed :

(1) The lower the opening stock the higher will be the profit, and

(2) The higher the closing stock the higher is the profit, and vise versa.

For instance if the opening stock figures are more in financial accounts, profit as per financial accounts are to be increased to arrive at the profit as per cost accounts, and vise versa.

(c) Items purely of financial nature:

There are some items which are of purely financial nature having no counterpart accounting. This will lead to difference in profit. The common financial expenses are :

(1) Lapses on sale of fixed assets.

(2) Interest on bank loan, debentures, mortgage etc.

(3) Remuneration paid to proprietor in excess at fair reward for services rendered.

(4) Damages payable at Law.

(5) Penalties payable.

(6) Preliminary expenses or goodwill written-off.

(7) Cost for issue of shares, debentures and bonds.

(8) Discount on issue of bonds, debentures etc.

On the other hand, the common financial incomes are :

(1) Profit on sale of Fixed assets.

(2) Interest received on bank deposits.

(3) Interest, dividends etc. received on investments.

(4) Rent received

(5) Fees or commission received on issue of shares, debentures etc.

(6) Transfer fees received.

(d) Items purely of cost accounts:

The items which appear only in cost accounts generally are:

(1) Interest on capital supplied by the proprietor.

(2) Rent on own premises.

(3) Depreciation on fully depreciated assets.

(e) Appropriations of profit not dealt with in the cost accounts:

(1) Transfer to Reserve or other funds.

(2) Corporate tax.

(3) Dividend paid.

(4) Additional provisions for depreciation, bad debts etc.

(5) Appropriation to sinking funds for the purpose of providing for repayment of loans or debentures.

(f) Others:

There are some other items which may lead to difference in profits in two sets of accounts .For example, the rates and methods of charging depreciation may vary in two sets of accounts. Someone may adopt the method of charging direct wages to cost of products at predetermined rates. This will result in a difference between the predetermined amount charged to cost accounts and the actual wages booked in the financial accounts.

Steps for Reconciliation

Step 1

Start with a profit as base as per any set of books (either cost or financial).

Step 2

Items of expenditures already deducted to calculate the above base profit, but not considered for profit shown by other set should be added back.

Step 3

Items of income already bedded to calculate the above base profit but not considered for profit town by other set should be deducted.

Step 4

Similarly, the expenditures not taken into account in calculating the base profit should be deducted.

Step 5

The incomes not taken into accounts in calculating the base profit should be added back.

Step 6

The expenditures under-charged for calculating base profit should be deducted.

Step 7

The amount of income under-stated in calculating base profit should be added.

Step 8

The expenditures over-stated in calculating base profit should be added.

Step 9

The income over-stated in calculating base profit should be deducted.

Step 10

The resultant figures will be the profit as per the other set of books.

Advantages of Reconciliation

Although in an interlocking system both cost and financial accounts are to be maintained separately, it is preferred to integrated system, because of the following advantages:

(1) As the two profits are ascertained independently, arithmetical inaccuracies, if any, are detected quickly.

(2) From the magnitude of variations validity of cost account can be judged. As for example ,a high under-absorption of overhead indicates that products are under cost.

(3) Further variation may also indicate inefficiency which required controlling measures.

(4) Frauds may also be detected if there is any wide difference in value of physical stock and the stock as per books of accounts.

(5) Independency of cost book is preferred as these are not relevant to preparing profit and loss account and so not subject to statutory audit.

Indicate wheather the following statements are true or false :--

a) The need of reconciliation arises only under integrated accounting system.

b) There is only one figure of Profit under integrated accounting system.

c) No accounts for debtors and creditors are opened in Integrated Accounts.

d) Integrated Account eliminate the necessity of operating General Ledger Control Account

e) Loss on Sale of Capital Assets is not included in accounts under integrated system

f) lncom Tax is provided in Cost Accounts only.

The answer will be as follows --

a) False,

b) True,

c) False,

d) True,

e) False,

f) False.

Topic

Module 6: Project Management, Monitoring and Control

INTERMEDIATE

Group II - Paper-9

Operations Management and Strategic Management (OMSM)

Operations Management

In this issue, we will recapitulate our knowledge on CRASHING under project management with a numerical example.

- Crashing is done only on Activities on the critical path
- The activity on the critical path that has the least crash cost/crash time is to be crashed first
- Crashing of an activity is done for one unit period of time in each crashing, i.e. say one activity can be crashed by 3days. Then first crash it by 1 day. Check if there is any change in the critical path. If no change, then crash the activity again by one day. Check the critical path again and then proceed
- If there is more than one critical path, then in each critical path, crash one activity on the basis of the least crash cost/crash time basis

Illustration:

The details of the activities of a project are given below. Find the minimum cost project schedule.

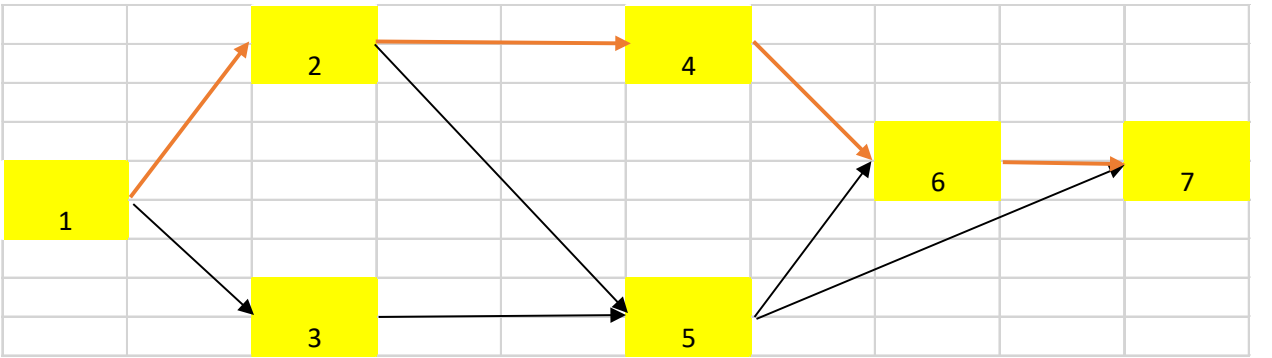
Activity	Duration	Crash Time	Normal Cost	Crash Cost
1-2	8	4	4000	7000
1-3	5	3	8000	12000
2-4	9	6	5500	7000
3-5	7	5	3000	4200
2-5	5	1	9000	13000
4-6	3	2.5	10000	11200
5-6	6	2	6000	8800
6-7	10	7	5000	7700
5-7	9	5	10000	14800
Total			60500	85700
Plus Rs.3000/Week as indirect cost				

Ans:

Prelim computations are given below:

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration
1-2	8	4	4000	7000	1	0	0	0	0	8	0	8	8
1-3	5	3	8000	12000	2	8	8	0	0	5	2	7	7
2-4	9	6	5500	7000	3	5	7	2	8	17	8	17	9
3-5	7	5	3000	4200	4	17	17	0	5	12	7	14	9
2-5	5	1	9000	13000	5	13	14	1	8	13	9	14	6
4-6	3	2.5	10000	11200	6	20	20	0	17	20	17	20	3
5-6	6	2	6000	8800	7	30	30	0	13	19	14	20	7
6-7	10	7	5000	7700					20	30	20	30	10
5-7	9	5	10000	14800					13	22	21	30	17

From the above table, it is clear that the critical path will be 1-2-4-6-7 and accordingly, the network diagram is (Critical path is drawn in red colour)



Total cost of completion of the project = 60500 + 30 * 3000 = 150500

Crash cost/Crash time for different activities are:

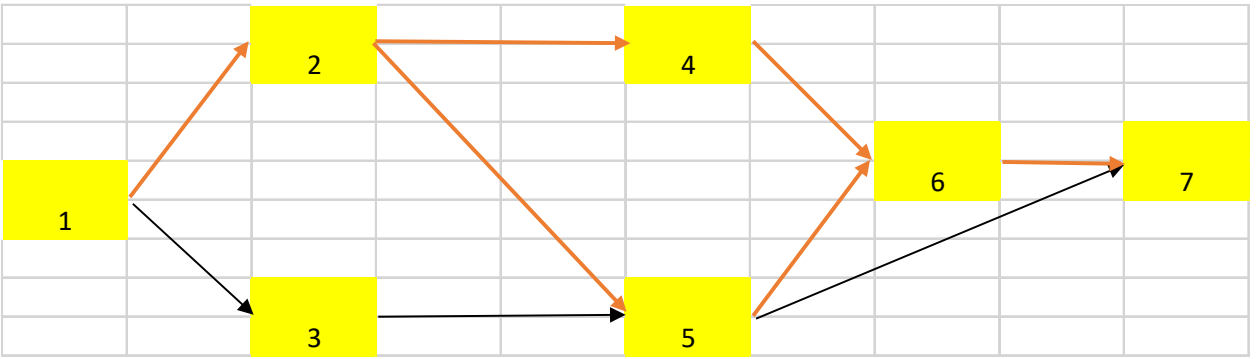
Activity	Crash Cost/ Crash time
1-2	750
1-3	2000
2-4	500
3-5	600
2-5	1000
4-6	2400
5-6	700
6-7	900
5-7	1200

On the critical path, activity 2-4 has the minimum crash cost/crash time. So this activity is to be crashed first by one day, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	8	4	4000	7000	1	0	0	0	0	8	0	8	8	
1-3	5	3	8000	12000	2	8	8	0	0	5	1	6	6	
2-4	8	6	5500	7000	3	5	6	1	8	16	8	16	8	
3-5	7	5	3000	4200	4	16	16	0	5	12	6	13	8	
2-5	5	1	9000	13000	5	13	13	0	8	13	8	13	5	
4-6	3	2.5	10000	11200	6	19	19	0	16	19	16	19	3	
5-6	6	2	6000	8800	7	29	29	0	13	19	13	19	6	
6-7	10	7	5000	7700					19	29	19	29	10	
5-7	9	5	10000	14800					13	22	20	29	16	
Total			60500	85700										
Plus Rs.3000/Week														148000

Total cost of completion = 60500 + 29 * 3000 + (9 - 8) * (500) = 148000

From the above table, it is clear that after 1st crashing, there will be two critical paths, and those are 1-2-4-6-7 & 1-2-5-6-7

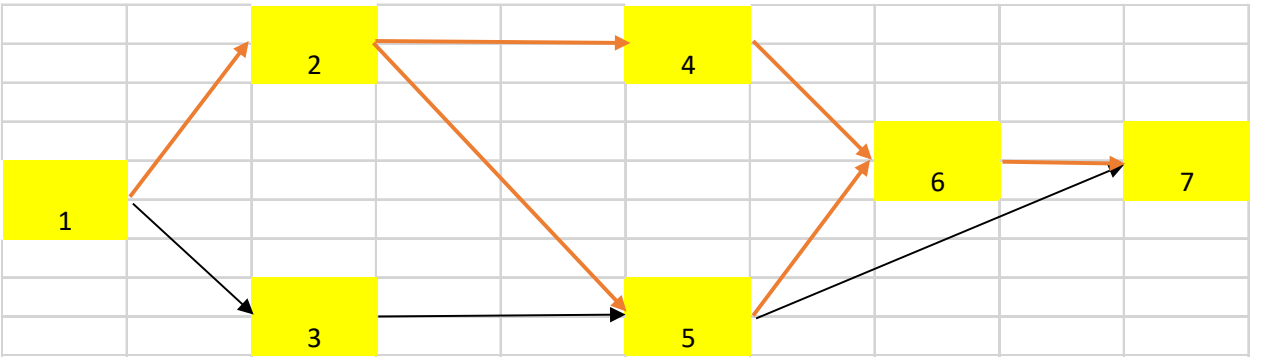


On these critical path activities 2-4 & 5-6 have the minimum crash cost/crash time respectively, and so these activities are to be crashed by one day now, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	8	4	4000	7000	1	0	0	0	0	8	0	8	8	
1-3	5	3	8000	12000	2	8	8	0	0	5	1	6	6	
2-4	7	6	5500	7000	3	5	6	1	8	15	8	15	7	
3-5	7	5	3000	4200	4	15	15	0	5	12	6	13	8	
2-5	5	1	9000	13000	5	13	13	0	8	13	8	13	5	
4-6	3	2.5	10000	11200	6	18	18	0	15	18	15	18	3	
5-6	5	2	6000	8800	7	28	28	0	13	18	13	18	5	
6-7	10	7	5000	7700					18	28	18	28	10	
5-7	9	5	10000	14800					13	22	19	28	15	
Total			60500	85700										
Plus Rs.3000/Week														146200

Total cost of completion = 60500 + 28 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 = 146200

From the above table, it is clear that after this crash, critical paths remained the same.

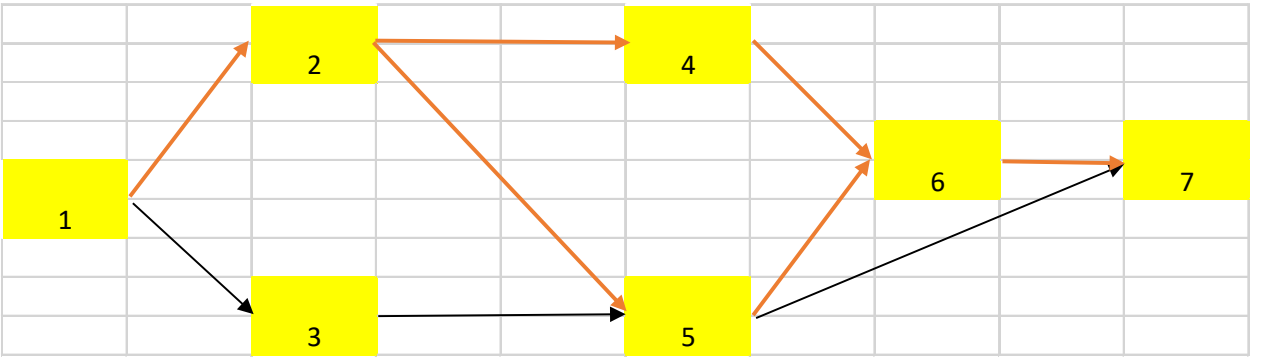


So again activities 2-4 & 5-6 on respective critical paths are to be crashed by one day, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	8	4	4000	7000	1	0	0	0	0	8	0	8	8	
1-3	5	3	8000	12000	2	8	8	0	0	5	1	6	6	
2-4	6	6	5500	7000	3	5	6	1	8	14	8	14	6	
3-5	7	5	3000	4200	4	14	14	0	5	12	6	13	8	
2-5	5	1	9000	13000	5	13	13	0	8	13	8	13	5	
4-6	3	2.5	10000	11200	6	17	17	0	14	17	14	17	3	
5-6	4	2	6000	8800	7	27	27	0	13	17	13	17	4	
6-7	10	7	5000	7700					17	27	17	27	10	
5-7	9	5	10000	14800					13	22	18	27	14	
Total			60500	85700										
Plus Rs.3000/Week														144400

Total cost of completion = 60500 + 27 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 = 144400

From the above table, it is clear that after this crash, the critical path remained the same.

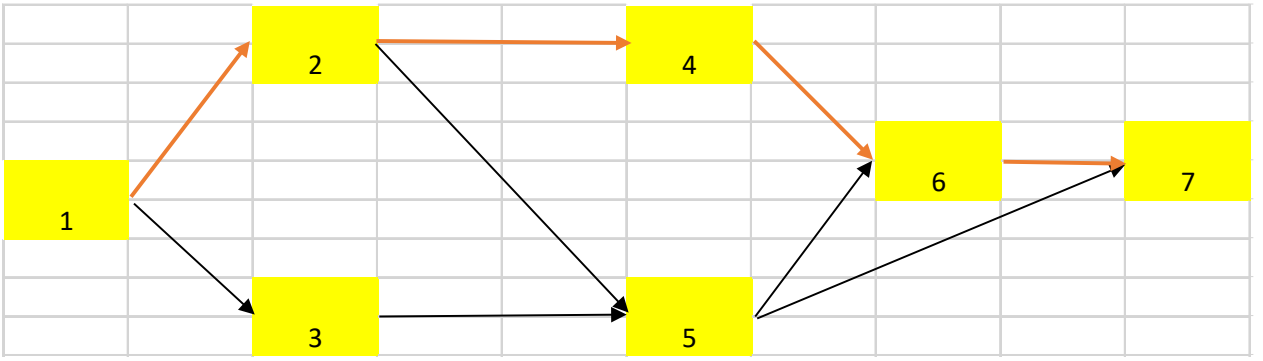


So activities, i.e., 1-2 & 5-6 on respective critical paths, are to be crashed by one day, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	7	4	4000	7000	1	0	0	0	0	7	0	7	7	
1-3	5	3	8000	12000	2	7	7	0	0	5	1	6	6	
2-4	6	6	5500	7000	3	5	6	1	7	13	7	13	6	
3-5	7	5	3000	4200	4	13	13	0	5	12	6	13	8	
2-5	5	1	9000	13000	5	12	13	1	7	12	8	13	6	
4-6	3	2.5	10000	11200	6	16	16	0	13	16	13	16	3	
5-6	3	2	6000	8800	7	26	26	0	12	15	13	16	4	
6-7	10	7	5000	7700					16	26	16	26	10	
5-7	9	5	10000	14800					12	21	17	26	14	
Total			60500	85700										
Plus Rs.3000/Week														142850

Total cost of completion = 60500 + 26 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700 = 142850

From the above table, it is clear that after this crash, the critical path changed, and it is now 1-2-4-6-7

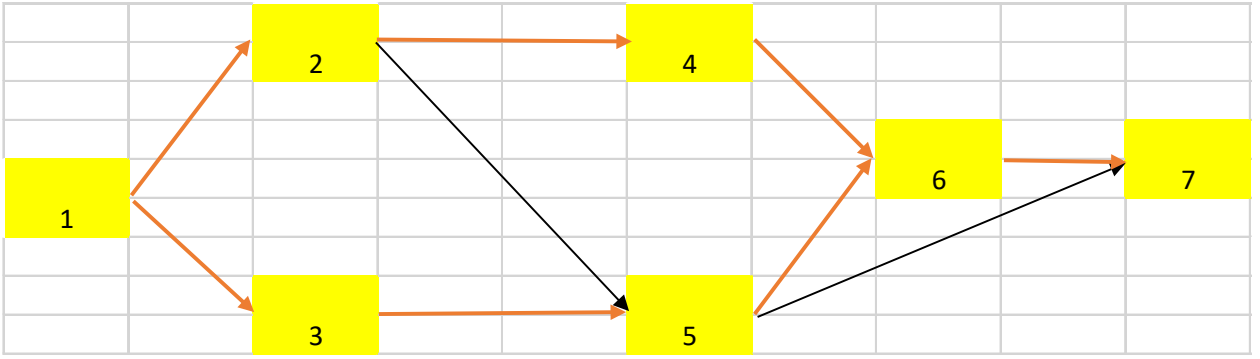


On the new critical path, activity 1-2 is to be crashed by one day, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	6	4	4000	7000	1	0	0	0	0	6	0	6	6	
1-3	5	3	8000	12000	2	6	6	0	0	5	0	5	5	
2-4	6	6	5500	7000	3	5	5	0	6	12	6	12	6	
3-5	7	5	3000	4200	4	12	12	0	5	12	5	12	7	
2-5	5	1	9000	13000	5	12	12	0	6	11	7	12	6	
4-6	3	2.5	10000	11200	6	15	15	0	12	15	12	15	3	
5-6	3	2	6000	8800	7	25	25	0	12	15	12	15	3	
6-7	10	7	5000	7700					15	25	15	25	10	
5-7	9	5	10000	14800					12	21	16	25	13	
Total			60500	85700										
Plus Rs.3000/Week														140600

Total cost of completion =60500+25*3000+1*500+1*500+1*700+1*500+1*700+1*750+1*700+1*750=140600

From the above table, it is clear that after this crash, the critical path will be 1-2-4-6-7 & 1-3-5-6-7

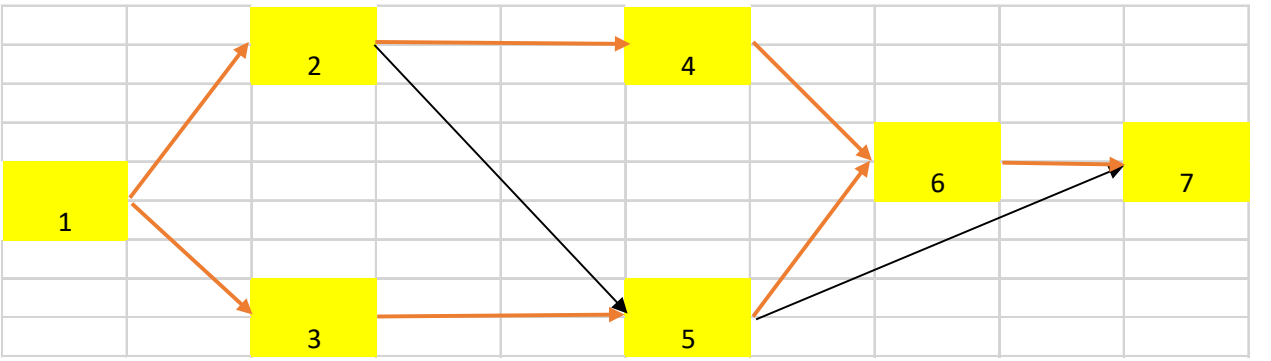


On the critical path, activities 1-2 & 3-5 are to be crashed, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	5	4	4000	7000	1	0	0	0	0	5	0	5	5	
1-3	5	3	8000	12000	2	5	5	0	0	5	0	5	5	
2-4	6	6	5500	7000	3	5	5	0	5	11	5	11	6	
3-5	6	5	3000	4200	4	11	11	0	5	11	5	11	6	
2-5	5	1	9000	13000	5	11	11	0	5	10	6	11	6	
4-6	3	2.5	10000	11200	6	14	14	0	11	14	11	14	3	
5-6	3	2	6000	8800	7	24	24	0	11	14	11	14	3	
6-7	10	7	5000	7700					14	24	14	24	10	
5-7	9	5	10000	14800					11	20	15	24	13	
Total			60500	85700										
Plus Rs.3000/Week														138950

Total cost of completion = 60500 + 24 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700 + 1 * 750 + 1 * 750 + 1 * 600 = 138950

From the above table, it is clear that after this crash, the critical paths remained the same.

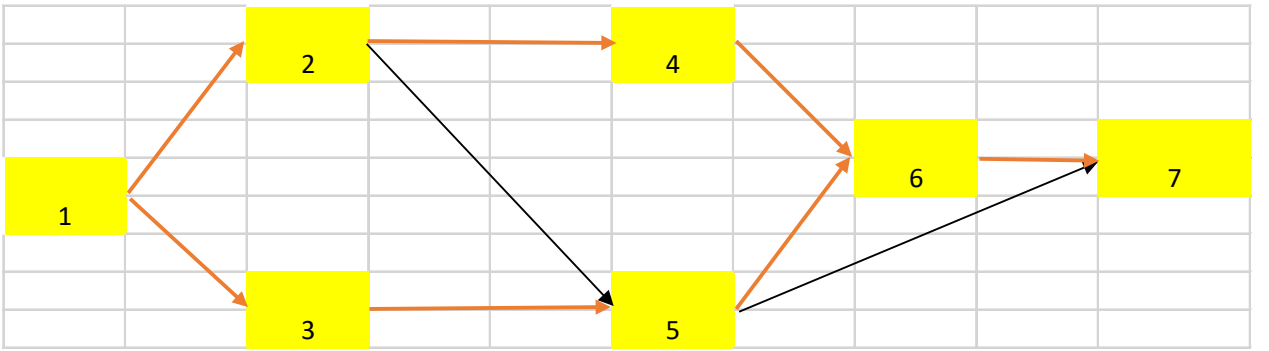


So, the same two activities 1-2 and 3-5 respectively are to be crashed by another unit, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	4	4	4000	7000	1	0	0	0	0	4	0	4	4	
1-3	5	3	8000	12000	2	4	4	0	0	5	0	5	5	
2-4	6	6	5500	7000	3	5	5	0	4	10	4	10	6	
3-5	5	5	3000	4200	4	10	10	0	5	10	5	10	5	
2-5	5	1	9000	13000	5	10	10	0	4	9	5	10	6	
4-6	3	2.5	10000	11200	6	13	13	0	10	13	10	13	3	
5-6	3	2	6000	8800	7	23	23	0	10	13	10	13	3	
6-7	10	7	5000	7700					13	23	13	23	10	
5-7	9	5	10000	14800					10	19	14	23	13	
Total			60500	85700										
Plus Rs.3000/Week														137300

Total cost of completion = 60500 + 23 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700 + 1 * 750 + 1 * 750 + 1 * 600 + 1 * 750 + 1 * 600 = 137300

After this, the crashing critical paths remain the same.

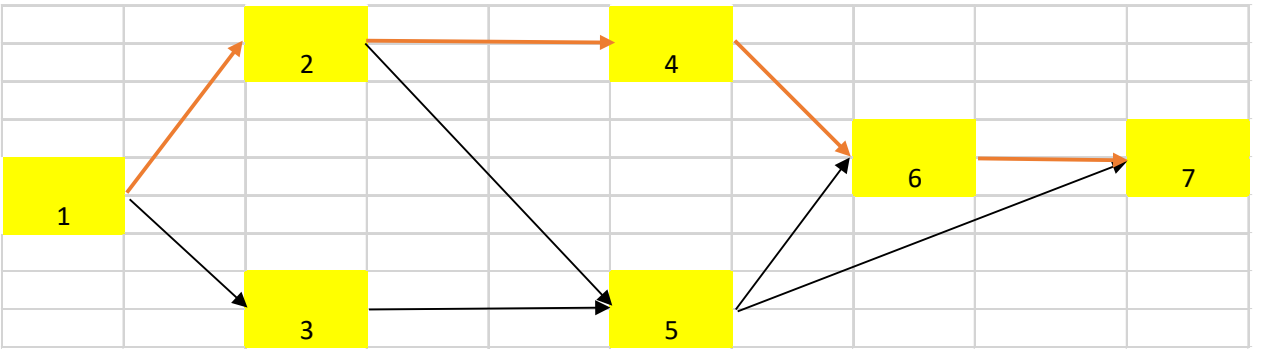


So now activities 6-7 and 5-6 respectively are to be crashed, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	4	4	4000	7000	1	0	0	0	0	4	0	4	4	
1-3	5	3	8000	12000	2	4	4	0	0	5	1	6	6	
2-4	6	6	5500	7000	3	5	6	1	4	10	4	10	6	
3-5	5	5	3000	4200	4	10	10	0	5	10	6	11	6	
2-5	5	1	9000	13000	5	10	11	1	4	9	6	11	7	
4-6	3	2.5	10000	11200	6	13	13	0	10	13	10	13	3	
5-6	2	2	6000	8800	7	22	22	0	10	12	11	13	3	
6-7	9	7	5000	7700					13	22	13	22	9	
5-7	9	5	10000	14800					10	19	13	22	12	
Total			60500	85700										
Plus Rs.3000/Week														135900

Total cost of completion = 60500 + 22 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700 + 1 * 750 + 1 * 750 + 1 * 600 + 1 * 750 + 1 * 600 + 1 * 700 + 1 * 900 = 135900

After this, the critical path will be 1-2-4-6-7

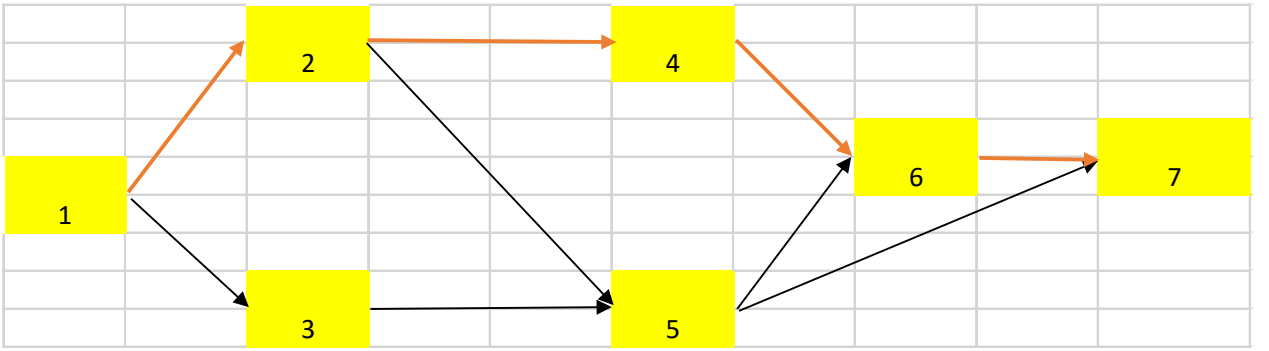


Activity 6-7 is to be crashed by one unit, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	4	4	4000	7000	1	0	0	0	0	4	0	4	4	
1-3	5	3	8000	12000	2	4	4	0	0	5	1	6	6	
2-4	6	6	5500	7000	3	5	6	1	4	10	4	10	6	
3-5	5	5	3000	4200	4	10	10	0	5	10	6	11	6	
2-5	5	1	9000	13000	5	10	11	1	4	9	6	11	7	
4-6	3	2.5	10000	11200	6	13	13	0	10	13	10	13	3	
5-6	2	2	6000	8800	7	21	21	0	10	12	11	13	3	
6-7	8	7	5000	7700					13	21	13	21	8	
5-7	9	5	10000	14800					10	19	12	21	11	
Total			60500	85700										
Plus Rs.3000/Week														133800

Total cost of completion = 60500 + 21 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700 + 1 * 750 + 1 * 750 + 1 * 600 + 1 * 750 + 1 * 600 + 1 * 700 + 1 * 900 + 1 * 900 = 133800

After this, the critical path remains the same.

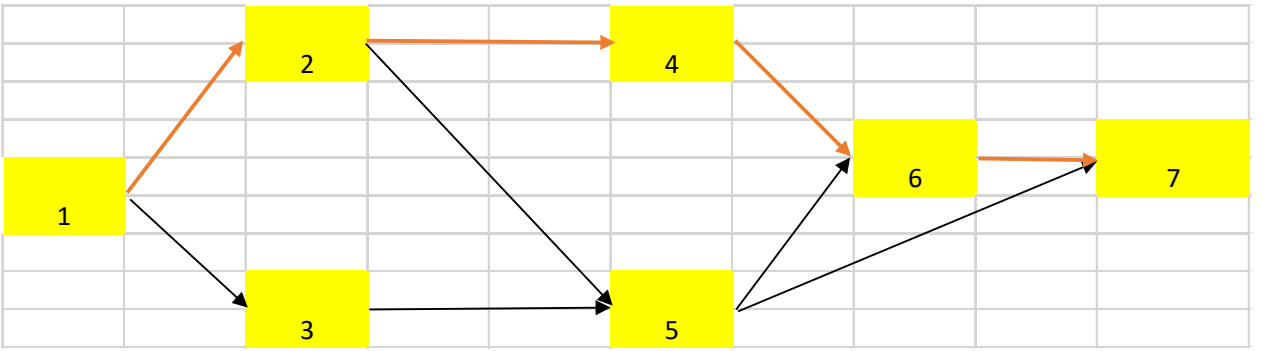


Therefore, activity 6-7 is to be crashed further by one unit, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	4	4	4000	7000	1	0	0	0	0	4	0	4	4	
1-3	5	3	8000	12000	2	4	4	0	0	5	1	6	6	
2-4	6	6	5500	7000	3	5	6	1	4	10	4	10	6	
3-5	5	5	3000	4200	4	10	10	0	5	10	6	11	6	
2-5	5	1	9000	13000	5	10	11	1	4	9	6	11	7	
4-6	3	2.5	10000	11200	6	13	13	0	10	13	10	13	3	
5-6	2	2	6000	8800	7	20	20	0	10	12	11	13	3	
6-7	7	7	5000	7700					13	20	13	20	7	
5-7	9	5	10000	14800					10	19	11	20	10	
Total			60500	85700										
Plus Rs.3000/Week														131700

Total cost of completion = 60500 + 20 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700+ 1 * 750 + 1 * 750 + 1 * 600 + 1 * 750 + 1 * 600 + 1 * 700 + 1 * 900 + 1 * 900 + 1 * 900 = 131700

After this, the critical path remains 1-2-4-6-7



Now in this critical path, activities 1-2, 2-4, and 6-7 are already crashed to the fullest. So the only remaining activity 4-6 is to be crashed by 0.5 day, and the result is

Activity	Duration	Crash Time	Normal Cost	Crash Cost	Event	EOT	LOT	Slack	EST	EFT	LST	LFT	Duration	Total Cost
1-2	4	4	4000	7000	1	0	0	0	0	4	0	4	4	
1-3	5	3	8000	12000	2	4	4	0	0	5	0.5	5.5	5.5	
2-4	6	6	5500	7000	3	5	5.5	0.5	4	10	4	10	6	
3-5	5	5	3000	4200	4	10	10	0	5	10	5.5	10.5	5.5	
2-5	5	1	9000	13000	5	10	10.5	0.5	4	9	5.5	10.5	6.5	
4-6	2.5	2.5	10000	11200	6	12.5	12.5	0	10	12.5	10	12.5	2.5	
5-6	2	2	6000	8800	7	19.5	19.5	0	10	12	10.5	12.5	2.5	
6-7	7	7	5000	7700					12.5	19.5	12.5	19.5	7	
5-7	9	5	10000	14800					10	19	10.5	19.5	9.5	
Total			60500	85700										
Plus Rs.3000/Week														131400

Total cost of completion = 60500 + 19.5 * 3000 + 1 * 500 + 1 * 500 + 1 * 700 + 1 * 500 + 1 * 700 + 1 * 750 + 1 * 700 + 1 * 750 + 1 * 750 + 1 * 600 + 1 * 750 + 1 * 600 + 1 * 700 + 1 * 900 + 1 * 900 + 1 * 900 + 0.5 * 2400 = 131400

After this crashing the critical path remains 1-2-4-6-7 where each activity is already crashed to the maximum permissible limit and so further crashing is not possible.

So the project can be completed earliest by 19.5 days at a cost of R131400.

Suggestions:

This writing is an aid to the topic discussed in the study guide on Paper 9- Operations Management & Strategic Management, written and issued by the Institute. Further knowledge could be developed from supplementary readings: Modern Production/Operations Management by Buffa and Sarin; Operations Management by R.S. Russell & B.W. Taylor; Operations Management by Lee J. Krajewski.

Best Wishes.

Topic

Module 2:
Preparation of the Statement of Profit and Loss and Balance Sheet (As per Schedule III of Companies Act, 2013)

Module 6:
Basic Concepts of Auditing

INTERMEDIATE

Group II - Paper-10

Corporate Accounting and Auditing (CAA)

Section A: Corporate Accounting

Topic: Preparation of the Statement of Profit and Loss and Balance Sheet

1. Schedule III to the Companies Act, 2013 primarily prescribes the format of:

a) CSR Report

b) Financial Statements of companies

c) Auditor's Report

d) Board's Report

Answer: b) Financial Statements of companies

2. Division I of Schedule III applies to:

a) Banking companies

b) Insurance companies

c) Companies following Accounting Standards (AS)

d) Companies following Ind AS

Answer: c) Companies following Accounting Standards (AS)

3. Comparative figures presented in the financial statements should normally relate to:

a) Next accounting year

b) Previous reporting period

c) Five previous years

d) Current year only

Answer: b) Previous reporting period

4. If compliance with Schedule III is insufficient for a true and fair view, the company should:

a) Ignore the requirement

b) Provide additional disclosures

c) Seek shareholders' approval only

d) Prepare only notes to accounts

Answer: b) Provide additional disclosures

5. Items of similar nature and function should generally be:

a) Reported separately irrespective of the amount

b) Aggregated

c) Ignored

d) Presented alphabetically

Answer: b) Aggregated

6. Material items should be:

a) Clubbed with miscellaneous expenses

b) Disclosed separately

c) Omitted from financial statements

d) Shown only in Board's Report

Answer: b) Disclosed separately

7. Schedule III requires disclosures to be made primarily through:

a) Balance Sheet only

b) Notes to Accounts wherever necessary

c) Auditor's Report

d) Director's Report only

Answer: b) Notes to Accounts wherever necessary

8. Offsetting of assets and liabilities is:

a) Mandatory

b) Permitted in all situations

c) Not permitted unless specifically required

d) Optional

Answer: c) Not permitted unless specifically required

9. Rounding off of figures under Schedule III depends mainly upon:

a) Number of shareholders

b) Turnover of the company

c) Total income of directors

d) Number of employees

Answer: b) Turnover of the company

10. Financial statements prepared under Schedule III should present:

a) Only statutory information

b) True and fair view of financial position and performance

c) Income tax computation

d) Secret reserves

Answer: b) True and fair view of financial position and performance

11. Revenue from operations is presented:

a) After finance costs

b) At the beginning of the Statement of Profit and Loss

c) After tax expense

d) Below exceptional items

Answer: b) At the beginning of the Statement of Profit and Loss

12. Finance costs generally include:

a) Depreciation

b) Interest expense

c) Income tax

d) Dividend received

Answer: b) Interest expense

13. Depreciation and amortisation expense is disclosed:

a) As an appropriation of profit

b) As an expense in the Statement of Profit and Loss

c) Under equity

d) Under reserves

Answer: b) As an expense in the Statement of Profit and Loss

14. Profit before tax is determined:

a) Before deducting finance costs

b) After all income and expenses except tax

c) Before operating expenses

d) After dividend distribution

Answer: b) After all income and expenses except tax

15. Tax expense disclosed in the Statement of Profit and Loss generally includes:

a) Current tax and deferred tax

b) GST only

c) Customs duty only

d) Dividend distribution tax

Answer: a) Current tax and deferred tax

16. Property, Plant and Equipment should generally be presented:

a) Under Current Assets

b) Under Non-current Assets

c) Under Current Liabilities

d) Under Equity

Answer: b) Under Non-current Assets

17. Capital Work-in-Progress is disclosed separately under:

a) Current Assets

b) Non-current Assets

c) Current Liabilities

d) Equity

Answer: b) Non-current Assets

18. Investments expected to be held for more than twelve months are generally classified as:

a) Current Investments

b) Non-current Investments

c) Inventories

d) Trade Receivables

Answer: b) Non-current Investments

19. Trade receivables should generally be classified based on:

a) Colour of invoices

b) Outstanding period and credit impairment disclosures

c) Amount of dividend

d) Number of customers

Answer: b) Outstanding period and credit impairment disclosures

20. Cash and Cash Equivalents generally include:

a) Long-term fixed deposits only

b) Cash in hand and balances with banks

c) Land held for sale

d) Investments in associates

Answer: b) Cash in hand and balances with banks

21. Loans classified as non-current assets are shown under:

a) Inventories

b) Non-current Assets

c) Equity

d) Current Liabilities

Answer: b) Non-current Assets

22. Inventories are presented:

a) Under Current Assets

b) Under Non-current Assets

c) Under Equity

d) Under Current Liabilities

Answer: a) Under Current Assets

23. Security deposits recoverable after twelve months are generally classified as:

a) Current Assets

b) Non-current Assets

c) Current Liabilities

d) Equity

Answer: b) Non-current Assets

24. Advances recoverable within the normal operating cycle are generally presented as:

a) Non-current Assets

b) Current Assets

c) Equity

d) Long-term Borrowings

Answer: b) Current Assets

25. Schedule III requires a separate disclosure of trade receivables that are:

a) Fully collected

b) Outstanding for specified ageing periods

c) Received in cash

d) Covered by insurance only

Answer: b) Outstanding for specified ageing periods

Section B: Auditing

Topic: Basic Concepts of Auditing

- **Comprehensive Questions**

Question 1: Discuss the inherent limitations of auditing as per SA 200

Answer:

SA 200 – ***Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing*** recognises that an audit cannot provide absolute assurance that the financial statements are free from material misstatement. This is because auditing is subject to certain **inherent limitations** arising from the nature of financial reporting, the nature of audit procedures, and practical constraints. Consequently, the auditor provides **reasonable assurance**, not absolute assurance.

The inherent limitations of auditing are discussed below.

1. Nature of Financial Reporting

Financial statements contain many items that require management to exercise judgment and make estimates. Accounting estimates such as depreciation, provisions for doubtful debts, impairment losses, warranty obligations, and fair value measurements involve assumptions about future events and uncertainties. Reasonable assumptions can yield different results, making it impossible for the auditor to determine a single "correct" amount. Consequently, the auditor can only assess whether management's estimates are reasonable and comply with the applicable financial reporting framework.

2. Nature of Audit Procedures

Auditors rely on audit procedures to obtain sufficient and appropriate audit evidence. However, these procedures have inherent limitations. Management or employees may deliberately conceal fraud through collusion, forgery, falsification of documents, or intentional omission of transactions. Sophisticated fraud can make seemingly genuine documents appear authentic, limiting the auditor's ability to detect material misstatements. Furthermore, auditors often rely on representations from management and external confirmations, which may themselves have limitations.

3. Use of Sampling

It is generally impracticable for auditors to examine every transaction undertaken by an entity. Therefore, auditors use **audit sampling** and other selective testing techniques. While sampling enables an efficient audit, there is always a risk that the selected sample may not represent the entire population. As a result, some material misstatements may remain undetected despite the application of appropriate audit procedures.

4. Time and Cost Constraints

Audits must be completed within a reasonable period and at a reasonable cost. It is neither practical nor economically feasible for auditors to examine every document or verify every transaction in detail. Therefore, auditors plan their work using a risk-based approach, concentrating on areas where the risk of material misstatement is higher. These practical constraints contribute to the inherent limitations of an audit.

5. Dependence on Management Information

The auditor's work largely depends on the accounting records, explanations, and information provided by management. Although the auditor performs procedures to verify the reliability of this information, the audit process cannot eliminate the possibility that

management has intentionally withheld information or provided misleading explanations.

6. **Limitations in Detecting Fraud**

   Fraud is generally more difficult to detect than error because it often involves deliberate concealment through collusion, forgery, manipulation of records, or override of internal controls by management. Even a properly planned and executed audit may fail to detect certain types of fraud, particularly those involving senior management or multiple parties acting together.

7. **Internal Control Limitations**

   Auditors assess and rely on the entity's system of internal control while planning the audit. However, internal controls themselves have inherent limitations. Human error, management override, collusion among employees, and changes in operating conditions may reduce the effectiveness of internal controls. Consequently, reliance on internal controls cannot guarantee the detection of all material misstatements.

8. **Persuasive Rather Than Conclusive Evidence**

   Most audit evidence is **persuasive rather than conclusive**. The auditor forms an opinion by evaluating evidence from various sources rather than proving every transaction with absolute certainty. Since evidence is rarely definitive in every respect, the audit opinion is based on professional judgment and the overall sufficiency and appropriateness of the evidence collected.

9. **Professional Judgment**

   Auditing involves extensive use of professional judgment in determining materiality, assessing audit risk, selecting audit procedures, evaluating evidence, and drawing conclusions. Experienced auditors may reach different yet reasonable conclusions in certain situations. This reliance on judgment contributes to the inherent limitations of an audit.

10. **Reasonable Assurance Rather Than Absolute Assurance**

    Because of all the above limitations, an audit cannot provide absolute assurance that the financial statements are completely free from material misstatement due to fraud or error. Instead, the auditor provides **reasonable assurance**, which is a high but not absolute level of assurance. This means there is always an unavoidable risk that some material misstatements may go undetected, even when the audit is properly planned and conducted in accordance with the Standards on Auditing.

    Because of the above inherent limitations, the objective of an audit is to obtain sufficient appropriate audit evidence to provide **reasonable assurance** and express an independent opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Topic

Module 3:
Tools for Financial Analyses

Module 9:
Data Processing, Organisation, Cleaning and Validation

INTERMEDIATE

Group II - Paper-11

Financial Management and Business Data Analytics (FMDA)

Financial Management

Fund Flow Analysis

Preparation and Analysis of Fund Flow Statement

Two statements are involved in preparing and analysing the fund flow statement.

- Statement or Schedule of Changes in Working Capital
- Statement of Funds Flow

1. **Statement of Changes in Working Capital:** This statement, when prepared, shows whether the working capital has increased or decreased during the two balance sheet dates. But this does not give the reasons for the increase or decrease in working capital. This statement is prepared by comparing the current assets and the current liabilities of two periods.
2. **Funds Flow Statement:** Funds Flow Statement is also called the Statement of Changes in Financial Position, or Statement of Sources and Applications of Funds or where got, where gone Statement. The purpose of the funds flow statement is to provide information about the enterprise's investing and financing activities.

The activities that the funds flow statement describes can be classified into two categories:

(i) Activities that generate funds, called Sources. It includes an increase in liabilities, an increase in capital and a decrease in assets and investments.

(ii) Activities that involve spending funds, called Uses. It includes a decrease in liabilities, a decrease in capital and an increase in assets and investments.

Fund Flow Statement (Horizontal Form)

Sources	₹	Applications	₹
1. Funds from Operations	xxxx	1. Loss from Operations	xxxx
2. Issue of share capital	xxxx	2. Redemption of shares	xxxx
3. Issue of Debentures	xxxx	3. Redemption of Debentures	xxxx
4. Long-term borrowings	xxxx	4. Repayment of Loans	xxxx
5. Sale of Assets/ Investments	xxxx	5. Purchase of Assets/ Investments	xxxx
6. Non-operating incomes	xxxx	6. Payment of Dividends	xxxx
7. Any other sources	xxxx	7. Any other use	xxxx
8. Decrease in Working Capital (Bal fig)	xxxx	8. Increase in Working Capital (Bal fig)	xxxx
Total	xxxx	Total	xxxx

Note: If the total of funds received exceeds that of the funds applied, the difference is excess funds, which will be represented by an increase in working capital. On the other hand, if the total of funds used exceeds the total of funds received, the difference is a shortage in funds represented by a decrease in working capital.

Illustration 1

The summarised Balance Sheets of COX Ltd. as on 31st March, 2024 and 2025 are as follows:

Particulars	31st March 2024 (₹)	31st March 2025 (₹)
Fixed Assets (at Cost)	16,00,000	19,00,000
Less: Depreciation	4,60,000	5,80,000
Net Fixed Assets	11,40,000	13,20,000
Trade Investments	2,00,000	1,60,000
Current Assets	5,60,000	6,60,000
Preliminary Expenses	40,000	20,000
Total Assets	19,40,000	21,60,000

Particulars	31st March 2024 (₹)	31st March 2025 (₹)
Share Capital	6,00,000	8,00,000
Capital Reserve	–	20,000
General Reserve	3,40,000	4,00,000
Profit & Loss A/c	1,20,000	1,50,000
Debentures	4,00,000	2,80,000
Liabilities for Goods & Services	2,40,000	2,60,000
Provision for Income Tax	1,80,000	1,70,000
Proposed Dividend	60,000	72,000
Unpaid Dividend	–	8,000
Total Equity & Liabilities	**19,40,000**	**21,60,000**

Additional information during the year 2024 - 25:

(i) The Company sold one machine for ₹50,000. The cost of the machine was ₹1,28,000, and the depreciation provided on it amounted to ₹70,000.

(ii) Provided depreciation amounting to ₹1,90,000.

(iii) Redeemed 30% of the debentures at ₹103.

(iv) Sold some trade investments at a profit, which was credited to Capital Reserve.

(v) Decided to value stock at cost, whereas previously the practice was to value stock at cost less 10%. The stock, according to the books on 31.03.2024, was ₹1,08,000. The stock on 31.03.2025 was correctly valued at cost.

You are required to prepare:

(a) Statement of Changes in Working Capital and

(b) Funds Flow Statement during the year 2024-25

Solution:

Statement of Changes in Working Capital

Particulars	31st March 2024 (₹)		31st March 2025 (₹)	
A. Current Assets	5,60,000			
Add: Increase due to Adjustment	12,000			
Total Current Assets		**5,72,000**		**6,60,000**
B. Less Current Liabilities				
- for Goods & Services	2,40,000		2,60,000	
- for Income Tax	1,80,000	**4,20,000**	1,70,000	**4,30,000**
Working Capital (A – B)		1,52,000		2,30,000
Increase in Working Capital		78,000		
		2,30,000		**2,30,000**

Funds Flow Statement for the Year 2024-25

Sources	₹	Applications	₹
Funds from Operations:	1,50,000	Purchase of Fixed Assets	4,28,000
Net Profit		Redemption of Debentures *(₹ 4,00,000 × 30% + ₹ 3,600 Premium)*	1,23,600
Add: Depreciation	1,90,000	Increase in Working Capital	78,000
Add: Loss on Sale of Assets	8,000	Dividend Paid:	

Sources	₹	Applications	₹
Add: Premium on Redemption charged to Profit & Loss A/c	3,600	Proposed Dividend for 2023-24	60,000
Add: Preliminary Expenses Written Off *(₹40,000 − ₹ 20,000)*	20,000	Less: Unpaid Dividend	(8,000)
Funds from Operations	**3,71,600**		**52,000**
Sale of Investments *(Cost realised ₹ 2,00,000 − ₹ 1,60,000 = ₹ 40,000; Profit credited to Capital Reserve ₹ 20,000)*	60,000		
Issue of Equity Shares *(₹ 8,00,000 − ₹ 6,00,000)*	2,00,000		
Sale of Fixed Assets	50,000		
Total Sources	**6,81,600**	**Total Applications**	**6,81,600**

Workings:

Profit and Loss Appropriation Account for the Year Ended 31.03.2025

Dr. Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To Proposed Dividend	72,000	By Balance b/d	1,20,000
To General Reserve (Transfer)	60,000	By Increase in Stock (31.03.2024)	12,000
To Balance c/d	1,50,000	By Profit & Loss A/c (Balancing Figure)	1,50,000
Total	**2,82,000**	**Total**	**2,82,000**

Adjustment of the Value of Stock

Value as on 31.03.2024 as per Balance Sheet	Value as on 31.03.2024 as per Adjustments
90	100
1,08,000	X

X = (100 × ₹1,08,000) / 90

= ₹ 1,20,000

Increase in the Value of Stock:

Particulars	₹
Value after adjustments	1,20,000
Less: Value as per Books (Balance Sheet)	1,08,000
Increase in Value of Stock	**12,000**

Fixed Assets Account

Dr. Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	16,00,000	By Disposal of Assets A/c	1,28,000
To Bank A/c – Purchases (Balancing Figure)	4,28,000	By Balance c/d	19,00,000
Total	**20,28,000**	**Total**	**20,28,000**

Accumulated Depreciation Account

Dr. Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To Disposal of Fixed Assets A/c (Transfer)	70,000	By Balance b/d	4,60,000
To Balance c/d	5,80,000	By Profit & Loss A/c	1,90,000
Total	**6,50,000**	**Total**	**6,50,000**

Disposal of Fixed Assets Account

Dr. Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To Fixed Assets Account	1,28,000	By Accumulated Depreciation A/c	70,000
		By Bank Account	50,000
		By Profit & Loss A/c (Loss on Sale)	8,000
Total	**1,28,000**	**Total**	**1,28,000**

Data Analytics

Data Cleaning

Data Cleaning: Meaning

Data cleaning or cleansing is the process of identifying, correcting or deleting inaccurate, corrupted, improperly formatted, duplicate, or insufficient data from a dataset. It removes irrelevant data from a dataset. Data cleaning is different from data transformation. The process of changing data from one format or structure to another is known as data transformation. Transformation procedures are sometimes known as data wrangling or data munging, since they map and change "raw" data into another format for warehousing and analysis.

Steps for data cleaning:

Step 1: Collect and understand data: At first, gather data from various sources such as databases, spreadsheets, surveys, websites, or ERP systems. Thereafter, analyse to understand the structure, variables and data types.

Step 2: Examine the data: Examine the dataset from different perspectives, such as quality, number of rows, columns, missing values, and duplicate records.

Step 3: Remove duplicate data: Eliminate unnecessary observations from your dataset, such as duplicate or irrelevant observations. Most duplicate observations will occur during data collection. When you merge data sets from numerous sites, scrape data, or get data from customers or several departments, there is a potential to produce duplicate data.

Step 4: Fix structural errors: When measuring or transferring data, detect unusual naming standards, typos, or wrong capitalisation. These contradictions may lead to mislabeled classes or groups. For instance, "N/A" and "Not Applicable" may both be present, but they should be examined as a single category.

Step 5: Filter unwanted outliers: Outliers are unusually high or low values that differ significantly from the rest of the data. Remember that the existence of an outlier does not imply that it is erroneous. This step is required to validate the number. Consider deleting an outlier if it appears to be unrelated to the analysis or an error.

Step 6: Handle missing data: Many algorithms do not accept missing values; hence, missing data cannot be ignored. There are several approaches to handling missing data. As a first alternative, the observations with missing values may be dropped, but doing so may result in the loss of information. This should be kept in mind before doing so. As a second alternative, the missing numbers may be entered based on other observations. Again, there is a chance that the data's integrity may be compromised, as action may be based on assumptions rather than real observations.

Step 7: Validation data inconsistency: One of the important steps is the validation of data inconsistency. In this step, check the logical relationship between variables.

Step 8: Verify and document the cleaning process: Before using the dataset for any decision-making, recheck the cleaned dataset and confirm that all identified issues have been resolved. Document every cleaning step for transparency and reproducibility.

Source: https://www.ovaledge.com/blog/data-cleaning-techniques

Topic

Module 3: Marginal Costing

INTERMEDIATE

Group II - Paper-12

Management Accounting (MA)

Module 3: Marginal Cost – Decision Making

Marginal Cost

The term 'marginal cost' is defined as the amount at any given volume of output by which aggregate costs are changed, if the volume of output is increased or decreased by one unit. It is a variable cost of one unit of a product or a service, i.e., a cost which would be avoided if that unit were not produced or provided.

Marginal Cost = Variable Cost = Direct Labour+ Direct Material + Direct Expenses + Variable Overheads

In other words, Marginal costing may be defined as the technique of presenting cost data wherein variable costs and fixed costs are shown separately for managerial decision-making. It should be clearly understood that marginal costing is not a method of costing like process costing or job costing. Rather, it is simply a method or technique of the analysis of cost information for the guidance of management.

Marginal Costs can be presented as follows:

Particulars	Amount
Raw Material Cost	x
Direct Labour Cost	x
Direct Expenses	x
Variable Manufacturing Expenses	x
Variable portions of Administration Expenses	x
Variable portions of Selling and Distribution Expenses	x
Total Marginal Costs/ Variable Costs	xxxx

Features of Marginal Costing

Features of marginal costing are as follows:

a. Marginal costing is used to determine the impact of variable costs on the volume of production or output.

b. Break-even analysis is an integral and important part of marginal costing.

c. Contribution of each product or department is a foundation for knowing the profitability of the product or department.

d. Addition of variable cost and profit to contribution is equal to the selling price.

e. Marginal costing is the basis of valuation of stock of finished product and work in progress.

f. Fixed cost is recovered from the contribution, and variable cost is charged to production.

g. Costs are classified on the basis of fixed and variable costs only. Semi-fixed costs are also divided into fixed costs and variable costs. costs

Assumptions of Marginal Costing

The technique of marginal costing is based upon the following assumptions:

a. All elements of cost-production, administration and selling and distribution can be segregated into fixed and variable components.

b. Variable cost remains constant per unit of output irrespective of the level of output and thus fluctuates directly in proportion to changes in the volume of output.

c. The selling price per unit remains unchanged or constant at all levels of activity.

d. Fixed costs remain unchanged or constant for the entire volume of production.

e. The volume of production or output is the only factor that influences the costs.

Contribution

Contribution can be computed by subtracting variable costs from sales or by adding fixed costs and profit. Symbolically,

$$C = S - V$$

Where

C = Contribution, S = Selling Price, V = Variable Cost

Also $C = F + P$

Where F = Fixed Cost and P = Profit

Profit Volume Ratio (P/V Ratio) or Contribution Ratio

P/V ratio or contribution ratio is an association of two variables. From this, one may assume that it is the ratio of profit and sales. But it is not so. It is the ratio of Contribution to Sales.

Symbolically,

$$\text{P/V ratio} = \frac{\text{Contribution per unit}}{\text{Key Factor}} \times 100 \rightarrow (1)$$

$$\Rightarrow \text{P/V ratio} = \frac{\text{Contribution}}{\text{Sales*}} \times 100$$

$$\Rightarrow \text{Contribution} = \text{Sales} \times \text{P/V ratio} \rightarrow (2)$$

$$\Rightarrow \text{Sales} = \frac{\text{Contribution}}{\text{P/V Ratio}} \times 100 \rightarrow (3)$$

When cost accounting data is given for two periods, then:

$$\text{P/V ratio} = \frac{\text{Change in Contribution}}{\text{Change in Sales}} \times 100$$

$$\text{or, P/V ratio} = \frac{\text{Change in Profit}}{\text{Change in Sales}} \times 100$$

* When the limiting factor or key factor is not specifically mentioned, Sales is considered the limiting factor.

Break-even Analysis

Break-even analysis can be used to help management select an action when several alternatives exist. This analysis is based on the conditions that variable costs will vary in constant proportion to the sales volume and that fixed costs will be fixed over a prescribed or relevant range of activity.

Therefore, if management wishes to test new proposals that will change the percentage of variable costs to sales volume, or the total amount of fixed costs, or a combination of these changes, then it can use the basic breakeven equation to calculate the results.

Break-even point represents the minimum level of sales (revenue or volume) needed to cover total costs (fixed and variable). At the breakeven point, profit is equal to zero because our total sales income is equal to total expenditure.

The formula for the breakeven volume is below:

Contribution per unit = unit selling price – unit variable costs

- Profit = (sales volume × contribution per unit) – fixed costs
- Break-even point = activity level at which there is neither profit nor loss = Total Fixed Costs÷ Contribution per unit = Contribution required to break-even÷ Contribution per unit
- Contribution÷ sales (C÷ S) ratio = profit/volume (P/V) ratio = (contribution÷ sales) × 100%
- Sales revenue at break-even point = fixed costs ÷ C/S ratio
- Margin of safety (in units) = Budgeted sales units – Break-even sales units
- Margin of safety (as %) = [(Budgeted sales - Break-even sales) ÷ Budgeted sales] × 100%
- Sales volume to achieve a target profit = (Fixed cost + Target profit) ÷ Contribution per unit

Multiple Choice Questions (MCQs):

A company has a contribution to sales ratio of 40%. It maintains a margin of safety of 20%, and annual fixed costs amount to ₹ 24 lakh. Answer questions 1 to 4 on the basis of this information.

1. Break-even sales
   - **a) ₹ 60 lakhs**
   - b) ₹ 40 lakhs
   - c) ₹ 50 lakhs
   - d) ₹ 80 lakhs
2. Margin of Safety and Total Sales
   - a) ₹ 12 lakhs and ₹ 72 lakhs
   - b) ₹ 18 lakhs and ₹ 90 lakhs
   - c) ₹ 16 lakhs and ₹ 80 lakhs
   - **d) ₹ 15 lakhs and ₹ 75 lakhs**
3. Total variable cost
   - a) ₹ 48 lakhs
   - **b) ₹ 45 lakhs**
   - c) ₹ 44 lakhs
   - d) ₹ 41 lakhs
4. Profit of the company
   - a) ₹ 8 lakhs
   - **b) ₹ 6 lakhs**
   - c) ₹ 5 lakhs
   - d) ₹ 4 lakhs

5. X Ltd., having a margin of safety of ₹ 8 lakh, makes a profit of ₹ 1,60,000. If its fixed cost is ₹ 10 lakh, what will be the break-even sales of X Ltd.?

   a) ₹ 25,00,000

   b) ₹ 50,00,000

   c) ₹ 20,00,000

   d) ₹ 10,00,000

6. From the given information, calculate profit: Sales – ₹ 2,00,000, Fixed Cost –₹ 40,000, BEP –₹ 1,60,000.

   a) ₹ 20,000

   b) ₹ 25,000

   c) ₹ 10,000

   d) ₹ 50,000

   A company prepares a budget for the production of 2,00,000 units. Variable cost per unit is ₹ 15, and the fixed cost is ₹ 2 per unit. The company fixes its selling price to fetch a profit of 10% on cost. On the basis of this information, answer questions 7 to 10.

7. Break-Even Point (both in units and ₹)

   a) 1,08,108 units and ₹ 20,21,622

   b) 1,05,100 units and ₹ 22,22,800

   c) 1,04,104 units and ₹ 21,21,400

   d) 1,06,108 units and ₹ 24,20,622

8. Profit volume ratio

   a) 21.78%

   b) 18.88%

   c) 21.35%

   d) 19.79%

9. If it reduces its selling price by 5%, what will be the break-even point (in units) and PV Ratio?

   a) 1,42,865 units and 14.65%

   b) 1,45,600 units and 15.50%

   c) 1,44,665 units and 15.65%

   d) 1,41,665 units and 18.68%

10. If a profit increase of 10% is desired more than the budget, what should be the sales at the reduced price?

    a) ₹ 45,72, 393

    b) ₹ 49,74, 293

    c) ₹ 54,84, 843

    d) ₹ 48,78, 448

Answer:

1. a
2. d
3. b
4. b
5. b
6. c
7. a
8. d
9. c
10. b

Fill in the Blanks:

1. Special order pricing is relevant when there is _____ capacity in production.
2. The make or buy decision involves considering _____ costs and opportunity costs.
3. Contribution is maximized by earning the highest _____ per unit of the limiting factor.
4. The _____ is used to determine which machine should be chosen.
5. The _____factor could be labour, material, or machine hours.

Answers

1. excess
2. marginal
3. Contribution
4. Cost indifference point
5. limiting

True and False

1. Where incremental costs of manufacture are less than those of buying in, the firm should make the product.
2. The appraisal of the various courses of action available is possible through the analysis of fixed costs.
3. If the selling price is above the marginal cost, it is preferable to shut down production because the losses are maximised.
4. It is assumed in limiting factor analysis that management would make a product mix decision or service mix decision based on the option that would maximise profit.
5. If the sales demand is limited, the profit-maximising decision will be to produce the top-ranked product(s) up to the sales demand limit.

Answer

1. True
2. False
3. False
4. True
5. True

CMA FINAL COURSE

Syllabus 2022

Topic

Module 5 : The Competition Act, 2002

FINAL

Group III - Paper-13

Corporate and Economic Laws (CEL)

Competition Act

Competition Act, 2002

- The Monopolies & Restrictive Trade Practices Act, 1969, is the first enactment to deal with competition issues and came into effect on 1st June 1970.
- The Government appointed a committee in October 1999 to examine the existing MRTP Act for shifting the focus of the law from curbing monopolies to promoting competition and to suggest a modern competition law. Pursuant to the recommendations of this committee, the Competition Act, 2002, was enacted on 13th January 2003. It was subsequently amended in 2007. The Act applies to the whole of India, including Jammu and Kashmir.
- It provides for different notifications for making different provisions of the Act effective, including the repeal of the MRTP Act and the dissolution of the MRTP Commission.

Objectives of the Act

The objectives of the Competition Act are to:

- prevent anti-competitive practices,
- promote and sustain competition,
- protect the interests of the consumers and
- ensure freedom of trade.
- Competition advocacy by creating awareness among various levels at the Government, industry and consumers.

Functions of the Competition Commission of India (CCI)

Being the regulator of the Act, CCI shall, inter alia, have the following functions.

i) CCI shall prohibit anti-competitive agreements, which determine prices, limit or control markets, bid rigging, etc.

ii) Regulate abuse of dominance and regulate combinations (merger or amalgamation or acquisition) which cause or likely cause an appreciable adverse effect or competition through a process of enquiry.

iii) It shall give an opinion on competition issues on a reference received from an authority established under any law (statutory authority)/Central Government.

iv) CCI is also to render competition advocacy, create public awareness, promote competition, protect the interests of consumers, ensure freedom of trade and impart training on competition issues.

v) Inquiry into certain agreements and dominant position by giving notices to the parties.

Prohibition of certain agreements

An agreement includes any arrangement, understanding or concerted action entered into between parties, and shall be presumed to be an anti-competitive agreement having appreciable adverse effects.

An anti-competitive agreement is an agreement having an appreciable adverse effect on competition. Anti-competitive agreements include:-

- agreement to limit production & supply, storage, distribution
- agreement to allocate markets
- agreement to fix prices
- bid rigging (manipulating the bids) or collusive bidding (bidding with understanding among the bidders)
- conditional purchase/sale (tie-in arrangement)
- exclusive supply/distribution arrangement-limit/ restrict/withhold/allocation of an area
- resale price maintenance
- refusal to deal/ tie up sales

Abuse of dominance

Dominance refers to a position of strength in a "relevant product market" which enables a dominant firm to operate independently in India of competitive forces or to affect its competitors, consumers, or the market in its favour.

- impedes fair competition between firms,
- exploits consumers and makes it difficult for the other players to compete with the dominant undertaking on merit.
- imposing unfair conditions or price, predatory pricing, limiting production/market, creating barriers to entry and applying dissimilar conditions to similar transactions.

Specific instances of dominance

(a) directly or indirectly, imposes unfair or discriminatory conditions in the purchase or sale of goods or services, including predatory pricing;

(b) limits, restricts production of goods/ provision of services/ technical development

(c) denial of market access

(d) uses dominant positioning in one market to enter into other relevant markets.

Orders the Commission can pass

- The Commission can grant interim relief restraining a party from continuing with an anti-competitive agreement or abuse of dominant position;
- Impose a penalty of not more than 10% of the turnover of the enterprises and in case of a cartel, 3 times the amount of profit made out of the cartel or 10% of the turnover of all the enterprises, whichever is higher;
    - The Commission may direct a delinquent enterprise to discontinue and not to re-enter an anti-competitive agreement or abuse the dominant position
    - To award compensation
- May be lenient in penalty, if any party gives true and vital information about the cartel;
- There may be a settlement of the penalty under certain conditions.
    - To modify the agreement.
    - To recommend to the Central Govt. for division of enterprise in case it enjoys a dominant position.
- Declare an agreement to be void.
- Violation of orders may result to imprisonment.

"Combination" under the Act and regulation thereof

The combination includes the acquisition of shares, the acquisition of control by the enterprise over another and the amalgamation between or amongst enterprises. Combination that exceeds the threshold limits specified in the Act in terms of assets or turnover, which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India, can be scrutinized by the Commission

In case of combination the threshold limits are-

- **For acquisition:** means acquiring shares/voting rights, directly or indirectly or control over mismanagement/ assets with or without agreement.
- **Individual:** Combined assets of the firms (acquirer and the enterprise) is more than ₹2000 Cr. or turnover is more than ₹ 6000 Cr. (these limits are US$ 1 billion, including at least ₹1000 Cr. in India and 3 billion, including at least 3000 cr. in India, in case one of the firms is situated outside India).
- **Group:** The limits are more than ₹8000 Cr or ₹24000 Cr and US$ 4 billion, including at least ₹1000 Cr in India and 12 billion, including at least ₹3000 Cr in India, in case the acquirer is a group in India or outside India, respectively.

Central Govt.(CG) has an exempted enterprise whose control, shares, voting rights or assets are being acquired has assets of value of not more than ₹350 Cr. and turnover of not more than ₹1000 Cr.

Deal Value Threshold: The value of the deal for acquisition that exceeds ₹2000 Cr., provided that the acquired company has substantial business in India.

For merger/amalgamation –

- The above limit will be valid for mergers also.

Asset means the written-down book value and shall include intellectual property.

A firm proposing to enter into a combination may, at its option, notify the Commission in the specified form disclosing the details of the proposed combination within 30 days of such proposal, i.e. approval of the board of directors or execution of the agreement or other document for acquisition. No combination shall come into effect until 210 days have passed from the day on which the notice has been given to the Commission or the Commission has given no objection, whichever is earlier.

Procedure for investigation of combinations

If the Commission is of the opinion that a combination is likely to cause or has caused an adverse effect on competition,

- It shall issue a notice to show cause to the parties as to why an investigation in respect of such a combination should not be conducted.
- On receipt of the response, if the Commission is of the prima facie opinion that the combination has or is likely to have an appreciable adverse effect on competition, it may direct publication of details inviting objections from the public and hear them, if considered appropriate.
- It may invite any person, likely to be affected by the combination, to file his objections. The Commission may also enquire whether the disclosure made in the notice is correct and the combination is likely to have an adverse effect on competition.

Orders the Commission can pass in case of combinations

- ➢ It shall approve the combination if no appreciable adverse effect on competition is found
- ➢ It shall disapprove of a combination in case it forms an opinion of appreciable adverse effect on competition
- ➢ May propose a suitable modification in the agreement/ arrangement.

Prohibition of abuse of dominance

i) an enterprise shall be considered to be dominant in the referent market in India, if -

   (a) operate independently of competitive forces;

   (b) affects the consumer, competitor or the relevant market in its favour.

ii) abuse of dominant position shall mean the use of unfair or discriminatory conditions in the purchase or sale or price of goods and services, or restricting the quality of production, services or scientific development to prejudice customers, denial of market access, supplementary obligations or predatory pricing.

Regulation of combinations

i) Persons proposing to enter into a combination shall give notice to the Commission within 30 days of approval of the proposal by the Board or execution of any agreement;

ii) no combination shall be effective before the lapse of 150 days of giving notice or getting approval of the Commission, whichever is earlier;

iii) do not apply to bank, FI, FII or venture capital fund. 7 days' notice needs to be given to the Commission.

Topic

Module 8: Portfolio Theory and Practice

FINAL

Group III - Paper-14

Strategic Financial Management (SFM)

Topic: Risks in Financial Market

- **Multiple Choice Questions**

1. Which of the following risks arises due to fluctuations in the prices of financial assets?

a) Credit Risk
b) Market Risk
c) Operational Risk
d) Liquidity Risk

Answer: b) Market Risk

2. Credit risk refers to the possibility that:

a) Interest rates may increase
b) Inflation may rise
c) A borrower may fail to meet contractual obligations
d) Market prices may fluctuate

Answer: c) A borrower may fail to meet contractual obligations

3. Liquidity risk is the risk that:

a) Securities cannot be sold quickly without a significant loss in value
b) Interest rates decline
c) Inflation falls below expectations
d) The company earns excessive profits

Answer: a) Securities cannot be sold quickly without a significant loss in value

4. Which of the following is an example of systematic risk?

a) Employees' strike in one company
b) Product recall by a company
c) Global recession
d) Fraud by an employee

Answer: c) Global recession

5. Unsystematic risk is also known as:

a) Market Risk
b) Non-diversifiable Risk
c) Company-specific Risk
d) Inflation Risk

Answer: c) Company-specific Risk

6. Which type of risk can be substantially reduced through diversification?

a) Interest Rate Risk
b) Inflation Risk
c) Unsystematic Risk
d) Systematic Risk

Answer: c) Unsystematic Risk

7. Which one of the following risks cannot be eliminated through diversification?

a) Operational Risk
b) Credit Risk
c) Systematic Risk
d) Liquidity Risk

Answer: c) Systematic Risk

8. Purchasing Power Risk arises primarily because:

a) Interest rates fluctuate
b) Inflation reduces the real value of money
c) Credit ratings decline
d) Exchange rates appreciate

Answer: b) Inflation reduces the real value of money

9. Interest Rate Risk mainly affects the value of:

a) Equity shares only
b) Fixed-income securities
c) Inventory
d) Goodwill

Answer: b) Fixed-income securities

10. Operational risk generally arises from:

a) Changes in market prices
b) Failure of internal processes, people, systems, or external events
c) Exchange rate fluctuations
d) Inflation

Answer: b) Failure of internal processes, people, systems, or external events

11. Which statistical measure is most commonly used to measure the total risk of an investment?

a) Mean
b) Standard Deviation
c) Median
d) Geometric Mean

Answer: b) Standard Deviation

12. Beta (β) measures:

a) Total risk
b) Systematic risk
c) Credit risk
d) Liquidity risk

Answer: b) Systematic risk

13. The formula for Beta (β) is:

a) Standard Deviation of Market Return/ Mean Market Return

b) Covariance between Security and Market Return/ Variance of Market Return

c) Variance of Market Return/Covariance between Security and Market Return

d) Mean Market Return/ Standard Deviation of Market Return

Answer: b) Covariance between Security and Market Return/ Variance of Market Return

14. The Coefficient of Variation (CV) is calculated as:

a) Standard Deviation × Mean

b) Mean ÷ Standard Deviation

c) Standard Deviation ÷ Mean

d) Variance ÷ Mean

Answer: c) Standard Deviation ÷ Mean

15. A Beta value greater than 1 indicates that the security is:

a) Less volatile than the market

b) Equally volatile as the market

c) More volatile than the market

d) Free from market risk

Answer: c) More volatile than the market

16. Which of the following is the most effective technique for reducing unsystematic risk?

a) Hedging

b) Diversification

c) Insurance

d) Asset securitisation

Answer: b) Diversification

17. Which financial derivative is commonly used to hedge interest rate risk?

a) Interest Rate Swap

b) Equity Share

c) Treasury Bill

d) Commercial Paper

Answer: a) Interest Rate Swap

18. Credit risk can be reduced by:

a) Increasing fixed costs

b) Conducting proper credit appraisal and obtaining collateral

c) Holding more cash

d) Purchasing more inventory

Answer: b) Conducting proper credit appraisal and obtaining collateral

19. Which of the following is an appropriate method for managing liquidity risk?

a) Maintaining adequate liquid assets

b) Increasing long-term debt only

c) Reducing equity capital

d) Purchasing speculative securities

Answer: a) Maintaining adequate liquid assets

20. Inflation risk may be managed by investing in:

a) Idle cash balances

b) Inflation-indexed securities and real assets

c) Non-interest-bearing deposits

d) Obsolete machinery

Answer: b) Inflation-indexed securities and real assets

- **Comprehensive Case Study on Risks in Financial Markets**

Globe Tech Industries Ltd. is a multinational corporation headquartered in Germany with manufacturing facilities in India, Vietnam, and Mexico. The company produces advanced industrial machinery and exports its products to more than 60 countries. Its operations involve international procurement, manufacturing, financing, and global distribution.

Recently, the management has observed several challenges affecting its business operations.

The company imports sophisticated electronic components from Japan and South Korea. During the year, sudden fluctuations in international prices of raw materials and changes in global demand caused significant variations in the prices of these components, resulting in higher production costs and reduced profit margins.

A large portion of Globe Tech's sales is made on credit to overseas distributors. Due to the economic slowdown in some importing countries, several customers delayed payments, while a few major distributors defaulted completely on their outstanding balances.

The company also maintains substantial investments in long-term government and corporate bonds. During the year, central banks across various countries increased policy interest rates to control inflation. Consequently, the market value of these bonds declined considerably.

Globe Tech retains significant cash in its foreign subsidiaries for operational purposes. However, persistent inflation in certain countries reduced the purchasing capacity of these cash balances, increasing operating expenses and reducing real profitability.

To finance a recent expansion project, the company borrowed funds at a floating interest rate linked to international benchmark rates. Over the past year,

benchmark rates increased substantially, leading to a sharp rise in borrowing costs and lower net earnings.

Although the company reported healthy profits, it experienced temporary cash shortages because large inventories remained unsold and trade receivables were not realized on time. Consequently, the company faced difficulties in meeting certain short-term payment obligations.

During the year, the company also suffered a major disruption when its Enterprise Resource Planning (ERP) system was affected by a cyberattack. The disruption delayed production schedules, interrupted customer deliveries, and resulted in additional expenditure on system restoration and cybersecurity enhancements.

At the same time, the global economy entered a recession due to geopolitical tensions and declining industrial demand. Stock markets declined sharply, commodity prices became highly volatile, and investor confidence weakened. Despite its efficient internal management, GlobeTech experienced a significant fall in its market valuation.

Finally, one of the company's manufacturing plants in Mexico experienced a labour strike due to local wage disputes. Production at that facility remained suspended for several weeks, although operations at the company's other plants continued normally.

Questions on the Case:

1. Identify the different types of risks faced by GlobeTech Industries Ltd. in each of the above situations.
2. Explain why each situation represents the identified risk.
3. Suggest one or two suitable risk mitigation techniques for each identified risk.

Answer:

Situation	Risk Identified	Possible Mitigation Techniques
Fluctuation in prices of imported electronic components and global demand	**Market Risk**	Use commodity derivatives or futures contracts, diversify suppliers, and enter into long-term procurement contracts.
Overseas customers are delaying or defaulting on payments	**Credit Risk**	Conduct rigorous credit assessment, obtain credit insurance, require collateral or letters of credit, and diversify the customer base.
Decline in bond values due to an increase in interest rates	**Interest Rate Risk**	Maintain a balanced portfolio, use interest rate swaps or futures, and adjust portfolio duration.
Inflation reduces the purchasing power of cash balances	**Purchasing Power (Inflation) Risk**	Invest surplus funds in inflation-indexed securities, periodically revise product prices, and reduce idle cash holdings.
Floating-rate borrowings are becoming more expensive.	**Interest Rate Risk**	Convert floating-rate debt into fixed-rate debt using interest rate swaps or refinance at fixed interest rates.
Cash shortage despite profits due to slow inventory turnover and delayed collections	**Liquidity Risk**	Improve working capital management, accelerate receivable collections, optimize inventory levels, and maintain adequate cash reserves or credit lines.
ERP system disruption caused by a cyberattack	**Operational Risk**	Strengthen internal controls, implement robust cybersecurity measures, maintain disaster recovery systems, and conduct regular employee training.
The global recession is affecting the company's market value	**Systematic Risk**	Diversification cannot eliminate this risk completely. Maintain diversified investments, stress-test business strategies, and strengthen financial resilience.
Labour strike at one manufacturing plant	**Unsystematic (Company-specific) Risk**	Develop contingency production plans, improve industrial relations, diversify manufacturing locations, and maintain business continuity plans.

Topic

Module 6: Different Aspects of Tax Planning

FINAL

Group III - Paper-15

Direct Tax Laws and International Taxation (DIT)

Tax Planning, Tax Evasion and Tax Avoidance

Tax planning is the legitimate and systematic structuring of a taxpayer's financial affairs—encompassing components like salary composition, property income, and investments—to minimize tax liability within the express framework of the law. Recognizing the complexity of modern tax legislation, involves making informed choices and exercising prudent judgment to utilize legally sanctioned exemptions, deductions and reliefs, without exploiting unintended legislative loopholes. Ultimately, it is a socially acceptable practice that aligns a taxpayer's financial goals with optimal tax efficiency, ensuring they pay the right amount of tax and no more.

Tax planning involves analyzing finances from a tax perspective to ensure maximum tax efficiency. It helps individuals and businesses to reduce tax liability and ensure that they contribute to the economy through legal means.

It is a way to reduce tax liability by taking full advantage of the provisions provided by the Act through various exemptions, deductions, rebates & relief. In other words, it is a way to reduce tax liability by applying the script & moral of the law. The two basic approaches of tax planning are:

1. **Reducing taxable income:** As a rule, the higher the income or profit, the higher the tax liability on such income or profit. Gross income is total profits or income from all sources, and taxable income is such gross income less adjustments allowable under various tax laws and other provisions. Such adjustments are based on the nature of income and expenditure. Opting for the income or expenditure heads that allow maximum setoffs from the gross income reduces taxable income, and by extension, tax liability.
2. **Deferring payment of taxes to the extent possible:** An underestimated dimension of tax planning is timing investments and financial transactions so that the tax liability for such transactions arises at the farthest possible time. While this does not reduce the amount of tax payable, it delays tax outgo, thereby effectively providing interest-free cash on hand. Individuals may not need to resort to such a strategy, but a delayed payout is valuable for small businesses that very often face cash flow difficulties.

The goal of tax planning is to arrange your financial affairs so as to minimize your taxes. It is the planning so as to attract minimum tax liability or postponement of tax liability for the subsequent period by availing various incentives, concessions, allowances, rebates and relief provided in the Act.

Objectives of Tax Planning

Tax planning is an exercise undertaken to minimize tax liability through the best use of all available allowances, deductions, exclusions, exemptions, etc. The objectives of tax planning cannot be regarded as offending any concept of the taxation laws and subjected to reprehension of reducing the inflow of revenue to the Government's coffer, so long as the measures are in conformity with the statute laws and the judicial expositions thereof. The basic objectives of tax planning are:

a. Reduction of Tax liability

Tax law provides multiple choices and options to taxpayers. This necessary offer of options within tax legislation creates the opportunity for choice on the part of the taxpayer. However, due to a lack of awareness of legal requirements, in many cases, a taxpayer may suffer heavy taxation. Through proper tax planning and awareness, a taxpayer may reduce such a heavy tax burden.

b. Minimisation of litigation

In the matter of taxation, the taxpayers will try to pay the least tax, and on the other hand, the tax administrator will attempt to extract the maximum. This conflicting behaviour may results into litigations. However, where proper tax planning is adopted by the tax payer in conformity with the provisions of the taxation laws, the incidence of litigation can be minimised. This saves him from the hardships and inconveniences caused by the unnecessary litigation.

c. Productive investment

A taxpayer may reduce a heavy tax burden through proper tax planning. Such a reduction results in a reduction in cash outflow. In the days of credit squeeze and dear money conditions, even a rupee of tax decently saved may be taken as an interest-free loan from the Government, which perhaps an assessee need not repay. Such retained cash can be utilised in other productive ventures, which also provide additional earnings to the taxpayer. That means, proper tax planning is a measure of proper utilisation of available resources, which in turn maximises the cash inflow and minimises the tax burden.

d. Healthy growth of the economy

The growth of a nation's economy is synonymous with the growth and prosperity of its citizens. In this context, a saving of earnings by legally sanctioned devices fosters the growth of both, because savings by dubious means lead to the generation of black money, the evils of which are obvious. Conversely, tax-planning measures are aimed at generating white money with a free flow and generation without reservations for the overall progress of the nation. Tax planning assumes great significance in this context.

e. Economic stability

Tax planning results in economic stability by way of:

(i) productive investments by the taxpayers; and

(ii) harnessing of resources for national projects aimed at the general prosperity of the national economy and reaping of benefits even by those not liable to pay tax on their incomes.

Essentials of Tax Planning

The following are the essentials of tax planning:

- Up-to-date Knowledge of tax laws along with circulars, notifications, clarifications and Administrative instructions issued by the CBDT.
- Disclosure of full and true material information
- Avoid sham transactions or make-believe transactions or colourable devices
- Foresight of future development or changes and the enterprise's goal.

Types of Tax Planning

The tax planning exercise ranges from devising a model for specific transaction as well as for systematic corporate planning. These are:

(a) Short-range tax planning: Short-range planning refers to planning to achieve some specific or limited objective of a particular fiscal year. E.g., an individual assessee whose income is likely to register unusual growth in a particular year as compared to the preceding year, may plan to subscribe to the PPF/NSCs within the prescribed limits in order to enjoy substantive tax relief. By investing in such a way, he is not making a permanent commitment but is substantially saving in taxes.

(b) Long-range tax planning: Long-range planning, on the other hand, involves entering into activities that may not pay off immediately. E.g., when an assessee transfers his equity shares to his minor son, he knows that the Income from the shares will be clubbed with his own income. But clubbing would also cease after his son attains majority.

Ethical way of reducing tax

Tax planning is an art of logically planning one's financial affairs, in such a manner that benefit of all eligible provisions of the taxation law can be availed effectively so as to reduce or defer tax liability. As tax planning follows an honest approach, by conforming to those provisions which fall within the framework of the taxation law. However, many time in the name of planning, assessee misleads the law, with / without making an offence. And to do so, the taxpayer uses any scheme or arrangement, which reduces, defers and even completely prevents the payment of tax. This may also be done by shifting tax liability to another person, so as to minimise the incidence of tax.

Tax evasion is the illegal way to reduce tax liability by deliberately suppressing income or sales or by increasing expenses, etc., which results in a reduction of the total income of the assessee. Dishonest taxpayers try to reduce their taxes by concealing income, inflation of expenses, submitting misleading information, falsification of accounts and willful violation of the provisions of the Income-tax Act. Such unethical practices often create problems for tax evaders. The tax department not only imposes huge penalties but also initiates prosecution in such cases. It is illegal, both in script & moral. It is the cancer of modern society and work as a clog in the development of the nation. It is a grave problem in a developing country like ours, as it leads to the creation of a 'resource crunch' for developmental activities of the State.

Tax avoidance is an exercise by which the assessee legally takes advantage, with a malicious motive, of loopholes in the Act. Tax avoidance is minimising the incidence of tax by adjusting the affairs in such a manner that, although it is within the four corners of the law, it is done with a purpose to defraud the revenue. It is a practice of dodging or bending the law without breaking it. It is a way to reduce tax liability by applying the script of law only. E.g. if A gives a gift to his wife, the income from the asset gifted will be clubbed in the hands of A. But to avoid this clubbing provision, "A" decides to give a gift to B's wife and B reciprocates it by giving a gift to A's wife. This is not tax planning but tax avoidance. Most of the amendments are aimed at curbing such loopholes.

The Direct Taxes Enquiry Committee (Wanchoo Committee) has tried to draw a distinction between the two items in the following words.

"The distinction between 'evasion' and 'avoidance', therefore, is largely dependent on the difference in methods of escape resorted to. Some are instances of merely availing, strictly in accordance with law, the tax exemptions or tax privileges offered by the government. Others are manoeuvres involving an element of deceit, misrepresentation of facts, falsification of accounting calculations or downright fraud. The first represents what is truly tax planning, the latter tax evasion. However, between these two extremes, there lies a vast domain for selecting a variety of methods which, though technically satisfying the requirements of law, in fact circumvent it with a view to eliminating or reducing tax burden. It is these methods which constitute "tax avoidance".

The Royal Commission on Taxation for Canada has explained the concept of tax avoidance as under:

"Tax Avoidance" will be used to describe every attempt by legal means to prevent or reduce tax liability which would otherwise be incurred, by taking advantage of some provisions or lack of provisions of law. It excludes fraud, concealment or other illegal measures.

Distinguish between Tax Planning, Tax Evasion, Tax Avoidance and Tax Management

Points of distinction	Tax planning	Tax Avoidance	Tax Evasion	Tax Management
Definition	It is a way to reduce tax liability by taking full advantages provided by the Act through various exemptions, deductions, rebates & relief.	It is an exercise by which the assessee legally takes advantage of the loopholes in the Act.	It is an illegal way to reduce tax liability by deliberately suppressing income or sales or by increasing expenses, etc., which results in a reduction of the total income of the assessee.	It is a procedure to comply with the law's provisions.
Feature	Tax planning is the practice of following the provisions of law within a moral framework.	Tax avoidance is a practice of bending the law without breaking it.	Tax evasion is illegal, both in script & moral.	It is the implementation or execution part of the taxation department of an organisation.
Object	To reduce tax liability by applying script & moral of law.	To reduce the tax liability to the minimum by applying script of law only	To reduce tax liability by applying unfair means.	To comply with the provisions of laws.
Approach	It is futuristic and positive in nature. The plan is made today to avail the benefits in future.	It is futuristic but short term in nature, as loophole of the law will be corrected in future by amendments of the law.	It is concerned with past and applied after the liability of tax has arisen. It is done with negative approach to avail benefits by killing the moral of law.	It is a continuous approach, which is concerned with past (rectification, revisions etc.), present (filing of return, etc.) & future (corrective action).
Benefit	Generally, arises in the long run.	Generally, arises in the short run.	Generally, benefits do not arise, but it causes penalty and prosecution.	Penalty, interest & prosecution can be avoided.
Treatment of Law	It uses the benefits of the law.	It uses loopholes in the law.	It overrules the law.	It implements the law.
Practice	It is tax-saving.	It is tax hedging.	It is tax concealment.	It is tax administration.
Need	It is desirable	It is avoidable	It is objectionable	It is essential.
Morality	It is moral in nature.	It is immoral in nature	It is illegal.	It is duty.

GAAR

To curb aggressive tax avoidance, Chapter X-A of the Income Tax Act, 1961, provides the General Anti-Avoidance Rules (GAAR), granting revenue authorities the statutory power to declare any transaction as an 'Impermissible Avoidance Arrangement' (IAA). An arrangement is classified as an IAA u/s 96 if its primary purpose is to obtain a tax benefit and it concurrently lacks commercial substance (Sec. 97), creates non-arm's length rights, abuses the provisions of the Act, or is executed in a manner not ordinarily employed for bona fide purposes.

Conclusion

Ultimately, tax planning is a dynamic and continuous discipline that demands a proactive alignment of financial strategies with the ever-evolving statutory landscape. While tax evasion and avoidance represent legal and ethical breaches that invite severe penal and prosecutorial consequences, legitimate tax planning empowers taxpayers to optimize their wealth and maintain long-term financial stability. For aspiring professionals, mastering the subtle demarcation among planning, management, avoidance, and evasion is not merely an academic requirement, but a foundational skill essential for delivering robust, compliant, and value-driven advisory services in today's complex economic environment.

Topic

Module 2: Quality Cost Management

FINAL

Group III - Paper-16

Strategic Cost Management (SCM)

Quality Cost Management

1. Introduction

Quality is no longer treated as a purely technical or production-floor matter — it is a strategic cost variable. Every rupee spent on preventing a defect, inspecting a product, or fixing a failure is a cost that flows straight into the organisation's profitability. Quality Cost Management (QCM) is the discipline of identifying, measuring, analysing, and controlling these costs so that a firm achieves the "right" level of quality at the lowest total cost — not the highest possible quality at any cost, and not the cheapest process regardless of defects.

The central idea examiners test again and again is this: **quality costs are not just the cost of making a product well — they are the cost of the gap between actual quality and the quality the customer expects**. Every cost incurred because a product could fail, or did fail, is a quality cost.

2. Definition of Cost of Quality (COQ)

Cost of Quality is the total cost incurred by an organisation in ensuring that a product/service conforms to specified quality standards, plus the cost incurred when it fails to do so.

COQ = Cost of Conformance + Cost of Non-Conformance

- **Cost of Conformance (COC):** money spent to make sure things go right (prevention + appraisal).
- **Cost of Non-Conformance (CONC):** money lost because things went wrong (internal + external failure).

This conformance/non-conformance split is the modern restatement of the classical four-way PAF classification discussed below:

3. The PAF Model — Four Categories of Quality Cost

The **PAF (Prevention–Appraisal–Failure) model**, originally formalised by Armand Feigenbaum, is a fundamental framework for understanding the different components of Quality Costs. It classifies quality-related costs into four categories: **Prevention, Appraisal, Internal Failure, and External Failure**.

3.1 Prevention Costs

Prevention costs are incurred to avoid defects before they occur. These costs are generally incurred during the planning, design, and preparation stages, before production or service delivery begins.

Examples:

- Quality planning and quality engineering
- Design reviews and new-product quality reviews
- Supplier evaluation and vendor quality assurance
- Employee training in quality techniques
- Quality circles and process capability studies
- Preventive maintenance of machinery
- Designing and implementing Statistical Process Control (SPC) systems

3.2 Appraisal Costs

Appraisal costs are incurred to detect and identify defects and to verify that products or services conform to established quality standards. These activities typically take place during or after production, but before the defective product reaches the customer.

Examples:

- Inspection of incoming materials
- In-process and final inspection and testing
- Calibration of measuring and testing equipment
- Quality audits
- Sample testing and field testing

3.3 Internal Failure Costs

Internal failure costs arise when a defect is identified before the product or service reaches the customer. These costs result from correcting or managing problems within the organisation.

Examples:

- Scrap and spoilage
- Rework and repair
- Re-inspection and re-testing after rework
- Production downtime caused by quality problems
- Disposition costs for defective batches
- Failure analysis to identify the root cause of defects

3.4 External Failure Costs

External failure costs occur when a defect is discovered after the product or service has reached the customer. These are generally the most costly and damaging quality costs, as they can affect both profitability and the organisation's reputation.

Examples:

- Warranty claims and product replacements
- Investigation and handling of customer complaints
- Product recalls
- Liability claims and litigation
- Loss of customer goodwill and future sales
- Product returns and allowances

In simple terms:

Prevention - Stop defects from occurring

Appraisal - Detect defects before delivery

Internal Failure - Correct defects before the customer receives them

External Failure - Deal with defects after the customer receives them

4. The Quality Cost Curve - Traditional vs Modern View

The Quality Cost Curve explains the relationship between expenditure on quality activities and the resulting costs of failure. Two major approaches are commonly discussed: the Traditional Trade-off View and the Modern Zero-Defects View.

4.1 Traditional (Trade-off) View

The traditional approach assumes that prevention and appraisal costs increase as failure costs decrease. According to this view, an organisation should spend on quality only up to the point where the total Cost of Quality (COQ) is at its minimum.

This produces a U-shaped total quality cost curve:

- At low levels of prevention and appraisal, failure costs are high.
- As prevention and appraisal activities increase, failure costs decline.
- Beyond a certain point, additional spending on prevention and appraisal was believed to cost more than the failure costs it could save.
- Therefore, the traditional approach identifies an "economic" or "optimal" level of quality, rather than aiming for complete conformance.

In this view, 100% conformance was considered economically impractical, because the marginal cost of achieving further quality improvement was assumed to exceed the marginal reduction in failure costs.

4.2 Modern (Zero-Defects) View

The modern approach, strongly associated with Philip Crosby's "Quality is Free" philosophy and Japanese Total Quality Management (TQM) practices, challenges the traditional U-shaped curve.

The modern view argues that poor quality is more expensive than preventing poor quality.

Key points include:

- Investment in prevention can generate increasing returns, because the actual cost of failures—particularly hidden external failure costs—is often much greater than what organisations initially measure.
- As prevention improves conformance, failure costs fall significantly, causing total COQ to continue declining even at very high levels of quality.
- The objective should therefore be to move towards 100% conformance or zero defects, rather than accepting a predetermined "economic" defect rate.
- The modern quality cost curve is therefore generally represented as continuously declining, rather than U-shaped.

Key Shift in Thinking

Traditional view:

Quality has a cost, so an economically optimal defect level exists.

Modern view:

Quality itself is not the problem; poor quality is the real cost.

Thus, the central shift is from "quality costs money" to "quality is free (poor quality costs money." This transition from an economic level of quality to a zero-defects philosophy

5. The Iceberg / Multiplier Effect — Hidden Quality Costs

The Iceberg Effect highlights an important problem in Quality Cost Management: only a small portion of the total cost of poor quality is visible in accounting records. Like an iceberg, the costs that can be easily measured are only the tip, while a much larger portion remains hidden beneath the surface.

Visible Quality Costs

These are the costs that are directly recorded and relatively easy to measure, such as:

- Scrap and material wastage
- Rework and repairs
- Warranty claims
- Product returns
- Replacement costs

Hidden Quality Costs

Beneath these visible costs, there are several indirect costs that may be difficult to identify or quantify:

- Loss of customer goodwill and future orders
- Loss of market share
- Additional inventory maintained as a buffer against quality failures
- Management and engineering time spent solving recurring quality problems

- Reduced employee morale and productivity
- Opportunity cost of production capacity lost to rework and repairs

Multiplier Effect

The Multiplier Effect suggests that the actual cost of quality failures can be several times higher than the costs recorded in the accounting system. A commonly cited estimate is that the true failure cost may be around 3–4 times the measured cost when hidden costs are taken into account.

For example, if a company records ₹1 lakh as the direct cost of quality failures, the actual economic impact could potentially be ₹3–4 lakh or more after considering lost customers, management time, excess inventory, and other hidden effects.

The Iceberg Effect explains why external failure costs are strategically significant. Although they are often the most difficult to measure, they can create substantial long-term damage through lost customers, reputation, market share, and future revenue.

6. Allied Quality Management Concepts

6.1 Total Quality Management (TQM)

Total Quality Management (TQM) is an organisation-wide approach that focuses on continuous improvement, customer satisfaction, employee involvement, and effective process management. Its ultimate aim is to achieve consistently high quality and move towards zero defects.

Key pillars of TQM:

- **Customer focus –** understanding and meeting customer needs and expectations.
- **Continuous improvement (Kaizen) –** constantly improving processes, products, and services.
- **Employee involvement and empowerment –** encouraging employees to participate in quality improvement.
- **Fact-based decision making –** using data and evidence rather than assumptions.
- **Process approach –** managing and improving the processes that produce products and services.

6.2 Kaizen Costing

Kaizen Costing refers to the practice of achieving continuous, incremental cost reduction during the manufacturing stage of a product's life cycle.

Unlike Target Costing, which primarily operates during the design and development stage, Kaizen Costing focuses on reducing costs after production has begun.

Small teams and quality circles identify and implement frequent, incremental improvements that gradually reduce:

- Production costs
- Defects and waste
- Process inefficiencies
- Rework and failure costs

The underlying principle is that many small improvements can collectively produce significant cost and quality benefits.

6.3 Six Sigma

Six Sigma is a data-driven and statistical approach to process improvement that aims to reduce variation and achieve near-zero defects. A Six Sigma process is commonly associated with approximately 3.4 defects per million opportunities (DPMO).

DMAIC is used to improve existing processes:

D – Define → M – Measure → A – Analyse → I – Improve → C – Control

For designing new processes, **DMADV/DFSS** is commonly used:

D – Define → M – Measure → A – Analyse → D – Design → V – Verify

7. Strategic Significance of Quality Cost Management

Quality Cost Management is not limited to the quality department; it supports important strategic and managerial decisions across the organisation.

7.1 Pricing Decisions

A firm with a lower Cost of Quality (COQ), particularly lower failure costs, can operate more efficiently. This may allow it to offer competitive prices while maintaining profit margins.

7.2 Make-or-Buy Decisions

When comparing internal production with external suppliers, managers should consider total quality-related costs, rather than simply comparing purchase prices.

Supplier-related costs such as:

- Incoming inspection
- Rejection and returns
- Rework
- Supplier-related delays
- Quality-related disruption

should be included to obtain a true make-or-buy comparison.

7.3 Investment Appraisal

Investments in quality improvement—such as employee training, better inspection technology, automation, or process improvements—should be evaluated based on the failure costs they are expected to prevent or reduce, rather than merely looking at the immediate expenditure.

7.4 Balanced Scorecard Linkage

Quality-related measures can be integrated into the Balanced Scorecard, particularly within the:

- **Internal Business Process Perspective** – defect rates, rework, process capability, cycle time, etc.
- **Customer Perspective** – complaints, returns, customer satisfaction, retention, and loyalty.

This connects Quality Cost Management directly with strategic performance measurement, demonstrating that quality is not merely an operational issue but a major contributor to overall business performance.

Problem 1 — Preparation of Cost of Quality Report

The following information has been extracted from the cost records of Nova Appliances Ltd. for the year ended 31 March 2026. The company reported sales of ₹5,00,00,000 during the year.

Particulars	Amount (₹)
Product design review	4,00,000
Supplier quality assessment	2,20,000
Quality improvement training	2,00,000
Inspection of incoming materials	3,00,000
Finished product testing	4,50,000
Rework of defective products before dispatch	6,00,000
Scrap due to manufacturing defects	3,50,000
Warranty claims and repairs	7,00,000
Customer complaint handling	1,80,000
Product recall expenses	2,50,000

Required:

1. Classify the above costs under the four categories of Cost of Quality (COQ):
   - o Prevention Costs
   - o Appraisal Costs
   - o Internal Failure Costs
   - o External Failure Costs
2. Prepare a Cost of Quality Statement, showing:
   - o Total cost under each category
   - o Cost of Conformance
   - o Cost of Non-Conformance
   - o Total Cost of Quality
   - o Each category as a percentage of sales
3. Briefly comment on the company's quality cost profile.

Solution

1. Classification of Costs

Category	Particulars	Amount (₹)
Prevention	Product design review	4,00,000
Prevention	Supplier quality assessment	2,20,000
Prevention	Quality improvement training	2,00,000
Prevention Total		**8,20,000**
Appraisal	Inspection of incoming materials	3,00,000
Appraisal	Finished product testing	4,50,000
Appraisal Total		**7,50,000**
Internal Failure	Rework of defective products before dispatch	6,00,000
Internal Failure	Scrap due to manufacturing defects	3,50,000
Internal Failure Total		**9,50,000**
External Failure	Warranty claims and repairs	7,00,000
External Failure	Customer complaint handling	1,80,000
External Failure	Product recall expenses	2,50,000
External Failure Total		**11,30,000**

2. Cost of Quality Statement

Sales = ₹5,00,00,000

Category	Amount (₹)	% of Sales
Prevention Costs	8,20,000	1.64%
Appraisal Costs	7,50,000	1.50%
Total Cost of Conformance	15,70,000	3.14%
Internal Failure Costs	9,50,000	1.90%
External Failure Costs	11,30,000	2.26%
Total Cost of Non-Conformance	20,80,000	4.16%
Total Cost of Quality	36,50,000	7.30%

3. Comment on Quality Cost Profile

The company's Total Cost of Quality is ₹36.50 lakh, representing 7.30% of sales. The Cost of Non-Conformance is ₹20.80 lakh (4.16% of sales), which is considerably higher than the Cost of Conformance of ₹15.70 lakh (3.14% of sales).

External failure costs are the highest individual category at ₹11.30 lakh, indicating that a significant portion of quality problems is reaching customers. The company may therefore benefit from greater emphasis on prevention activities such as design review, supplier quality assessment and employee training, which could help reduce rework, scrap, warranty claims and product recalls.

Conclusion: The quality cost profile suggests that the company has scope to strengthen preventive quality measures in order to reduce its relatively high failure costs.

Topic

Module 10: Management Reporting Issues and Analysis

Module 15: Operational Audit and Internal Audit under Companies Act, 2013

FINAL

Group IV - Paper-17

Cost and Management Audit (CMAD)

Management Reporting Issues and Analysis

Management reporting is the systematic process of collecting, analysing, and presenting financial and non-financial information to management for planning, controlling, decision-making, and performance evaluation. Effective management reports enable executives to identify shortcomings in operational areas, monitor strategic objectives, and take necessary corrective actions promptly.

Major Management Reporting Issues

1. Data Accuracy and Reliability

Management decisions are only as good as the information on which they are based. Inaccurate, incomplete, or inconsistent data may lead to poor strategic and operational decisions. Attention needs to be drawn towards -

- Lapses in standardized data collection process
- Errors in manual data entry
- Availability of multiple versions of the same data
- Weak internal controls over information systems

2. Timeliness of Reporting

Delayed reports reduce their usefulness in decision-making. Rapidly changing business environments require real-time or near-real-time information for analysis and effective recommendations. To ensure the timeliness of reporting for early decision-making, the following shortcomings need to be resolved.

- Delay in consolidation of financial data
- Inefficient reporting processes
- Hybrid (manual and electronic) process of data analysis and collation
- Inadequate ERP integration

3. Information Overload

Management reports often contain excessive information, making it difficult to identify critical business issues in accomplishing specific goals. Brevity and clarity of expression in reports with appropriate data support and report layout (seriatim of importance with respect to performance indicators) are the prerequisites for a management audit report. Decision-makers spend more time interpreting reports than taking action; hence, the following factors are avoidable.

- Considering too many performance indicators simultaneously in one report
- Lack of prioritisation
- Poor report design/layout

4. Lack of Relevant Key Performance Indicators (KPIs)

Reports should focus on performance measures aligned with organizational objectives. The deviations and suggestions for improvement will only be fruitful to the decision makers when the following aspects are taken care of. Frequent shifting of KPIs, merging/demerging of objectives related to KPIs, misalignment, etc., can't deliver the desired outcome.

- Relevance of metrics
- Proper linkage with strategic goals
- Monitoring operational risks

5. Inadequate Risk Reporting

Organizations increasingly require integrated reporting on strategic, operational, financial, compliance, and cybersecurity risks.

- Risk information not linked with business objectives.
- Emerging risks are not reported in a timely manner.
- Weak coordination between risk management and reporting functions.

6. Poor Visualization

Complex reports with lengthy tables reduce readability.

- Limited use of dashboards.
- Absence of graphs and trend analysis.
- Difficult comparison across reporting periods.

7. Lack of Predictive Analytics

Traditional reports are historical and fail to support future planning.

- Minimal use of forecasting.
- Limited scenario analysis.
- No predictive modelling using data analytics.

8. Weak Accountability

Reports should clearly assign responsibility for achieving targets.

- Undefined ownership.
- No follow-up mechanism.
- Absence of variance analysis.

9. Integration Challenges

Organizations use multiple software platforms, resulting in fragmented information.

- Data silos.

- Lack of common databases.
- Manual reconciliation.

10. Regulatory Compliance

Management reports should also support statutory compliance and governance.

- ESG reporting
- Business Responsibility and Sustainability Reporting (BRSR)
- Internal financial controls
- Related party transaction monitoring

11. Timeliness of reporting

Time is the essence for reporting. Delayed reporting on urgent management issues may put management totally unguarded for the huge consequences.

Best Practices in Management Reporting

- Develop standardized reporting templates
- Focus on strategic KPIs
- Implement ERP and Business Intelligence tools
- Use dashboards and visualization
- Incorporate risk indicators
- Ensure data governance
- Conduct regular variance analysis against each KPI
- Automate report generation
- Include predictive analytics
- 'Root cause' analysis before initiating corrective action
- Periodically review reporting requirements

Operation Audit and Internal Audit under Companies Act 2013

Meaning of Operational Audit

Operational Audit is a systematic and independent evaluation of an organization's operations to assess economy, efficiency, effectiveness (3E) and compliance. Unlike a financial audit, it focuses on improving business processes and operational performance.

Objectives

- Improve operational efficiency
- Evaluate internal controls
- Optimize resource utilization
- Reduce operational risks
- Improve productivity
- Ensure compliance with policies
- Recommend process improvements
- Enhance organizational performance

Scope

Operational audit may cover:

- Procurement
- Production
- Inventory Management
- Human Resources
- Sales and Marketing
- Logistics
- Information Technology
- Customer Service
- Project Management
- Supply Chain Management

Characteristics

- Future-oriented
- Improvement-focused
- Independent evaluation by experts
- Performance measurement against definitive yardstick
- Risk-based approach towards operational issues
- Covers both financial and non-financial aspects
- Continuous improvement orientation

Operational Audit Process

1. Planning
2. Understanding business processes
3. Risk assessment
4. Internal control evaluation
5. Fieldwork
6. Data analysis
7. Identification of inefficiencies
8. Recommendations
9. Reporting
10. Follow-up review

Performance Evaluation Criteria (3Es)

Economy

Acquiring resources at the lowest reasonable cost without compromising quality.

Efficiency

Maximum output from available resources, which in turn reduces product/service cost.

Effectiveness

Achievement of organizational objectives and desired outcomes.

Advantages

- Reduces operational costs
- Improves productivity
- Strengthens internal controls
- Enhances governance
- Improves customer satisfaction
- Supports strategic decision-making
- Encourages continuous improvement

Limitations

- Recommendations may face resistance (resistance to change)
- Benefits may be difficult to quantify
- Requires experienced auditors
- Time-consuming and detailed work
- Scope may be extensive

Internal Audit under the Companies Act, 2013

Internal Audit is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations by evaluating risk management, governance, and internal control processes.

Statutory Provisions

Snapshot on statutory requirements under Companies Act 2013.

In view of the above requirements, importance of Internal Audit is increasing gradually. The requirement for internal audit is prescribed under:

- Section 138 of the Companies Act, 2013
- Rule 13 of the Companies (Accounts) Rules, 2014

These provisions empower the Central Government to prescribe classes of companies that must appoint an internal auditor.

Applicability (Rule 13)

Internal audit is mandatory for specified classes of companies, including certain:

Listed Companies

- Every listed company

Unlisted Public Companies

Meeting prescribed thresholds relating to:

- Paid-up share capital
- Turnover
- Outstanding loans or borrowings
- Outstanding deposits

Private Companies

Meeting prescribed thresholds based on:

- Turnover
- Outstanding loans or borrowings from banks or public financial institutions

Internal Auditor

The internal auditor may be:

- Chartered Accountant (CA)
- Cost Accountant (CMA)
- Any other professional as decided by the Board possessing the required expertise.

The internal auditor may be either:

- An employee, or
- An external professional

Appointment

- Appointed by the Board of Directors
- Terms of appointment determined by the Board
- Scope approved by the Audit Committee or the Board, as applicable

Scope of Internal Audit

Internal audit generally covers:

- Internal financial controls
- Risk management
- Corporate governance
- Compliance with laws
- Operational efficiency
- Asset protection
- Fraud prevention
- Information technology controls
- ESG and sustainability governance (where applicable)
- Cybersecurity governance

Role of Internal Auditor

- Evaluate internal control systems
- Assess risk management processes
- Detect control weaknesses
- Review operational efficiency
- Verify regulatory compliance
- Recommend improvements
- Assist the Audit Committee
- Strengthen governance practices

Relationship with the Audit Committee

Under Section 177 of the Companies Act, 2013, the Audit Committee oversees the internal audit function in applicable companies by:

- Reviewing internal audit reports
- Monitoring corrective actions
- Evaluating internal control effectiveness
- Reviewing risk management processes
- Coordinating with statutory auditors

Difference between Operational Audit and Internal Audit

Criterion	Audit Type	
	Operational	Internal
Objective	Improve operational efficiency	Evaluate internal controls, governance, and risk management
Coverage	Specific business operations or functions	Entire organization
Focus	Economy, Efficiency, Effectiveness (3Es)	Risk, Control, Compliance, Governance
Nature	Performance-oriented	Assurance and consulting
Frequency	As required	Periodic and continuous
Reporting	Functional management	Audit Committee/ Board and Management
Legal Requirement	Not specifically mandated by the Companies Act	Mandatory for prescribed companies under Section 138

Conclusion

Management reporting, operational audit, and internal audit are complementary components of a robust governance framework. High-quality management reporting provides timely and reliable information for decision-making, operational audit enhances efficiency and effectiveness through process improvements, and internal audit—mandated for specified companies under Section 138 of the Companies Act, 2013—provides independent assurance on governance, risk management, and internal controls. Together, these mechanisms strengthen accountability, improve organizational performance, support regulatory compliance, and contribute to long-term sustainable value creation.

Topic

Module 3: Accounting of Financial Instruments

FINAL

Group IV - Paper-18

Corporate Financial Reporting (CFR)

Topic: Financial Instruments

- **Multiple Choice Questions**

1. The primary objective of Ind AS 109 is to prescribe principles for:
   a) Presentation of financial statements
   b) Recognition and measurement of financial instruments
   c) Revenue recognition
   d) Accounting for leases

   Answer: b) Recognition and measurement of financial instruments

2. A financial asset is initially recognized when the entity:
   a) Signs the annual report
   b) Becomes a party to the contractual provisions of the instrument
   c) Receives cash
   d) Issues financial statements

   Answer: b) Becomes a party to the contractual provisions of the instrument

3. Which of the following is NOT a category for classifying financial assets under Ind AS 109?
   a) Amortised Cost
   b) Fair Value through Other Comprehensive Income (FVOCI)
   c) Fair Value through Profit or Loss (FVTPL)
   d) Historical Cost

   Answer: d) Historical Cost

4. The classification of a financial asset under Ind AS 109 depends primarily on:
   a) Size of the entity
   b) Business model and contractual cash flow characteristics
   c) Age of the asset
   d) Market capitalization

   Answer: b) Business model and contractual cash flow characteristics

5. The SPPI test under Ind AS 109 stands for:
   a) Standard Payments and Principal Investments
   b) Solely Payments of Principal and Interest
   c) Simple Principal Payment Instrument
   d) Standard Principal and Interest

   Answer: b) Solely Payments of Principal and Interest

6. A debt instrument held solely to collect contractual cash flows that satisfy the SPPI criterion is measured at:
   a) Fair Value through Profit or Loss
   b) Amortised Cost
   c) Replacement Cost
   d) Fair Value through Equity

   Answer: b) Amortised Cost

7. Investments in equity instruments are generally measured at:
   a) Historical Cost
   b) Amortised Cost
   c) Fair Value
   d) Net Realisable Value

   Answer: c) Fair Value

8. For equity investments not held for trading, an entity may irrevocably elect to present changes in fair value in:
   a) Retained Earnings
   b) Statement of Changes in Equity only
   c) Other Comprehensive Income
   d) Cash Flow Statement

   Answer: c) Other Comprehensive Income

9. Which financial assets are measured at Fair Value through Profit or Loss (FVTPL)?
   a) Assets failing the SPPI test
   b) Cash in hand
   c) Trade receivables without financing component
   d) Security deposits

   Answer: a) Assets failing the SPPI test

10. The impairment model prescribed by Ind AS 109 is based on:
    a) Incurred Loss Model
    b) Expected Credit Loss Model

c) Replacement Cost Model

d) Historical Loss Model

Answer: b) Expected Credit Loss Model

11. Which of the following is recognized even before an actual default occurs?

a) Realized Gain

b) Expected Credit Loss

c) Extraordinary Loss

d) Capital Loss

Answer: b) Expected Credit Loss

12. Which approach is generally applied for trade receivables without a significant financing component?

a) General Approach

b) Simplified Approach

c) Fair Value Approach

d) Cost Recovery Approach

Answer: b) Simplified Approach

13. Derecognition of a financial asset occurs when:

a) The asset becomes old

b) Contractual rights to cash flows expire or are transferred

c) Depreciation is charged

d) Dividend is received

Answer: b) Contractual rights to cash flows expire or are transferred

14. Which of the following is a financial liability?

a) Inventory

b) Trade Payables

c) Prepaid Expenses

d) Goodwill

Answer: b) Trade Payables

15. Financial liabilities are generally measured subsequently at:

a) Replacement Cost

b) Amortised Cost

c) Historical Cost

d) Net Realisable Value

Answer: b) Amortised Cost

16. Which of the following is measured at Fair Value through Profit or Loss?

a) Trading liabilities

b) Trade creditors

c) Long-term borrowings

d) Debentures held to maturity

Answer: a) Trading liabilities

17. Hedge accounting is primarily intended to:

a) Increase taxable income

b) Match gains and losses of hedging instruments with hedged items

c) Reduce depreciation

d) Increase dividend distribution

Answer: b) Match gains and losses of hedging instruments with hedged items

18. Which of the following is NOT one of the hedge accounting relationships under Ind AS 109?

a) Fair Value Hedge

b) Cash Flow Hedge

c) Hedge of Net Investment in a Foreign Operation

d) Inventory Hedge

Answer: d) Inventory Hedge

19. A derivative instrument is generally classified and measured at:

a) Amortised Cost

b) Historical Cost

c) Fair Value through Profit or Loss

d) Net Realisable Value

Answer: c) Fair Value through Profit or Loss

20. Which statement best describes the Expected Credit Loss (ECL) model?

a) Losses are recognized only after default occurs.

b) Credit losses are recognized on a forward-looking basis using expected losses.

c) Impairment is recognized only when approved by auditors.

d) Losses are recognized only at maturity of the financial asset.

Answer: b) Credit losses are recognized on a forward-looking basis using expected losses.

21. Under Ind AS 109, reclassification of financial assets is permitted only when:

    a) The fair value of the asset changes significantly

    b) The entity changes its accounting policy

    c) The entity changes its business model for managing financial assets

    d) The auditor recommends reclassification

    Answer: c) The entity changes its business model for managing financial assets

22. Which of the following financial assets generally does not satisfy the SPPI (Solely Payments of Principal and Interest) criterion?

    a) A fixed-rate bond

    b) A variable-rate loan linked to a market interest rate

    c) An investment in equity shares

    d) A term loan repayable with interest

    Answer: c) An investment in equity shares

23. Which of the following is NOT considered a financial instrument under Ind AS 109?

    a) Trade receivables

    b) Bank overdraft

    c) Advance payment made to a supplier for purchase of inventory

    d) Corporate bonds

    Answer: c) Advance payment made to a supplier for purchase of inventory

    Explanation: An advance to a supplier creates a contractual right to receive goods or services rather than cash or another financial asset. Therefore, it is not a financial instrument.

24. Which of the following statements regarding transaction costs is correct under Ind AS 109?

    a) Transaction costs are always charged to the Statement of Profit and Loss.

    b) Transaction costs are added to the initial carrying amount of financial assets measured at Amortised Cost or FVOCI.

    c) Transaction costs are ignored in the initial measurement of all financial instruments.

    d) Transaction costs are recognized directly in Other Comprehensive Income.

    Answer: b) Transaction costs are added to the initial carrying amount of financial assets measured at Amortised Cost or FVOCI.

25. Which of the following financial assets is most likely to be measured at Amortised Cost under Ind AS 109?

    a) Equity shares held for trading

    b) Corporate bonds held solely to collect contractual cash flows that satisfy the SPPI criterion

    c) Commodity derivatives

    d) Mutual fund units

    Answer: b) Corporate bonds held solely to collect contractual cash flows that satisfy the SPPI criterion.

- **Comprehensive Problems**

1. A Ltd. issued 5,00,000, 8% Debentures of face value ₹100 each on a par value basis on 1st January, 2025. These debentures are redeemable at 12% premium at the end of 2028 or exchangeable for ordinary shares of A Ltd. on a 1:1 basis. The interest rate for similar debentures that do not carry conversion entitlement is 12%.

You are required to calculate the value of the debt portion and equity portion of the above compound financial instrument and show the journal entry at the inception of the financial instrument.

The present value of ₹1 at the end of years 1 to 4 at 8% and 12% are supplied below:

	8%	12%
End of year 1	0.926	0.893
End of year 2	0.857	0.797
End of year 3	0.794	0.712
End of year 4	0.735	0.636

Answer to Question

Present value of Debentures redeemable in 2026 [₹5,00,00,000 × 1.12 × 0.636]	₹3,56,16,000
Present value of interest on debentures [₹40,00,000*×3.038 (sum of 4 years discount factors @12%)]	₹1,21,52,000
Value of Debt component of the convertible debentures (I)	₹4,77,68,000
Issue proceeds from convertible debenture (II)	₹5,00,00,000
Value of equity component (II – I)	₹22,32,000

* Interest payable on debentures every year = ₹5,00,00,000 × 8% = ₹40,00,000.

Journal entry at initial recognition

Particulars	Dr. (₹)	Cr. (₹)
Cash/Bank A/c Dr.	5,00,00,000	
To 8% Debenture (Liability component) A/c		4,77,68,000
To 8% debenture (Equity component) A/c		22,32,000
(Being equity and the debt component recognized on issue of convertible debentures)		

Topic

Module 4: Valuation (Advanced)

FINAL

Group IV - Paper-19

Indirect Tax Laws and Practice (ITLP)

Value of Supply

In the architecture of the Goods and Services Tax (GST), the 'Value of Supply' under Section 15 of the CGST Act operates as the definitive fulcrum for quantifying tax liability. Moving beyond the historical patchwork of indirect taxes, this unified valuation mechanism dictates the exact monetary baseline upon which statutory tax rates are applied. For professionals and businesses alike, mastering valuation principles is paramount. A precise grasp of this framework not only ensures unimpeachable compliance and accurate Input Tax Credit (ITC) utilization but also fortifies defenses against intense departmental scrutiny.

Under Section 15(1) of the CGST Act, 2017, the value of a supply of goods or services is the 'transaction value', the price actually paid or payable, provided that the supplier and the recipient are not related and the price is the sole consideration for the supply. Furthermore, sec. 15(2) mandates specific statutory inclusions to this transaction value. These include any taxes, duties, cesses, fees, and charges levied under any law other than GST. Crucially, the value must also include any amount the supplier is legally liable to pay in relation to the supply but which has been incurred by the recipient, alongside any incidental expenses—such as commission, packing, freight, or insurance—charged by the supplier at or before the time of delivery.

Inclusions in the Value of Supply

The following elements need to be included in the value of supply:

- **Price** paid by the recipient (excluding GST)
- **Taxes, duties, cesses, fees, and charges** (excluding GST) paid by the supplier, which are incidental to the supply
- Any amount that the supplier is liable to pay but has been charged to the recipient (e.g., freight, insurance)
- **Incidental expenses**, such as commission and packing, charged by the supplier to the recipient if they form part of the price of supply
- **Interest, late fees, or a penalty** for delayed payment
- **Subsidies** linked to the supply, except for subsidies provided by the Central and State governments

Exclusions from the Value of Supply

Certain components are excluded from the value of supply:

- **Discounts** given before or at the time of supply, if such discounts are recorded in the invoice
- **Post-supply discounts** provided they are established in the agreement and can be linked to relevant invoices

Key Considerations in Determining the Value of Supply

Several factors are crucial in determining the value of supply under GST:

1. **Transaction Value**: The transaction value is the most common method of determining the value of supply. It is the price agreed upon between the supplier and the recipient in an arm's-length transaction. However, certain conditions must be met for the transaction value to be considered the value of supply:
   - ➢ The buyer and seller must not be related parties.
   - ➢ The price must be the sole consideration for the supply.
2. **Related Party Transactions**: If the supplier and recipient are related parties, the transaction value may not reflect the true value of the supply. In such cases, the tax authorities may apply special valuation rules to determine the arm's-length price. These rules may involve comparing the transaction price with prices in similar transactions between unrelated parties.
3. **Barter Transactions**: When payment is made in kind, the value of supply is determined based on the open market value of the goods or services received. This ensures that the tax liability is based on the true value of the transaction.
4. **Supplies to Government**: Specific rules apply to determine the value of supplies in transactions with government entities. These rules may involve considering factors such as the nature of the supply, the terms of the contract, and the prevailing market prices.
5. **Exclusions from Value of Supply**: Certain items are specifically excluded from the value of supply. These include:
   - ➢ The GST amount itself
   - ➢ Genuine discounts offered and recorded in the invoice
   - ➢ Subsidies received from the government
   - ➢ Taxes and duties that are not charged separately by the supplier

Special Cases in Value Determination

In certain specific scenarios, the determination of the value of supply requires careful consideration and may involve applying specific valuation rules. These cases include:

1. **Composite Supplies**: Composite supplies involve a combination of goods and services that are

inextricably linked. The value of supply for composite supplies is determined based on the principal supply, which is the primary object of the transaction.

2. **Mixed Supplies**: Mixed supplies involve a combination of goods and services that are not inextricably linked. The value of supply for mixed supplies is determined based on the highest rate applicable to the goods or services supplied.
3. **Leases and Rentals**: The value of supply for leases and rentals is determined based on the consideration received for the use of the property. This may include factors such as the duration of the lease, the location of the property, and the prevailing market rates.
4. **Works Contracts**: Works contracts involve the supply of both goods and services. The value of supply for works contracts is determined based on the total consideration received for the contract, including the cost of materials and labour.

Significance of the Value of Supply in GST

The value of supply plays a pivotal role in the GST regime for several reasons:

1. **Tax Calculation**: The value of supply is the basis on which GST is calculated. The tax liability is determined by multiplying the value of supply by the applicable GST rate.
2. **Input Tax Credit (ITC)**: The ITC is a mechanism that allows businesses to set off the GST paid on inputs against the GST payable on outputs. The ITC available to businesses is linked to the value of the supply of inputs.
3. **Accurate Record-Keeping**: Businesses are required to maintain accurate records of the value of supplies for various purposes, including tax compliance, reconciliation, and audits.
4. **GST Returns**: The value of supply is a critical element in the preparation and filing of GST returns. Businesses must report the value of the supply of both taxable and exempt supplies in their returns.

Quick Revision

Inclusions in Value of Supply	Exclusions from Value of Supply
Taxes/duties (excluding GST) are charged separately	GST component
Incidental expenses (freight, insurance, packing, etc.)	Discounts mentioned on the invoice or post-supply are linked to the invoice
Interest, penalty, late fee	Government subsidies
Amounts paid by the recipient but liable to be paid by the supplier	Duties/taxes not charged separately

Conclusion

Ultimately, determining the correct value of supply is not merely a mathematical exercise, but a statutory compliance mandate that forms the bedrock of the GST levy. Erroneous valuation inevitably cascades into flawed tax payments, distorted ITC claims, and the subsequent attraction of penal interest and litigation. Therefore, a meticulous application of Section 15 is indispensable. For aspiring Cost and Management Accountants, developing an expert command over these provisions is a critical prerequisite for delivering tax advisory and navigating the rigours of modern professional practice.

Topic

Module 2:
Performance Measurement, Evaluation and Improvement Tools

Module 6:
Laws and Compliance in Business Valuation

ELECTIVES

Paper-20A

Strategic Performance Management and Business Valuation (SPMBV)

FINAL

Performance Measurement, Evaluation and Improvement Tools

In order to sustain and survive in a dynamic business world, it is essential for an organization to outgrow its competitors. Performance management assists organization to move along the strategic direction towards securing its pre-determined strategic goal(s). It creates an enabling environment where everyone in the organization acts in a manner that achieves its competitive advantage. In this context, it is essential that organizational performance needs to be properly measured, evaluated and reported. Further, while managing performance at various levels in an organization, it is desirable that necessary direction is created for their continuous improvement.

Two elements merit attention in this context:

- **People performance management (PPM) -** It acts as a focal point for the communication process, standard setting process and the performance measurement techniques/tools agreed upon
- **Corporate Performance Management (CPM)** – It focuses on the entire organizational performance and is also referred to as Enterprise Performance Management (EPM). It is understood as a set of management processes that helps the organization define and execute its strategy.

The following tools and techniques are generally used to measure/evaluate/appraise corporate performance under a given set of conditions and in a given context, and to further initiate corporate performance improvement at various activity levels where possible scope for improvement exists: -

1. Balance Score Card (BSC)
2. Designing appropriate KPI(s) - Key Performance Indicators
3. Budgeting and Forecasting
4. Benchmarking & Bench Trending
5. Business Excellence Model
6. Statistical Quality Control
7. Six Signa
8. Total Quality Management
9. Total Productive Maintenance
10. Enterprise Risk Management
11. Performance Reporting
12. Responsibility Accounting & Responsibility reporting

Let us briefly discuss some of the above tools and techniques: -

BSC (Balance Score Card) –

A company's success is related to the realisation of its vision and mission. BSC augments the process of translation of a business vision and strategy into tangible objectives and measures. BSC stresses that financial and non-financial measures must be a part of the performance measurement system at the strategic level as well as at the operational level. The basic premise of the measure is that it endeavours to balance the financial measures for shareholder wealth maximisation, operational measures for customer satisfaction, and internal business processes. It is a set of financial and non-financial measures relating to a company's critical success factors. As a management tool, it helps companies to assess overall performance, improve operational processes, and enable management to develop better plans for long-term improvements. The aim of BSC is to provide a comprehensive framework for translating a company's strategic objectives into a coherent set of performance measurement indicators.

The four perspectives of BSC –

1. **Customer perspective** – How do customers see the entity
2. **Internal Business perspective** – What must the entity excel at
3. **Learning and Growth perspective** – Can the entity continue to improve and create value
4. **Financial perspective -** Under this perspective, the focus will be on financial measures like operating profit, ROI, residual income, EVA, revenue growth, cost reduction, asset utilization, growth in net worth, working capital management, etc

Main Benefits of BSC –

- Better strategic planning initiatives
- Improved strategy execution and communication
- Better alignment of projects/programs and initiatives
- Designing a better management information system
- Improved performance reporting
- Better organizational alignment
- Better process alignment

KPIs (Key Performance Indicators) –

These are Key Performance Indicators set by management to evaluate performance standards and their reliability or acceptance. Different KPIs are fixed in a given context depending on the nature of the organization, its size, authority structure and strategic goals & objectives.

Benchmarking and Bench Trending -

Benchmarking is the process of evaluating business performance against industry-standard metrics. The business processes that are measured for their performance include productivity (both overall & factorial), cycle time, cost and quality. Bench trending is used to monitor performance and operations, drive improvements, and set direction. Bench trending is a technique used to bridge gaps and improve performance levels through new technological methods.

Six Sigma and Lean Management & Lean Manufacturing –

Six Sigma is a tool for process improvement and is prima facie quality focused, identifies defects, and finds ways and means to remove them to ensure processes are efficient, effective and economical under a given set of conditions. Lean Manufacturing, on the other hand, refers to systematised reduction of time within the production/ process cycle, including response times of customers & suppliers. Lean manufacturing focuses on the reduction of inventory cost & wastages and increased productivity. It eliminates all such activities that do not add value to the finished product.

Five principles of Lean Manufacturing are: Value, Value Stream, Flow, Pull and Perfection

Statistical Quality Control (SQC) –

SQC is a technique of applying appropriate statistical methods (probability and sampling) to establish a quality standard and to sustain a minimum qualitative process at least cost.

Techniques of SQC -

- Statistical process control (control charts)
- Acceptance sampling (related to products)

Management Information System –

Properly designed MIS, depending on the size of the organization, authority structure, nature of the entity's business, technology impact, management objectives, etc., contributes significantly towards performance measurement, evaluation and initiating performance improvement.

Performance Reporting / Responsibility Accounting & Responsibility Reporting –

The frequency, nature, information coverage and reliability of management reports related to key responsibility areas highlight responsibility accounting and help management to identify performance gaps or weaknesses in a given situation and help to initiate suitable performance improvement measures to attain the desired objectives & goals with due earnest.

Total Productivity Maintenance (TPM) –

Adoption of a well-designed TPM in an organization helps performance improvement in the following manner:

- Improving overall equipment effectiveness & productivity
- Involving operators in a meaningful way with routine & preventive maintenance of equipment(s) and, thus, improving employee safety
- Improving maintenance efficiency and thereby overall machinery effectiveness
- Lifecycle equipment management and reducing breakdown maintenance.
- Reducing overall maintenance cost over time.

Total Quality Management and Business Excellence Model -

In the context of performance evaluation & improvement, TQM contributes as under:-

- An integrated organizational effort to improve quality at all levels
- It is an organizational vision
- It is a part of long-term business performance planning
- It is also a part of the Annual Quality Plan of an organization and forms a part of the overall Business Improvement Plan.

Essentials of TQM in the context of Performance Improvement –

(a) Customer focus

(b) Continuous Improvement

(c) Employee empowerment

(d) Use of appropriate Tools & Equipment

(e) Appropriate product design

(f) Process management

(g) Suppliers' quality management

The core concepts of TQM are -

(a) Quality Control

(b) Quality Assurance

(c) Quality Management

Essentially, TQM trades off between quality control costs (quality prevention costs & quality appraisal costs) and quality failure costs (internal failure costs & external failure costs)

TQM is a part of the Business Excellence Model (BEM), whilst BEM covers more comprehensive business

functions, including quality of overall management performance & decisions, and directs focus as to how excellence in key business performances may be attained over a period of time.

Budgeting and Variance Analysis –

It is also an important performance improvement tool and can give impressive results if budgets are prepared covering all key responsibility centres, considering possible limiting factors and proper participation of all responsible officials in the implementation and running of the budgetary process is assured.

More importantly, it is the promptness of the management to identify and take necessary action to rectify the budget variances at the earliest opportunity that determines how effectively this tool can control and improve performance with reference to predetermined standards/yardsticks under a given set of conditions.

Enterprise Risk Management (ERM) –

It is a process of identifying, analysing, evaluating and prioritising business risks followed by integrated application of resources to reduce and control the probability or impact of unwanted events or to maximise the realization of possible opportunities commensurate with the overall & long-term objectives of an organization.

Main elements of ERM –

- Risk Identification
- Risk Analysis & Assessment
- Risk Response
- Risk Prioritization
- Risk Mitigation & Avoidance
- Risk Sharing & Transfer
- Risk Avoidance
- Risk Acceptance
- Risk Governance (Communication & Monitoring)

If effectively implemented and monitored, ERM can be a very significant performance-enhancing tool in an organisation over time by eliminating various risk-driven unwanted events/incidents that diminish organisational productivity and further redirecting enterprise resources (including costs & manpower) toward better attainment of organisational goals.

Concluding Remarks

The tools / methods discussed above are all uniquely significant to measure, evaluate and improve organisational performance, but it is the top management's understanding as to which tools and methods to use under a given set of conditions and circumstances, depending on the purpose, objectives, goals and in the overall interest of the various stakeholders.

Laws & Compliance in Business Valuation

Business valuation refers to the process of determining the economic worth of a company or its assets. In India, valuation has gained increasing importance with the rise of startup investments, cross-border transactions, and regulatory scrutiny. Valuers must not only apply appropriate financial methodologies but also comply with various legal provisions set by statutes such as the Companies Act, Income Tax Act, FEMA regulations, IBB Code , SEBI regulations ,etc. and multiple guidelines issued by the professional bodies.

1. Companies Act, 2013

The Companies Act, 2013, is one of the most significant legislations governing business valuation in India. It mandates valuation in several corporate actions such as mergers, amalgamations, the issue of shares, and restructuring.

Key Provisions:

- **Section 247:** This section introduces the concept of Registered Valuers. Only individuals or entities registered with the Insolvency and Bankruptcy Board of India (IBBI) can conduct valuations for specified purposes.
- Valuation is required in cases of:
  - Issue of shares on a preferential basis
  - Buyback of shares
  - **Sec 62:** Further Issue of Share Capital
  - Corporate restructuring (mergers and demergers, etc) (Sections 230, 231 and 232 related to mergers & amalgamations)

Compliance Requirements:

- Appointment of a registered valuer
- Ensuring independence and impartiality
- Disclosure of valuation methods and assumptions in valuation reports
- Ensuring compliance with the provisions of Companies Act, 2013 which may be applicable in a given case.

2. Insolvency and Bankruptcy Code, 2016 (IBC)

The IBC plays a crucial role in valuation during insolvency proceedings. Accurate valuation is essential to determine the liquidation value and the fair value of assets.

Key Aspects:

- Registered valuers are appointed to determine:
  - **Fair Value:** Estimated realizable value under normal conditions
  - **Liquidation Value:** Value, if assets are sold under distress

Compliance Requirements:

- Valuers must follow IBBI Valuation Rules
- Confidentiality of valuation reports
- Use of internationally accepted valuation standards

3. Income Tax Act, 1961

Valuation has direct implications for taxation, particularly in the context of share transfers and the issue of shares.

Important Sections:

- **Section 56(2)(viib):** Taxes on excess premium received by closely held companies over fair market value (commonly known as "Angel Tax")
- **Section 50CA:** Governs valuation of unquoted shares for capital gains
- **Rule 11UA:** Prescribes methods for determining fair market value (FMV)

Compliance Requirements:

- Use of prescribed valuation methods (DCF or NAV)
- Certification by a merchant banker or chartered accountant (depending on the given case)
- Proper documentation to justify valuation

4. Foreign Exchange Management Act (FEMA), 1999

FEMA regulations are critical in cross-border transactions involving foreign investors.

Governing Authority:

- Reserve Bank of India (RBI)

Key Guidelines:

- Valuation must be done as per an internationally accepted pricing methodology
- Pricing guidelines apply to:
  - Issue of shares to non-residents
  - Transfer of shares between residents and non-residents

Compliance Requirements:

- Fair valuation on an arm's length basis
- Certification by a SEBI-registered merchant banker or a chartered accountant
- Adherence to sectoral caps and pricing norms

5. Securities and Exchange Board of India (SEBI) Regulations

SEBI governs valuation for listed companies and entities accessing capital markets.

Relevant Regulations:

- SEBI (Issue of Capital and Disclosure Requirements) Regulations (ICDR)
- SEBI (Substantial Acquisition of Shares and Takeovers) Regulations (SAST)
- SEBI (Delisting of Equity Shares) Regulations

Valuation Scenarios:

- Initial Public Offerings (IPOs)
- Open offers during acquisitions
- Delisting of shares

Compliance Requirements:

- Transparent pricing mechanisms
- Disclosure of valuation basis in offer documents
- Fairness opinions from independent experts

6. Indian Accounting Standards (Ind AS)

Ind AS plays a significant role in valuation, especially for financial reporting.

Key Standards:

- Ind AS 113 – Fair Value Measurement
- Ind AS 36 – Impairment of Assets
- Ind AS 103 – Business Combinations

Compliance Requirements :

- Use of fair value hierarchy (Level 1, 2, 3 inputs)
- Regular impairment testing
- Consistency in valuation techniques

7. IBB (Registered Valuers and Valuation) Rules, 2017

These rules establish the framework for the valuation profession in India.

Key Features:

- Registration of valuers under IBBI
- Categorization into asset classes:
  - Land and building
  - Plant and machinery
  - Securities and financial assets

Compliance Requirements:

- Adherence to a code of conduct
- Continuous professional education
- Maintenance of valuation records

8. International Valuation Standards (IVS)

Although not mandatory in all cases, IVS is often followed for global consistency and for cross-border mergers & acquisitions

Importance:

- Used in cross-border transactions
- Enhances credibility with international investors

Compliance Requirements :

- Adoption of globally accepted valuation approaches:
  - Market approach
  - Income approach
  - Cost approach

Following IVS may be further referred to on a case-by-case basis requirement: -

IVS 101 (Scope of Work)

IVS 102 (Investigation & Compliance)

IVS 103 (Reporting)

IVS 104 (Bases of Value)

IVS 105 (Valuation Approaches & Methods)

IVS 200 (Business & Business Interests)

IVS 210 (Intangible Assets)

IVS 220 (Non Financial Liabilities)

IVS 230 (Inventory)

IVS 300 (Plant & Machinery)

IVS 400 ((Rela Property Interests)

IVS 410 (Development Property)

IVS 500 (Financial Instruments)

9. Stamp Duty and State Laws

Valuation affects the stamp duty payable on the transfer of assets and shares.

Key Considerations:

- Stamp duty is levied based on transaction value or circle rate
- States may have different rules

Compliance Requirements :

- Proper valuation to avoid underreporting
- Adherence to state-specific stamp laws

10. Competition Act, 2002

Valuation is relevant in mergers and acquisitions that may affect market competition.

Governing Authority:

- Competition Commission of India (CCI)

Compliance Requirements :

- Determining transaction thresholds
- Filing combinations with CCI if thresholds are exceeded
- Supporting valuation data in filings

11. SARFAESI Act, 2002

The Securitization & Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act,2002, is a legislation that has been framed to address the problem of NPAs or bad assets through a separate process and mechanisms. This enactment enabled banks and financial institutions to sell off their NPAs to asset reconstruction companies registered with the RBI.

The objectives of the Act are :

a) To regulate securitisation of financial assets

b) Enforcement of security interests and to provide for a central database of security interests created on property rights.

Hence, in case of valuation of financial assets falling under the aforesaid category for the purpose of securitisation, the provisions of this Act have a bearing.

12. Sector-Specific Regulations

Certain industries have additional valuation requirements.

Examples:

- Banking and Financial services (RBI guidelines)
- Insurance (IRDAI regulations)
- Telecommunications (DoT guidelines)

Compliance Requirements:

- Industry-specific valuation norms
- Specific Regulatory approvals, where required

13. Documentation and Reporting Standards

Regardless of the governing law, valuation reports must meet certain standards.

Key Elements:

- Purpose of valuation
- Scope and limitations
- Methodology used
- Assumptions and disclaimers

Compliance Requirements:

- Transparency and defensibility
- Proper record-keeping
- Ability to withstand regulatory scrutiny

Challenges in Compliance

Business valuation in India faces several challenges:

- Frequent regulatory changes
- Differences as to approach between tax and regulatory valuation methods
- Subjectivity in assumptions
- Lack of standardized practices across sectors

Valuers must exercise professional judgment while ensuring adherence to applicable laws.

Conclusion

Business valuation in India is deeply intertwined with legal and regulatory compliance. From the Companies Act to FEMA, Income Tax laws, and SEBI regulations, each framework serves a specific purpose in ensuring that valuations are fair, transparent, and reliable. The introduction of registered valuers and standardised rules has significantly improved the credibility of the valuation process, but there are certain grey areas and overlaps that need to be addressed.

For businesses, investors, and professionals, understanding these legal requirements is essential not only for compliance but also for making informed financial decisions. As India continues to integrate with global markets, adherence to both national and international valuation standards will become increasingly important.

FINAL

Topic

Module 1:
Introduction to Risk Management

Module 6:
Introduction to Insurance Business

ELECTIVES

Paper-20B

Risk Management In Banking and Insurance (RMBI)

Risk Management in Banking

Introduction to Risk Management

Risk is an inseparable component of the banking business. Banks operate by accepting deposits from the public and deploying these funds in various earning assets such as loans, investments, and other financial products. Every banking transaction carries an element of uncertainty that may affect the bank's earnings, capital, liquidity, reputation, or even its continued existence. Unlike manufacturing or trading enterprises, banks deal primarily with financial assets and liabilities whose values are influenced by economic conditions, market fluctuations, borrower behaviour, regulatory changes, technological developments, and global financial events. Consequently, effective risk management has become one of the most important pillars of modern banking.

Risk management has therefore evolved from being merely a compliance function to becoming a strategic management tool. It enables banks to optimize returns while maintaining acceptable levels of risk. It also enhances stakeholder confidence by ensuring that risks are managed within the bank's approved risk appetite.

Meaning of Risk:

Risk may be defined as the possibility of an adverse deviation from the expected outcome due to uncertainty. In banking, risk represents the probability that actual financial results may differ from anticipated results because of internal or external events. Such deviations may lead to financial losses, operational disruptions, legal liabilities, reputational damage, or capital erosion.

Risk does not necessarily imply loss alone. It also signifies uncertainty surrounding future outcomes. However, banking regulations and prudential management primarily focus on downside risks because they have the potential to threaten the safety and soundness of financial institutions.

The banking business fundamentally involves taking calculated risks. Banks cannot eliminate risks altogether because lending, investing, and financial intermediation inherently involve uncertainty. Instead, banks strive to identify, assess, mitigate, monitor, and control risks so that they remain within acceptable limits.

Concept of Risk Management:

Risk management is the systematic process of identifying, measuring, evaluating, controlling, monitoring, and reporting risks that may affect the achievement of an organization's objectives. In banking, it refers to the continuous process of managing various financial and non-financial risks to safeguard the bank's capital, profitability, liquidity, reputation, and long-term sustainability.

Risk management encompasses both preventive and corrective measures. Preventive measures aim at avoiding excessive risk-taking, while corrective measures seek to minimize losses when adverse events occur. Effective risk management ensures that the bank maintains adequate capital, sufficient liquidity, and sound governance to withstand unexpected shocks.

Modern banking emphasizes Enterprise Risk Management (ERM), where all categories of risks are managed in an integrated manner rather than in isolation. This holistic approach recognizes the interrelationship among various risks and facilitates informed decision-making.

Evolution of Risk Management in Banking:

Banking risk management has undergone significant transformation over the past few decades. Traditionally, banks focused primarily on credit risk because lending constituted the major business activity. Risk assessment relied largely on the judgment and experience of loan officers.

With globalization, deregulation, technological innovation, financial engineering, and the emergence of complex financial products, banks became exposed to multiple categories of risks simultaneously. Consequently, risk management expanded to include market risk, operational risk, liquidity risk, interest rate risk, cyber risk, climate risk, compliance risk, and strategic risk.

International regulatory initiatives, such as the Basel Committee on Banking Supervision, introduced globally accepted standards for risk measurement and capital adequacy. Basel-I emphasized capital adequacy, Basel II introduced risk-sensitive capital frameworks, while Basel III strengthened capital, leverage, liquidity, and stress testing requirements following the Global Financial Crisis. These developments transformed risk management into a highly quantitative, technology-driven, and governance-oriented discipline.

Importance of Risk Management in Banking:

Risk management has become indispensable because banks perform the critical function of financial intermediation in the economy. Failure of banks can trigger systemic crises affecting depositors, investors, businesses, governments, and the entire financial system.

A strong risk management framework enables banks to identify emerging threats at an early stage. It supports better credit decisions, prudent investment strategies, effective liquidity planning, and appropriate capital allocation. Banks with sound risk management practices generally enjoy higher credit ratings, lower funding costs, improved market confidence, and better long-term profitability.

Moreover, technological advancements have introduced new dimensions of risk, including cyber-attacks, digital frauds, data privacy breaches, artificial intelligence risks, and operational disruptions. Effective risk management, therefore, serves as a competitive advantage in the rapidly evolving financial landscape.

Fundamental Principles of Risk Management:

Successful risk management is founded on several universally accepted principles. Risks should first be identified comprehensively before they materialize into losses. Accurate measurement techniques should then be employed to quantify potential exposures using qualitative and quantitative methods.

Risk ownership should be clearly assigned across organizational levels. Decision-making must align with the bank's approved risk appetite and risk tolerance. Continuous monitoring through early warning systems helps detect deterioration in risk profiles. Independent review and internal audit provide assurance regarding the effectiveness of controls.

Risk management should also be integrated into business strategy rather than functioning merely as a regulatory requirement. It should support informed decision-making while balancing profitability with safety.

Risk Appetite and Risk Tolerance:

Every bank determines the level of risk it is willing to accept in pursuit of its strategic objectives. This acceptable level is known as the Risk Appetite. It reflects the bank's capacity and willingness to undertake risks while maintaining financial stability.

Risk tolerance defines the permissible variation around the approved risk appetite. It establishes operational limits within which individual business units may function. Exceeding these limits triggers escalation mechanisms requiring management intervention.

An appropriately defined risk appetite enables consistent decision-making across lending, investment, treasury operations, and business expansion while ensuring alignment with capital strength and regulatory expectations.

Risk Governance Framework:

Effective risk management begins with strong governance. The Board of Directors bears ultimate responsibility for approving the bank's risk strategy, risk appetite, and risk management policies. The Board oversees implementation through specialized committees such as the Risk Management Committee, Audit Committee, and Asset Liability Management Committee.

Senior management is responsible for translating board-approved policies into operational procedures. Business units identify and manage risks within approved limits, while independent risk management departments continuously monitor exposures and recommend corrective actions.

Internal auditors provide independent assurance regarding compliance with policies and effectiveness of internal controls. External auditors and banking regulators further strengthen governance through independent supervision and periodic inspections.

Risk Management Process:

Risk management follows a structured and continuous process beginning with risk identification. Banks systematically identify all potential sources of risk associated with lending, treasury operations, investments, technology, human resources, legal matters, and external economic conditions.

The identified risks are then measured using quantitative models, statistical techniques, scenario analysis, sensitivity analysis, and expert judgment. Following measurement, risks are evaluated based on their probability and potential impact.

Appropriate mitigation strategies are subsequently developed through diversification, collateral, insurance, hedging, internal controls, policy limits, and contingency planning. Continuous monitoring ensures that risks remain within approved thresholds. Finally, comprehensive reporting enables senior management and the Board to make informed decisions based on accurate risk information.

Role of Technology in Risk Management:

Digital transformation has fundamentally reshaped banking risk management. Banks increasingly rely on advanced technologies, including Artificial Intelligence, Machine Learning, Big Data Analytics, Cloud Computing, Blockchain, and Robotic Process Automation, for identifying and monitoring risks.

Real-time dashboards provide management with continuous visibility into key risk indicators. Predictive analytics facilitates early detection of deteriorating credit quality and potential fraud. Artificial intelligence supports customer due diligence, transaction monitoring, anti-money laundering surveillance, and cyber threat detection.

Technology also enhances regulatory reporting, stress testing, scenario analysis, and model validation while reducing operational errors and improving decision-making speed.

Challenges in Banking Risk Management:

Risk management has become increasingly complex due to rapid technological advancements, globalization,

interconnected financial markets, climate change, geopolitical uncertainties, evolving customer expectations, and sophisticated financial crimes.

Banks must continuously adapt to changing regulatory requirements while maintaining profitability in a competitive environment. Cybersecurity threats, digital frauds, model risks, artificial intelligence governance, third-party outsourcing risks, and climate-related financial risks require new approaches to risk assessment and mitigation.

Another significant challenge is balancing innovation with prudent risk management. Banks introducing digital products and fintech collaborations must ensure that emerging risks are identified and adequately controlled without stifling innovation.

To Sum Up:

Risk management has become the cornerstone of modern banking. In an increasingly uncertain and interconnected financial environment, banks can no longer rely solely on traditional methods of managing risks. Instead, they must adopt comprehensive, technology-enabled, and governance-driven frameworks that integrate risk considerations into every strategic and operational decision.

An effective risk management system enables banks to identify emerging threats, measure potential losses, allocate capital efficiently, maintain adequate liquidity, comply with regulatory requirements, and protect the interests of depositors, shareholders, and other stakeholders. It also supports sustainable profitability by ensuring that risk-taking remains aligned with the institution's risk appetite and long-term objectives.

Risk Management in Insurance

Introduction to Insurance Business

Insurance is one of the most significant pillars of the modern financial system and plays an indispensable role in promoting economic growth, financial stability, and social welfare. It serves as a mechanism for transferring risks from individuals, businesses, and institutions to insurance companies that possess the financial capacity and expertise to manage such risks. Every individual and business entity is exposed to numerous uncertainties arising from accidents, illnesses, natural disasters, fire, theft, cyber-attacks, legal liabilities, and other unforeseen events. These uncertainties may lead to substantial financial losses that could adversely affect personal wealth, business continuity, and economic development. Insurance provides financial protection against such uncertainties by pooling risks across a large number of policyholders and compensating those who suffer losses.

With increasing globalization, technological innovation, climate change, cyber threats, demographic shifts, and changing customer expectations, the insurance industry today faces a far more complex risk environment than ever before. Regulatory authorities across the world, including the Insurance Regulatory and Development Authority of India (IRDAI), have strengthened prudential regulations to ensure that insurers maintain adequate solvency, robust governance, effective internal controls, and comprehensive enterprise risk management systems. Consequently, risk management has evolved from being merely an operational necessity to becoming a strategic function that influences every aspect of the insurance business.

Meaning of Insurance:

Insurance is a contractual arrangement under which one party, known as the insurer, agrees to compensate another party, known as the insured, for specified financial losses arising from uncertain future events in exchange for payment of a premium. The insurance contract, commonly known as a policy, specifies the risks covered, exclusions, conditions, premium payable, policy period, and claim settlement procedures.

Insurance therefore converts uncertain and potentially devastating financial losses into relatively certain and affordable premium payments, thereby providing financial security and peace of mind to individuals and businesses alike.

Objectives of Insurance:

The primary objective of insurance is to provide financial protection against unforeseen losses that may arise due to specified risks. Insurance helps individuals preserve their financial stability by compensating for losses resulting from accidents, illnesses, property damage, death, disability, or legal liabilities.

For businesses, insurance facilitates continuity by protecting assets, revenues, and operations against unexpected disruptions. It encourages entrepreneurship by reducing financial uncertainties associated with business activities. Insurance also supports economic development by mobilizing long-term savings and channelling them into productive investments such as infrastructure, government securities, corporate bonds, and capital markets.

Another important objective is promoting social security. Life insurance protects families against loss of income resulting from the death of the earning member, while health insurance reduces the financial burden of medical

expenses. Agricultural insurance safeguards farmers against crop failures, and various government-sponsored insurance schemes promote financial inclusion among economically weaker sections of society.

Risk as the Foundation of Insurance:

Risk constitutes the very foundation of insurance business. Without uncertainty, insurance would not exist. Every insurance product is designed to protect against a specific category of risk that may adversely affect individuals or businesses.

However, not every risk is insurable. Insurance generally covers pure risks where only the possibility of loss exists. Speculative risks involving potential gains as well as losses, such as stock market investments or gambling, are normally not insurable. Insurable risks should be measurable, accidental, independent, financially significant, and capable of being pooled across a sufficiently large number of similar exposure units.

The insurer's challenge lies in accurately assessing the probability and financial impact of these risks while determining appropriate premium rates that ensure long-term financial sustainability.

Meaning of Risk Management in Insurance:

Risk management in insurance refers to the systematic process of identifying, measuring, evaluating, controlling, monitoring, and reporting all risks that may affect the insurer's financial condition, solvency, profitability, reputation, and operational continuity. Since insurers themselves assume risks from policyholders, effective risk management becomes central to their business model.

Insurance risk management extends beyond underwriting risks to include investment risk, market risk, credit risk, liquidity risk, operational risk, cyber risk, legal risk, compliance risk, reputational risk, strategic risk, and emerging risks arising from climate change and technological innovation.

Enterprise Risk Management (ERM) has emerged as the preferred framework for managing these interconnected risks comprehensively across the entire organization.

Risk Pooling and Diversification:

One of the distinguishing features of insurance business is the concept of risk pooling. Insurance companies collect premiums from a large number of policyholders facing similar risks. Since losses occur only to a relatively small proportion of policyholders during a given period, the pooled premium fund becomes sufficient to compensate those who actually experience losses.

Diversification further strengthens risk management by spreading exposures across different geographical regions, industries, customer segments, products, and risk categories. Diversified portfolios reduce concentration risks and enhance the insurer's ability to withstand adverse events affecting particular sectors or locations.

Reinsurance complements diversification by enabling insurers to transfer portions of exceptionally large or catastrophic risks to specialized global reinsurance companies.

Insurance Business Model:

The insurance business model differs substantially from other commercial enterprises. Premium income is received in advance, whereas claims are paid only when insured events occur. During the intervening period, insurers invest premium funds to generate investment income that supplements underwriting profits.

The profitability of an insurer, therefore, depends upon prudent underwriting, effective claims management, sound investment decisions, operational efficiency, and disciplined expense management. Excessive underwriting risks, poor investment decisions, inadequate reserves, or weak governance may adversely affect financial stability.

Maintaining an appropriate balance between underwriting profitability and investment performance remains one of the key strategic objectives of insurance management.

Digital Transformation and Insurance:

Digital technology has fundamentally transformed insurance operations. Artificial Intelligence, Machine Learning, Internet of Things (IoT), Blockchain, Big Data Analytics, Cloud Computing, and Robotic Process Automation are reshaping underwriting, claims management, customer service, fraud detection, and risk assessment.

Usage-based insurance products utilize telematics data from motor vehicles to determine individualized premiums. Wearable devices facilitate health insurance underwriting. Satellite imagery assists agricultural insurance claim assessments, while drones improve property inspections following natural disasters.

Digital platforms enhance customer experience, improve operational efficiency, reduce fraud, and enable real-time monitoring of emerging risks.

Emerging Risks in Insurance Business:

The insurance industry increasingly faces complex emerging risks that require innovative management approaches. Climate change has significantly increased the frequency and severity of floods, cyclones, droughts, heatwaves, and wildfires, resulting in escalating catastrophe claims.

Cyber insurance has emerged as a rapidly growing segment due to increasing cyber-attacks, ransomware incidents, data breaches, and digital fraud. Artificial Intelligence

introduces both opportunities and governance challenges relating to algorithmic bias, data privacy, and model risk.

Pandemics, geopolitical conflicts, supply chain disruptions, demographic changes, environmental sustainability, and evolving legal liabilities further contribute to the dynamic risk landscape confronting modern insurers.

Importance of Risk Management in Insurance:

Risk management is indispensable for ensuring the long-term sustainability of insurance companies. Effective risk management enables insurers to maintain adequate solvency, fulfil contractual obligations, preserve financial stability, and safeguard policyholders' interests.

Sound risk management facilitates appropriate product pricing, prudent underwriting, efficient capital allocation, improved investment decisions, and enhanced operational resilience. It also strengthens regulatory compliance and protects insurers against financial distress arising from catastrophic events or market volatility.

A robust risk management framework further enhances customer confidence, improves credit ratings, reduces capital costs, supports innovation, and promotes sustainable growth in an increasingly competitive marketplace.

Future of Insurance Business:

The future of insurance will be characterized by greater reliance on advanced analytics, artificial intelligence, predictive modelling, digital ecosystems, embedded insurance, climate risk assessment, and personalized insurance products. Insurers will increasingly utilize real-time data collected through connected devices to improve underwriting accuracy and customer engagement.

Environmental, Social, and Governance (ESG) considerations will significantly influence underwriting policies, investment strategies, and risk management practices. Regulatory expectations regarding operational resilience, cybersecurity, climate disclosures, and consumer protection will continue to strengthen.

The integration of technology with scientific risk assessment will enable insurers to provide faster claims settlement, more customized products, and improved customer experiences while maintaining financial stability and regulatory compliance.

To Sum Up:

A robust risk management framework supported by sound corporate governance, advanced analytics, effective internal controls, and strong regulatory compliance enables insurers to maintain financial strength, honour policyholder commitments, withstand adverse events, and achieve sustainable profitability. As the insurance industry continues to evolve, institutions that successfully integrate innovation with disciplined risk management will remain resilient, competitive, and capable of fulfilling their fundamental mission of providing financial security and contributing to the long-term stability and development of the economy.

Topic

Module 2:
The Entrepreneurial Ecosystem

ELECTIVES

Paper-20C

Entrepreneurship and Start Up (ENTS)

Working Capital Management

Working Capital Management (WCM) is the process of managing a startup's short-term assets and liabilities to ensure it has enough liquidity to meet day-to-day operational needs. It also measures a company's efficiency and short-term financial health by balancing current assets (like cash and inventory) against current liabilities (like unpaid bills). For startups, managing this balance is often a matter of survival rather than just optimisation.

Importance of Working Capital Management in Startups

1. **Ensures smooth business operations:** Many startups fail not from a lack of profitability, but because they run out of cash to pay immediate bills. So, WCM helps to ensure smooth operations of business.
2. **Supports business growth**: It provides funds for expanding operations, hiring employees, and increasing production and allows startups to seize new market opportunities quickly.
3. **Boosts investor confidence**: Investors prefer startups with strong financial discipline and effective cash management. Strong working capital management proves operational discipline.
4. **Supplier leverage**: Paying suppliers on time builds trust. This trust helps you negotiate better prices or longer payment terms later.
5. **Improves creditworthiness:** Timely payment to suppliers and lenders improves the startup's credit rating. It facilitates easier access to loans and trade credit in the future.
6. **Ensures business sustainability:** Proper management of current assets and liabilities increases the chances of long-term survival. It helps startups navigate periods of slow sales or delayed customer payments.

Strategies for Working Capital Management in Startups

Shorten the Cash Conversion Cycle	Reduce the time between buying raw materials and receiving cash from sales.
Offer Incentives	Give customers small discounts (e.g., 2% off) for early invoice payments.
Negotiate Vendor Terms	Ask suppliers for 60-day or 90-day payment windows instead of 30 days.
Use Tech Automation	Deploy automated invoicing and inventory tracking software to eliminate manual delays.
Maintain a Cash Buffer	Keep an emergency reserve to handle unexpected market drops or delayed funding rounds.

Determination of Working Capital

Particulars	Amount (₹)
(I) Estimation of Current Asset: Amount	
(a) Minimum desired cash and bank balances	xxxx
(b) Inventories	
• Raw material	xxxx
• Work-in-process	xxxx
• Finished Goods	xxxx
(c) Debtors*	xxxx
Total Current Assets	xxxxx
(II) Estimation of Current Liabilities:	
(a) Creditors**	xxxx
(b) Wages	xxxx
(c) Overheads	xxxx
Total Current Liabilities	xxxx
(III) Net Working Capital (I – II)	xxxx
Add: Margin for contingency (if any)	xxxx
(IV) Net Working Capital Required	

Tutorial Note

*If payment is received in advance, the item will be listed in CL.

**If an advance payment is to be made to creditors, the item would appear under CA. The same would

be the treatment for advance payment of wages and overheads.

Illustration 1

PICK Ltd. is launching a new project for the manufacture of a unique component. At full capacity of 24,000 units, the cost per unit will be as follows:

Particulars	Amount (₹)
Material	80
Labour and variable expenses	40
Fixed manufacturing and administrative expenses	20
Depreciation	10
Total	150

The Selling price per unit is expected to be ₹200. Selling expenses will be per unit: ₹10 (80% variable).

In the first two years, production, and sales are expected to as follows:

Year	Production	Sales
1	15,000	14,000
2	20,000	18,000

To assess working capital requirements, the following additional information is given:

(a) Stock of raw material – 3 months' average consumption.

(b) Work-in-process – Nil.

(c) Debtors – 1 month's average cost of sales.

(d) Creditors for supply of materials – 2 months' average purchases of the year.

(e) Creditors for expenses – 1 month's average of all expenses during the year.

(f) Minimum desired cash balance – ₹20,000.

(g) Stock of finished goods is taken at average cost.

You are required to prepare a projected statement of working capital requirements for two years showing all necessary calculations.

Answer:

Statement of Working Capital Requirement of PICK Ltd. for year 1 and year 2

Particulars	Year 1 (₹)	Year 2 (₹)
(A) Current Assets		
(i) Raw material stock (W/N 4)	3,00,000	4,00,000
Work in Progress	-	-
(ii) Finished goods (W/N 5)	1,52,000	4,33,143
(iii) Debtors (W/N 6)	1,90,667	2,32,571
(iv) Minimum desired Cash	20,000	20,000
Total Current Assets	**6,62,667**	**10,85,714**
(B) Current Liabilities		
Creditors for the supply of Material (W/N 7)	2,50,000	2,83,333
Creditors for supply of Expenses (W/N 8)	1,03,333	1,22,667
Total Current Liabilities	**3,53,333**	**4,06,000**
Net Working Capital (A) – (B)	3,09,334	6,79,714
Add: 20% Safety Margin	61,867	1,35,943
Working Capital Requirement	**3,71,201**	**8,15,657**

Workings

1. **Cost Structure**

Particulars	₹ per Unit
Material	80
Labour & Variable Expenses	40
Fixed Manufacturing & Administrative Expenses	20
Depreciation (non-cash)	10
Total Cost	**150**

2. **Selling Price = ₹200 per unit**

   Selling Expenses = ₹10 per unit

   1. Variable (80%) = ₹8

   2. Fixed (20%) = ₹2

3. **Production**

Year 1

Production = 15,000 units

Sales = 14,000 units

Year 2

Production = 20,000 units

Sales =18,000 units

4. **Raw Materials**

Particulars		Year 1	Year 2
Production units		15,000 Units	20,000 Units
Stock of Raw Materials			
Year 1(15,000 Units × ₹80 ×3/4) [₹]	@₹80 per unit	3,00,000	
Year 2 (20,000 Units × ₹80 ×3/4) [₹]	@₹80 per unit		4,00,000

5. Finished Goods

Particulars		Year 1	Year 2
Production units		15,000 Units	20,000 Units
Cost of Production			
Materials (₹)	@₹80 per unit	12,00,000	16,00,000
Labour and variable Expenses (₹)	@₹40 per unit	6,00,000	8,00,000
Total Fixed and Administrative Expenses (₹)	₹20 per unit × 24,000 units	4,80,000	4,80,000
Current Cost (Cash) (₹)		22,80,000	28,80,000
Add: Opening Stock at average cost (₹)	22,80,000 × (1,000/15,000)	-	1,52,000
Less: Closing Stock (₹)1,52,000 for year 1	28,80,000×(3,000/21,000) for year 2	1,52,000	4,33,143
Cost of Goods Sold (cash)		21,28,000	25,98,857

6. Debtors

Particulars		Year 1	Year 2
Production units		15,000 Units	20,000 Units
Cost of Goods Sold (cash) (₹)		21,28,000	25,98,857
Add: Variable Expenses [14,000 units] for year 1 (₹)	@₹8 per unit	1,12,000	
Add: Variable Expenses [18,000 units] for year 2 (₹)	@₹8 per unit		1,44,000
Add: Total fixed selling expenses [24,000 units] (₹)	@₹2 per unit	48.000	48,000
Cost of sales (Cash) [₹]		22,88,000	27,90,857
Debtors 1 month (22,88,000/12) for year 1 and 27,90,857/12 for year 2 [₹]		1,90,667	2,32,571

7. Creditors for supply of Material

Particulars		Year 1	Year 2
Production units		15,000 Units	20,000 Units
Materials consumed (₹)	@₹80 per unit	12,00,000	16,00,000
Add: Closing stock (equivalent to 3 months average consumption) [₹]		3,00,000	4,00,000
Less: Opening stock of purchase (₹)			3,00,000
Purchase [₹]		15,00,000	17,00,000
Creditors for suppliers for 2 months (15,00,000 ×2/12) for year 1 and (17,00,000 ×2/12) for year 2 [₹]		2,50,000	2,83,333

8. Creditors for Expenses

Particulars		Year 1	Year 2
Production units		15,000	20,000
Labour and variable Expenses (₹)	@₹40 per unit	6,00,000	8,00,000
Total Fixed and Administrative Expenses (₹)	₹20 per unit × 24,000 units	4,80,000	4,80,000
Variable Expenses [14,000 units] for year 1 (₹)	@₹8 per unit	1,12,000	
Variable Expenses [18,000 units] for year 2 (₹)	@₹8 per unit		1,44,000
Total fixed selling expenses [24,000 units] (₹)	@₹2 per unit	48.000	48,000
Total Expenses [₹]		12,40,000	14,72,000
Creditors for Expenses for year 1 ₹12,40,000 × 2/12		1,03,333	
for year 2 ₹14,72,000 × 2/12			1,22,667

Multiple Choice Questions:

1. Which of the following will be considered while calculating working capital?

   (1) Short-term advances

   (2) Stock of WIP

   (3) Short-term Investments

   (4) Personal Investment Policy

   Select the correct answer from the options given below:

   (A) (2) & (3)

   (B) (1) & (3)

   (C) (1), (2) & (3)

   (D) All of the above except (4)

   Answer: (D)

2. Following the data, calculate the finished goods conversion period for the years 2024 and 2025.

Particulars	2024 (₹)	2025 (₹)
Raw materials inventory	18,000	20,400
Finished goods inventory	10,000	15,000
Other information for 1 year		
Raw Materials Consumed	11,000	13,000
Raw materials inventory	1,25,000	1,40,000

   Note: 1 Year = 360 days

   (A) 29 days and 39 days

   (B) 39 days and 29 days

   (C) 25 days and 35 days

   (D) 35 days and 25 days

   Answer: (A)

3. Following the data, calculate total sales

   Debtors as per Working Capital Statement: ₹3,00,000

   Debtors' collection period: 45 days

   Gross profit ratio: 20%

   Cash sales ₹5,00,000

   1 year = 365 days

   (A) ₹24,00,000

   (B) ₹19,00,000

   (C) ₹29,00,000

   (D) ₹25,00,000

   Answer: (C)

4. If credit sales for the year are ₹5,40,000 and Debtors at the end of the year are ₹90,000, and the average collection period will be:

   (A) 30 days

   (B) 61 days

   (C) 90 days

   (D) 120 days

   Answer: (B)

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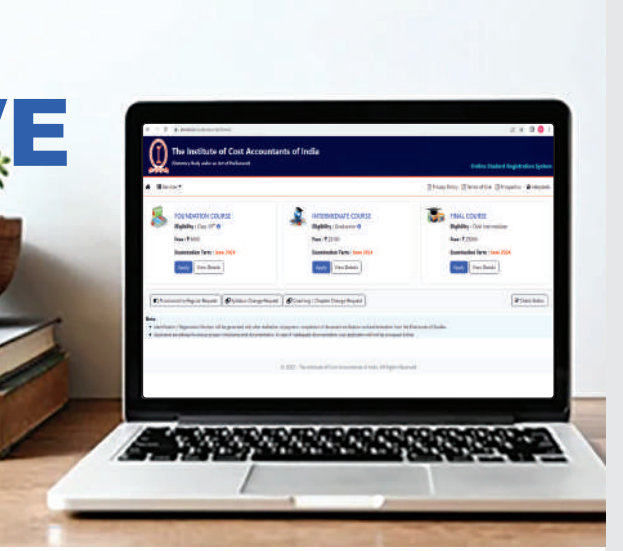

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