



**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](http://www.icmai.in)

# CMA STUDENT E-Bulletin

VOL 11 | NO. 01 | JANUARY 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, enrolls 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, 112 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 सदगमय  
तमसोमा ज्योतिर् गमय  
मृत्योर्मा मृतं 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

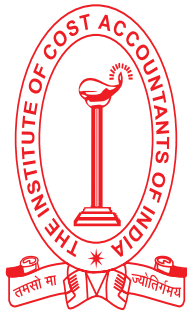
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# CHAIRMAN'S COMMUNIQUE

**Dear CMA Students,**

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

At ICAI, 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 ICAI, 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, ICAI**

# 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

### MULTIPLE CHOICE QUESTIONS (MCQ)

1. The primary purpose of business law is to:
  - a) Promote monopoly
  - b) Regulate business relationships
  - c) Eliminate competition
  - d) Control imports
2. Which of the following is NOT a source of law in India?
  - a) Customs
  - b) Judicial precedents
  - c) Personal opinions of judges
  - d) Legislation
3. A contract without consideration is:
  - a) Always valid
  - b) Void
  - c) Illegal
  - d) Enforceable
4. An agreement enforceable by law becomes:
  - a) Promise
  - b) Contract
  - c) Offer
  - d) Proposal
5. Which element ensures free consent in a contract?
  - a) Coercion
  - b) Misrepresentation
  - c) Undue influence
  - d) Absence of fraud
6. When both parties are under a mistake of fact essential to agreement, the contract is:
  - a) Valid
  - b) Voidable
  - c) Void
  - d) Illegal
7. An offer lapses after:
  - a) Acceptance
  - b) Revocation
  - c) Expiry of time
  - d) All of the above
8. Acceptance must be:
  - a) Conditional
  - b) Absolute and unqualified
  - c) Partial
  - d) Silent
9. A minor's agreement is:
  - a) Voidable
  - b) Valid
  - c) Void ab initio
  - d) Illegal
10. Quasi contracts are based on:
  - a) Agreement
  - b) Equity
  - c) Tort
  - d) Crime
11. Consideration must move at the desire of:
  - a) Promisor
  - b) Promisee
  - c) Any third party
  - d) Government
12. An agreement in restraint of marriage is:
  - a) Valid
  - b) Void
  - c) Voidable
  - d) Legal
13. The capacity to contract requires:
  - a) Majority age
  - b) Sound mind
  - c) Not disqualified by law
  - d) All of the above
14. A contract caused by undue influence is:
  - a) Void
  - b) Voidable
  - c) Illegal
  - d) Enforceable
15. Communication of acceptance is complete against the proposer when:
  - a) It is written
  - b) It is posted
  - c) It is received
  - d) It is understood

16. An invitation to offer is:
  - a) A valid contract
  - b) A type of acceptance
  - c) Not an offer
  - d) Illegal proposal
17. A contingent contract depends upon:
  - a) Performance of promise
  - b) Occurrence of uncertain event
  - c) Time
  - d) Agreement
18. Liquidated damages refer to:
  - a) Uncertain compensation
  - b) Pre-estimated compensation
  - c) Penalty
  - d) Fine
19. Discharge of contract by mutual agreement includes:
  - a) Novation
  - b) Rescission
  - c) Alteration
  - d) All of the above
20. Which agreement is expressly void?
  - a) Agreement with consideration
  - b) Agreement in restraint of trade
  - c) Agreement with free consent
  - d) Agreement with lawful object
21. Fraud includes:
  - a) Suggestion of untrue fact
  - b) Active concealment
  - c) Promise without intention to perform
  - d) All of the above
22. The doctrine of privity of contract means:
  - a) Only parties can sue
  - b) Anyone can sue
  - c) Third party can enforce
  - d) Government approval required
23. An agreement enforceable at the option of one party is:
  - a) Void
  - b) Voidable
  - c) Illegal
  - d) Unlawful
24. Performance of a contract may be:
  - a) Actual
  - b) Attempted
  - c) Both A and B
  - d) None
25. Effective communication primarily aims at:
  - a) Speaking fluently
  - b) Transferring information clearly
  - c) Using technical words
  - d) Writing long messages
26. Noise in communication refers to:
  - a) Loud sound only
  - b) Any barrier that distorts message
  - c) Silence
  - d) Feedback
27. Upward communication flows:
  - a) From superiors to subordinates
  - b) From subordinates to superiors
  - c) Between departments
  - d) Outside organization
28. The 7 C's of communication include:
  - a) Clarity
  - b) Courtesy
  - c) Completeness
  - d) All of the above
29. Non-verbal communication includes:
  - a) Reports
  - b) Emails
  - c) Body language
  - d) Circulars
30. Feedback in communication helps to:
  - a) Delay message
  - b) Confirm understanding
  - c) Increase noise
  - d) Avoid clarity

**Answer:**

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

## Topic

Fundamentals  
of Financial  
Accounting -

Module 1:  
Accounting  
Fundamentals

Module 2:  
Accounting for  
Special Transactions

Module 3:  
Preparation of Final  
Accounts

Fundamentals of  
Cost Accounting -

Module 4:  
Fundamentals of  
Cost Accounting

## FOUNDATION

### Paper-2

Fundamentals of  
Financial and Cost  
Accounting (FFCA)

1. Which of the following is not a concept of accounting?
  - (A) Dual aspect concept;
  - (B) Periodicity concept,
  - (C) Accounting cycle concept;
  - (D) Matching concept
2. On purchase of old furniture, ₹2,000 incurred on freight charges should be debited to
  - (A) Freight A/c;
  - (B) Trading A/c;
  - (C) Wages A/c;
  - (D) Furniture A/c
3. Which of the following documents is not required for preparing the Bank Reconciliation Statement?
  - (A) Bank pass book;
  - (B) Bank statement;
  - (C) Trial Balance;
  - (D) Cash book
4. Prepaid insurance is, by nature, a
  - (A) Direct expense;
  - (B) Nominal account;
  - (C) Tangible asset;
  - (D) Representative personal account
5. Original cost of a machine is 1,26,000 and rate of depreciation is 10% per annum, then the depreciation of the machine for 2nd year under Written Down Value Method will be
  - (A) ₹9,600;
  - (B) ₹10,800;
  - (C) ₹ 11,340;
  - (D) ₹13,140
6. A sum of 2,50,000 was paid as compensation to an employee who was retrenched. It is a
  - (A) Revenue expenditure;
  - (B) Deferred revenue expenditure;
  - (C) Capital expenditure;
  - (D) Appropriation of profits
7. Equipment Dealer, sold equipment on credit basis to Mr. Arora should be recorded in
  - (A) Sales day book;
  - (B) Cash book;
  - (C) General journal;
  - (D) Bills receivable book
8. Which of the following asset is considered to be non-depreciating?
  - (A) Land;
  - (B) Building;
  - (C) Plant;
  - (D) Fixtures
9. Joint Venture account is of the nature of
  - (A) Personal Account;
  - (B) Real Account;
  - (C) Nominal Account;
  - (D) Suspense Account
10. When consignor send goods to consignee he prepares and send a
  - (A) Debit note;
  - (B) Account sales;
  - (C) Proforma invoice;
  - (D) Sales invoice
11. D of Delhi sends out certain goods to K of Kolkata at cost plus 25%. 50% of the goods received by K is sold at 3,52,000 at 10% above Invoice Price. The Invoice Value of goods send out is Rs. ....
  - (A) 6,33,600;
  - (B) 7,04,000;
  - (C) 3,20,000;
  - (D) 6,40,000
12. At the end of the accounting year the balance of Nominal accounts are transferred to
  - (A) Trading Account only;
  - (B) Profit and Loss Account only;
  - (C) Trading and Profit & Loss Account;
  - (D) Balance Sheet
13. Under the Permanence Approach of Marshalling,
  - (A) most liquid assets are reflected first in the Balance Sheet;
  - (B) fixed assets comes before the current assets in the Balance Sheet;
  - (C) fixed assets comes after the current assets in the Balance Sheet;
  - (D) non-current liabilities comes after the current liabilities in the Balance Sheet

14. Which of the following is not a component of the financial statements of a sole proprietorship business?
- (A) Profit & Loss Account ;  
 (B) Balance Sheet;  
 (C) Trading Account ;  
 (D) Receipts and Payments Account
15. The Manufacturing account is prepared
- (A) ascertain gross profit;  
 (B) ascertain the cost of goods manufactured;  
 (C) ascertain profit or loss on the goods manufactured;  
 (D) ascertain the cost of goods sold
16. Capital Fund of a non-profit organisation is also known as
- (A) Equity;  
 (B) Accumulated Fund;  
 (C) Finance Reserve  
 (D) Cash Fund
17. Which of the following items are shown in the Income and Expenditure Account?
- (A) Both items of capital and revenue nature :  
 (B) Only items of capital nature;  
 (C) Only items of revenue nature which are received during the period of accounts ;  
 (D) Only items of revenue nature pertaining to the period of accounts
18. .... is a representation of inter-relationship between three important aspects of accounting namely, Liabilities Assets, and Equity.
- (A) Chart of Accounts;  
 (B) Accounting Equation;  
 (C) Trial Balance;  
 (D) Statement of Changes in Equity
19. Purchase Book records the transactions related to
- (A) all types of purchases;  
 (B) all purchases of goods;  
 (C) all types of credit purchases;  
 (D) credit purchases of goods only
20. Expenses paid but not accrued means
- (A) Capital expenses;  
 (B) Outstanding expenses;  
 (C) Prepaid expenses;  
 (D) Cash
21. Sale of goods on credit will:
- (A) Increase assets and increase capital;  
 (B) Increase liabilities;  
 (C) Decrease assets;  
 (D) Decrease capital
22. CAS ( Cost Accounting Standard ) 9 is related to –
- (A) Captive consumption;  
 (B) Packing Material Cost;  
 (C) Repairs and Maintenance Cost;  
 (D) Direct Expenses
23. Which of the following is a part of both Prime Cost and Conversion Cost ?
- (A) Direct Material;  
 (B) Indirect Labour;  
 (C) Direct Labour;  
 (D) All of these
24. From the information given, find value of purchases of Raw Material - Raw Material consumed ₹53,000, closing stock ₹9,000 and opening stock ₹6,000
- (A) ₹53,000;  
 (B) ₹56,000;  
 (C) ₹50,000;  
 (D) ₹68,000
25. Direct wages ₹2,46,000 and Factory Cost ₹5,60,000. If the ratio of Direct Wages and Factory Overhead is 3:1, then Direct Material cost will be –
- (A) ₹3,14,000;  
 (B) ₹3,96,000;  
 (C) ₹3,73,000;  
 (D) ₹2,32,000

26. Direct expenses are also known as:
- (A) Overhead Expenses;
  - (B) Manufacturing Expenses;
  - (C) Administrative Expenses;
  - (D) Chargeable Expenses
27. Which one is 'False'
- (A) Fixed costs per unit increase with increase in output;
  - (B) Out of pocket costs involve payment to outsiders;
  - (C) Rent on own building is imputed cost;
  - (D) Tender is an estimation of selling price
28. Prime Cost includes
- (A) Direct Material+Direct Labour+Direct Expenses;
  - (B) Direct Labour + Overheads;
  - (C) Direct Material + Overheads;
  - (D) Factory Overheads only
29. Variable cost per unit is
- (A) Constant;
  - (B) Increasing;
  - (C) Decreasing;
  - (D) Fluctuating randomly
30. Contribution =
- (A) Sales – Fixed Cost;
  - (B) Sales – Variable Cost;
  - (C) Fixed Cost – Variable Cost;
  - (D) Profit – Variable Cost

**Answer:**

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

## Topic

Fundamentals  
of Business  
Mathematics -

Module 1:  
Arithmetic

Fundamentals of  
Business Statistics -

Module 4:  
Statistical  
Representation of  
Data

## FOUNDATION

### Paper-3

Fundamentals  
of Business  
Mathematics and  
Statistics (FBMS)

In this issue we will carry out MCQs on Arithmetic and Statistical Representation of data--Refer Module 1 and Module 4 of Study guide.

- The ratio of ages of A and B is 4:5. After 8 years, the ratio becomes 6: 7. What is the present age of A?
  - 16
  - 24
  - 32
  - 40
- The ratio of incomes of A and B is 3: 5 and the ratio of their expenditures is 2:3. If each saves R2000, what is the income of A?
  - R6000
  - R9000
  - R12000
  - R15000
- If  $a : b = 2 : 3$  and  $b : c = 4 : 5$ , then  $a : b : c = ?$ 
  - 2 : 3 : 5
  - 4 : 6 : 5
  - 8 : 12 : 15
  - 6 : 9 : 10
- If  $x$  varies directly as  $y$  and  $x = 24$  when  $y = 8$ , what will be the value of  $x$  when  $y = 15$ ?
  - 30
  - 36
  - 40
  - 45
- If  $x$  varies inversely as  $y$ , and  $x = 20$  when  $y = 6$ , then what is  $x$  when  $y = 15$ ?
  - 8
  - 6
  - 10
  - 12
- A mixture contains milk and water in the ratio 5 : 3. How much water must be added to 32 litres of the mixture so that the ratio becomes 1 : 1?
  - 6 litres
  - 8 litres
  - 10 litres
  - 12 litres
- A car travels 60 km in 1 hour 30 minutes. What is its average speed?
  - 30 km/h
  - 40 km/h
  - 45 km/h
  - 50 km/h
- A train 200 m long crosses a pole in 10 seconds. What is its speed?
  - 54 km/h
  - 60 km/h
  - 72 km/h
  - 90 km/h
- A person travels 30 km at 60 km/h and returns at 40 km/h. What is the average speed for the whole journey?
  - 48 km/h
  - 50 km/h
  - 52 km/h
  - 55 km/h
- Two trains moving in opposite directions at 54 km/h and 72 km/h cross each other in 10 seconds. If the length of one train is 120 m, what is the length of the other?
  - 180 m
  - 200 m
  - 230 m
  - 250 m
- A man walks at 5 km/h and reaches his office 10 minutes late. If he walks at 6 km/h, he reaches 5 minutes early. What is the distance to the office?
  - 4 km
  - 5 km
  - 6 km
  - 7 km
- Two cities are 300 km apart. Two cars start simultaneously from both cities towards each other at 60 km/h and 40 km/h. After how many hours will they meet?
  - 2
  - 2.5
  - 3
  - 4

13. Statistical representation of data primarily helps to:
- Increase the amount of data
  - Simplify and present data in an understandable form
  - Eliminate errors in data
  - Replace data collection
14. The process of presenting data in rows and columns is called:
- Diagrammatic representation
  - Tabulation
  - Classification
  - Graphical analysis
15. Which of the following is not a type of diagrammatic representation?
- Bar diagram
  - Pie chart
  - Histogram
  - Pictogram
16. A pie chart is most suitable for showing:
- Trends over time
  - Comparison between variables
  - Proportion of components in a whole
  - Frequency distribution
17. A simple bar diagram is used to represent:
- One variable only
  - Two variables simultaneously
  - Percentage data
  - Continuous data
18. A multiple bar diagram is mainly used to:
- Show distribution of continuous data
  - Compare two or more related variables
  - Represent percentage distribution
  - Show cumulative frequencies
19. Which diagram is used when relative percentages are to be compared?
- Component bar diagram
  - Percentage bar diagram
  - Simple bar diagram
  - Pictogram
20. A pictogram represents data using:
- Mathematical formulas
  - Tables Symbols or pictures
  - Frequency curves
  - Symbols or pictures
21. Which graphical method is most suitable for continuous frequency distribution?
- Pie chart
  - Simple bar diagram
  - Histogram
  - Pictogram
22. A frequency polygon is constructed by:
- Joining midpoints of class intervals with straight lines
  - Joining highest frequencies
  - Plotting cumulative frequencies
  - Plotting percentages only
23. An Ogive curve is used to represent:
- Frequency distribution
  - Relative frequencies
  - Cumulative frequency distribution
  - Percentage distribution
24. Which graph is commonly used to identify the median graphically?
- Histogram
  - Frequency polygon
  - Ogive
  - Pie chart
25. A histogram differs from a bar diagram because:
- Bars are separated in a histogram
  - Histogram is used for categorical data
  - Histogram shows percentages only
  - Bars touch each other in a histogram
26. Which diagram is most appropriate to show trend of sales over several years?
- Pie chart
  - Line graph
  - Pictogram
  - Component bar diagram

27. In a component bar diagram, each bar represents:
- Total value divided into components
  - Only one variable
  - Continuous data
  - Cumulative frequencies
28. Which representation is most suitable for presenting large amounts of numerical data clearly?
- Tabulation
  - Pictogram
  - Pie chart
  - Diagram
29. A stem-and-leaf plot is useful because it:
- Eliminates raw data
  - Shows cumulative frequency
  - Shows only percentages
  - Shows exact data values along with distribution
30. One major advantage of graphical representation of data is that it:
- Eliminates need for numerical data
  - Makes comparison easy and quick
  - Increases complexity of data
  - Removes variability

**Answer:**

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

**Suggestions:**

*The study guide needs to be read 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 gathered from studying guide book to understand the correct answer of each question. Formula used here are all covered in study guide. Hints given for calculus portion.*

*Best Wishes.*

## Topic

Fundamentals of  
Business Economics -

Module 1 :  
Basic Concepts

Fundamentals of  
Management -

Module 5:  
Fundamentals of  
Management

## FOUNDATION

### Paper-4

Fundamentals of  
Business Economics  
and Management  
(FBEM)

**Let us start our Mock Test.****I. Choose the correct answer:**

1. Who was the founder of the scarcity definition of economics?
  - A. Samuelson
  - B. Marshall
  - C. Robbins
  - D. Smith
2. A point below the PPF curve indicates
  - A. Full employment
  - B. Under employment
  - C. Equilibrium
  - D. None of the above
3. When AP is rising, MP will
  - A. Rise
  - B. Fall
  - C. Change but Nothing definite can be said about the direction
  - D. None of the above
4. When TP is rising, then
  - A.  $MP=0$
  - B.  $MP<0$
  - C.  $MP>0$
  - D. None of the above
5. Market demand function is influenced by
  - A. Money income of the consumer
  - B. The demographic structure of the country
  - C. Consumer's preference
  - D. All of the above
6. Market demand curve for a commodity can be derived from
  - A. Horizontal summation of individual demand curves
  - B. Vertical summation of individual demand curves
  - C. Cumulative summation of individual demand curves
  - D. None of the above
7. An increase in the price of a commodity, when demand is inelastic, causes the total expenditure of the consumer on that commodity
  - A. To rise
  - B. To fall
  - C. To remain unchanged
  - D. None of the above
8. If the demand curve takes the shape of a rectangular hyperbola, then it implies
  - A. Elastic demand
  - B. Inelastic demand
  - C. Unitary elastic demand
  - D. None of the above
9. The demand for a commodity which can be put to a variety of uses will be
  - A. Relatively elastic
  - B. Relatively inelastic
  - C. Unitary elastic
  - D. None of the above
10. Steeper demand curve implies
  - A. Relatively elastic demand
  - B. Relatively inelastic demand
  - C. Perfectly elastic demand
  - D. None of the above
11. At higher prices the price elasticity of demand for the commodity will be
  - A. Relatively elastic
  - B. Relatively inelastic
  - C. Unitary elastic
  - D. None of the above
12. The price elasticity of demand is unitary at
  - A. The middle point of the linear demand curve
  - B. The top of that demand curve
  - C. The bottom of that demand curve
  - D. None of the above

13. For an inferior good the value of income elasticity of demand is
- Positive
  - Negative
  - Unity
  - Zero
14. For the increase in demand
- The demand curve will shift leftward
  - The demand curve will shift rightward
  - Along the same demand curve the consumer will move from top to bottom
  - None of the above
15. For a normal demand curve the MR curve will
- Appear below the demand curve
  - Appear above the demand curve
  - Be parallel to the demand curve
  - None of the above
16. SMC is equal to the
- Change in LMC
  - Change in TFC
  - Change in TVC
  - None of the above
17. When LAC is minimum then,
- $LAC=LMC$
  - $LAC<LMC$
  - $LAC>LMC$
  - None of the above
18. When plant size is optimal for any particular level of output, then
- $SMC<LMC$
  - $SMC>LMC$
  - $SMC=LMC$
  - None of the above
19. Money market is controlled by
- SEBI
  - RBI
  - IDBI
  - None of the above
20. Capital market is controlled by
- ICICI
  - RBI
  - IDBI
  - SEBI
21. When inflation is created by a rise in wages, it is called
- Demand pull inflation
  - Cost push inflation
  - Mark-up inflation
  - None of the above
22. There will be more organizational levels which in turn may impede communication, if the span of control is
- Wide
  - Narrow
  - Optimum
  - None of the above
23. The supervisory load may become too heavy if the span of control is
- Wide
  - Narrow
  - Optimum
  - None of the above
24. Responsibility can be assigned to
- Human being
  - Non-living objects
  - Both A and B
  - None of the above
25. Which one of the following is absolute and cannot be delegated
- Authority
  - Accountability
  - Responsibility
  - None of the above

26. Responsibility may be defined in terms of
- Functions
  - Targets
  - Goals
  - All of the above
27. Responsibility flows in
- Downward direction
  - Upward direction
  - All directions
  - None of the above
28. Subordinate is always responsible to his
- Peers
  - Foreman
  - Management
  - Superior
29. Authority is the right to give orders and the power to exact obedience defined by
- Barnard
  - Fayol
  - Strong
  - Louise Allen
30. Which theory is also called traditional authority theory
- The acceptance of authority theory
  - The formal authority theory
  - The competence theory
  - The organization theory

**Answer:**

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

*So, friends!!*

*Hope you have enjoyed the mock test thoroughly.*

*Please do not consult the key before you have finished solving all the problems. Try to maintain a record of your performance in different mock tests. This will go a long way to help you in preparing for the exam.*

*All the best !!!*

# CMA INTERMEDIATE COURSE

Syllabus 2022

## Topic

Module 2:  
Indian Contracts  
Act, 1872

INTERMEDIATE

Group I - Paper-5

Business Laws and  
Ethics (BLE)

## Legal Framework and Commercial Relevance of Contracts of Guarantee in India

### Introduction

Credit transactions constitute a fundamental aspect of contemporary economic systems. Both businesses and individuals often utilize borrowed capital to finance investments, facilitate expansion, and address working capital needs. Nevertheless, lending inherently entails the possibility of default by the borrower. In order to mitigate this risk, legal frameworks establish mechanisms that offer enhanced protection to creditors. Among these mechanisms is the contract of guarantee, which is regulated by Sections 126 to 147 of the Indian Contract Act, 1872.

A contract of guarantee provides that, should the principal debtor default, a third party designated as the surety will satisfy the outstanding obligation. The involvement of a surety reinforces creditor confidence and promotes the stability and efficiency of financial markets.

### Meaning and Structure of Contract of Guarantee

A contract of guarantee is defined as an agreement to perform the promise or discharge the liability of a third party in the event of default. The individual who provides the guarantee is referred to as the surety, the party whose obligation is guaranteed is known as the principal debtor, and the party in whose favor the guarantee is extended is termed the creditor.

This contractual arrangement creates a tripartite legal relationship. The principal debtor bears primary liability, whereas the surety's liability is contingent upon the occurrence of default by the principal debtor. Upon such default, the surety becomes legally obligated to the creditor.

This structure aims to enhance the creditor's financial security while simultaneously facilitating access to credit for the debtor.

### Essential Elements of a Valid Guarantee

A valid contract of guarantee must satisfy several essential legal requirements.

First, there must exist a legally enforceable primary obligation. If the principal debtor is not legally liable, the surety's liability cannot arise, as the guarantee is predicated upon the validity of the underlying obligation.

Second, consideration must be present. According to the Act, any benefit conferred upon the principal debtor constitutes sufficient consideration for the surety. For instance, when a loan is granted on the basis of a guarantee, the advancement of credit serves as valid consideration for the surety's undertaking.

Third, the guarantee must be entered into with free and informed consent. Any contract induced by fraud or misrepresentation may be rendered voidable.

Fourth, the guarantee must be explicitly communicated to, and accepted by, the creditor.

These requirements ensure that guarantees arise from voluntary and informed agreement, thereby safeguarding against coercion or misunderstanding.

### Case Study: Liability of Surety

An important judicial interpretation of the surety's liability is illustrated in *Bank of Bihar v. Damodar Prasad* (1969).

### Case Background

In this case, a debtor obtained a loan from a bank, and the defendant acted as surety for repayment. When the debtor defaulted, the bank sued both the debtor and the surety. The surety argued that the bank should first exhaust remedies against the principal debtor before proceeding against him.

### Court Decision

The Supreme Court rejected this argument and held that the liability of the surety is coextensive with that of the principal debtor unless the contract provides otherwise. Therefore, the creditor can directly proceed against the surety without first suing the debtor.

### Significance

This case clarified a key principle: although the surety's liability is secondary, the creditor is not obligated to pursue the debtor before proceeding against the surety. The decision reinforced the effectiveness of guarantees as security instruments in financial transactions.

### Continuing Guarantees and Revocation

The Act also recognizes continuing guarantees, which apply to a series of transactions instead of a single obligation. These guarantees are frequently used in banking relationships involving repeated transactions by a borrower.

A continuing guarantee may be revoked by the surety by providing notice to the creditor or upon the death of the surety.

### Case Study: Continuing Guarantee

The principle of continuing guarantees was examined in *Offord v. Davies* (1862).

### Case Background

In this English case, the defendant had guaranteed payment for goods supplied on credit to a third party. Later, he revoked the guarantee before further credit transactions took place.

### Court Decision

The court held that a continuing guarantee can be revoked for future transactions through notice to the creditor.

### Significance

This decision clarified that, while a surety remains liable for transactions that have already occurred, it cannot be held responsible for future transactions after the guarantee is revoked. The surety undertakes significant liability; the law provides several rights to ensure fairness.

One important right is the right of subrogation, which allows the surety, after paying the creditor, to assume the creditor's rights against the principal debtor.

Another right is the right of indemnity, meaning the principal debtor must reimburse the surety for any payments made under the guarantee.

### Case Study: Rights of Surety

The rights of the surety were discussed in *State Bank of Saurashtra v. Chitranjan Rangnath Raja* (1980).

### Case Background

In this case, the creditor bank released certain securities held against the principal debtor without the surety's consent.

### Court Decision

The Supreme Court held that the surety is entitled to the benefit of securities held by the creditor. If the creditor releases or loses such securities without the surety's consent, the surety may be discharged to that extent.

### Significance

The decision emphasized that creditors must exercise caution when dealing with securities, as their actions may affect the rights of the surety.

### Discharge of Surety

A surety may be discharged from liability in several circumstances.

One situation arises when there is a material alteration in the terms of the contract between the creditor and the principal debtor without the surety's consent.

In *Holme v. Brunskill* (1878), the court held that any material change in the contract between the creditor and debtor without the surety's consent discharges the surety from liability.

This principle ensures that the surety is not compelled to assume risks beyond those originally agreed upon.

### Importance of Guarantees in Modern Commerce

Contracts of guarantee occupy a prominent position in banking, corporate finance, and commercial transactions. Financial institutions frequently mandate personal guarantees prior to extending credit facilities, especially in instances where prospective borrowers possess inadequate assets or limited credit histories.

Likewise, guarantees are routinely incorporated into construction contracts, international trade agreements, and corporate financing arrangements to ensure the fulfillment of contractual obligations. The utilization of performance and financial guarantees serves to mitigate risk and bolster confidence among parties engaged in complex commercial undertakings.

### Conclusion

The contract of guarantee constitutes a fundamental legal instrument underpinning the operation of credit systems and commercial relationships. By engaging a surety who assumes responsibility for the obligations of another, the legal framework affords enhanced security to creditors and facilitates borrowers' access to financial resources.

Judicial pronouncements have been instrumental in defining the scope of the surety's liability, rights, and conditions for discharge. Such judicial interpretations ensure the effective functioning of guarantees while upholding principles of fairness among all parties. In contemporary economic systems, the contract of guarantee plays an important role in building trust, stability, and efficiency in financial transactions.

## Law of Agency under the Indian Contract Act, 1872: Principles, Authority and Judicial Perspectives

### Introduction

Modern commercial transactions often require individuals and organizations to conduct business through representatives instead of managing every activity personally. In today's complex economic environment, enterprises operate across various locations, markets, and sectors. Therefore, it is typically impractical for principals to supervise each negotiation, contract, or operational task directly. Delegation of authority thus becomes essential for maintaining organizational efficiency.

Sections 182 to 238 of the Indian Contract Act, 1872, provide the legal framework for agency relationships. These provisions define the relationship between principal and agent, outline the scope of the agent's authority, and specify the rights and liabilities resulting from the agent's actions. This framework ensures that acts performed by the agent within their authority are binding on the principal, thereby supporting efficient commercial operations.

The law of agency, by enabling representation and delegation, supports the growth of commercial activities and enhances trust among parties in the marketplace.

### Concept and Nature of Agency

An agent is an individual employed to perform acts for another or to represent another in dealings with third parties. The person for whom these acts are performed is called the principal. The principal-agent relationship is fundamentally based on authority and trust.

The central feature of an agency relationship is that the agent acts on behalf of the principal, and the acts performed by the agent's authority create legal obligations for the principal. Thus, the agent's conduct directly affects the principal's rights and liabilities. In contracts, the existence of authority to act on behalf of the principal is sufficient to establish agency. This principle enables agency relationships to arise even in informal situations where no payment or remuneration is involved.

Another key feature is that the agent typically acts in the principal's best interests, not for personal gain. The agent's authority must be exercised in good faith and in accordance with the principal's instructions.

### Creation of Agency

Agency relationships can arise in various ways, depending on the circumstances and the parties' intentions.

The most common method is agency by agreement, where the principal explicitly appoints the agent to act on his behalf. This appointment may be made through a written contract or an oral agreement. For instance, a

company may appoint a sales agent to represent it in a particular region.

An agency may also arise by implied authority, inferred from the parties' conduct or the nature of their relationship. For instance, a business manager is generally presumed to have the authority to conduct routine company transactions.

Agency by ratification occurs when a person acts without authority, but the principal subsequently approves or adopts the act. Upon ratification, the act becomes legally binding as if the agent had authority from the outset.

Agency may also arise in exceptional situations through agency by necessity, where a person acts on behalf of another to protect the latter's interests during emergencies when communication with the principal is not possible.

### Case Study: Agency by Ratification

The concept of ratification was illustrated in *Bolton Partners v. Lambert* (1889).

In this case, an agent accepted an offer on the principal's behalf without proper authority. The principal later approved the agent's action and ratified the contract.

The court held that ratification operates retroactively to the time of the original act. Thus, once the principal ratifies the agent's action, the contract is valid as if the agent had authority from the outset.

This case established an important principle in agency law. Ratification can validate an otherwise unauthorized act of an agent, provided that the principal adopts the act within a reasonable time and with full knowledge of the material facts.

### Authority of the Agent

The authority granted to an agent determines the extent to which the principal is bound by the agent's actions when dealing with third parties. The law recognizes several types of authority.

Express authority is authority explicitly granted by the principal, either in writing or orally. The agent must act strictly within the boundaries set by the principal.

Implied authority encompasses powers necessary to fulfill the express authority granted to the agent. Such powers arise from the nature of the assigned work or from customary business practices. Another important concept is apparent or ostensible authority. This arises when the principal's conduct leads third parties to believe that the agent has authority to act, even if such authority has not been expressly granted. In such cases, the principal may still be bound by the agent's actions to protect the interests of innocent third parties.

### Case Study: Apparent Authority

A significant case explaining apparent authority is *Freeman & Lockyer v. Buckhurst Park Properties Ltd.* (1964).

In this case, a company director who had not been formally appointed as managing director acted as if he had authority to enter into contracts on behalf of the company. The company permitted him to continue in this role for an extended period.

The court held that the company was bound by his actions because it allowed him to appear to possess such authority.

This case established the doctrine of apparent or ostensible authority, which protects third parties who rely on the principal's representation concerning the agent's authority.

### Duties of the Agent

Agents are subject to several duties toward their principals, as the agency relationship is fundamentally based on trust and confidence.

A principal duty is the duty of loyalty, which requires the agent to act honestly and prioritize the principal's best interests. Agents must avoid situations where their personal interests conflict with those of the principal.

Agents must comply with lawful instructions issued by the principal and may not exceed the authority granted to them. If an agent acts beyond their authority, the principal may refuse to accept responsibility for those actions.

Another important duty is maintaining accurate accounts. Agents must keep precise records of all transactions conducted on behalf of the principal and provide the principal with complete information upon request.

Agents are expected to exercise reasonable care, skill, and diligence in performing their duties. If an agent acts negligently and causes loss to the principal, the agent may be held liable for any resulting damages.

### Case Study: Duty of Agent

In *Keppel v. Wheeler* (1927), an estate agent was instructed to sell property on behalf of the principal. After agreeing to a sale at a specified price, the agent later received a higher offer but failed to inform the principal.

The court determined that the agent breached his duty by failing to act in the principal's best interests. The agent was obligated to inform the principal of the higher offer to enable an informed decision. This case illustrates that agents must prioritize their principals' interests and must not withhold information that could benefit the principal.

### Rights of the Agent

Agents possess specific rights that protect their interests and promote fairness within the agency relationship. A principal right is the entitlement to remuneration or commission for services rendered, particularly when the agency relationship is established for commercial purposes. Agents are also entitled to reimbursement

for lawful expenses incurred while carrying out the principal's instructions. For example, if an agent incurs transportation or documentation costs during a transaction, the principal is obligated to reimburse those expenses. those expenses.

Another important right is the right of indemnity, which allows the agent to recover losses sustained while performing lawful acts within the scope of authority. This protection ensures that agents are not unfairly penalized for actions undertaken on behalf of the principal.

An agency relationship is not permanent and may terminate under various circumstances. occur through mutual agreement between the principal and the agent. Additionally, the principal may revoke the agent's authority at any time, subject to contractual terms. The agency may also terminate upon completion of its purpose or upon expiration of the period specified in the contract.

Furthermore, the agency relationship may end upon the death or insanity of either the principal or the agent, or in cases of the principal's insolvency. In certain cases, destruction of the agency's subject matter may also result in termination.

Termination ensures that the authority granted to agents does not persist indefinitely without the principal's consent or knowledge. Agency is fundamental to modern business structures. Large corporations operate through directors, managers, and employees who serve as agents of the organization. Without such representation, companies would be unable to conduct large-scale operations efficiently. Similarly, brokers, distributors, commission agents, and sales representatives act as intermediaries between businesses and customers in commercial markets. These agents facilitate organizational expansion into new regions and markets. Through delegation and representation, agency enables businesses to operate more efficiently, reduce operational burdens on principals, and expand commercial activities across multiple locations.

### Conclusion

The law of agency provides a comprehensive framework that enables individuals and organizations to conduct transactions through authorized representatives. By defining the authority, duties, and rights of agents and principals, the Indian Contract Act ensures that commercial dealings remain reliable and legally enforceable. It has further clarified these principles, ensuring that agency relationships operate fairly and protect the interests of principals, agents, and third parties. In modern commerce, the law of agency remains essential for facilitating efficient and trustworthy business operations. By enabling the delegation of authority and legal recognition of representation, the law of agency continues to support the effective functioning of contemporary economic systems.

## Topic

Module 1:  
Accounting  
Fundamentals

# INTERMEDIATE

## Group I - Paper-6

### Financial Accounting (FA)

## Bank Reconciliation Statement / Depreciation and Amortisation

### Bank Reconciliation Statement

A Bank Reconciliation Statement (BRS) is a document that matches the cash balance on a company's balance sheet to the corresponding amount on its bank statement. The purpose is to ensure the accuracy of financial records and to identify any discrepancies.

#### Steps to Prepare a Bank Reconciliation Statement

1. **Compare the opening balances:** Ensure the opening balance of the cash book matches the bank statement.
2. **Check deposits and withdrawals:** Verify that all deposits and withdrawals are recorded in both records.
3. **Identify outstanding checks:** List all checks issued but not yet cleared.
4. **Identify deposits in transit:** List all deposits recorded in the cash book but not yet credited by the bank.
5. **Adjust for bank errors:** Note any errors made by the bank and adjust accordingly.
6. **Adjust for company errors:** Correct any errors made in the company's records.
7. **Prepare the reconciliation statement:** Start with the bank statement balance, add deposits in transit, deduct outstanding checks, and adjust for any errors to arrive at the adjusted cash book balance.

#### Key Concepts

- **Cash Book:** Records all cash transactions.
- **Bank Statement:** Issued by the bank, showing all transactions in the bank account.
- **Outstanding Checks:** Checks that have been issued but not yet cleared by the bank.
- **Deposits in Transit:** Deposits recorded in the company's books but not yet credited by the bank.
- **Bank Errors:** Mistakes made by the bank in recording transactions.
- **Company Errors:** Mistakes made by the company in recording transactions.

#### Importance of Bank Reconciliation Statement

##### 1. Ensures Accuracy of Financial Records

- o **Detection of Errors:** Identifies discrepancies between the company's records and the bank's records, such as incorrect entries or omissions.
- o **Prevents Mistakes:** Helps prevent errors in financial statements by ensuring that the cash book and bank statement balances match.

##### 2. Fraud Prevention and Detection

- o **Identifies Unauthorized Transactions:** Helps spot unauthorized or fraudulent transactions by comparing the bank statement with the company's cash book.
- o **Mitigates Risk of Embezzlement:** Regular reconciliation reduces the risk of internal fraud or embezzlement.

##### 3. Effective Cash Management

- o **Accurate Cash Position:** Provides an accurate picture of the company's cash position, helping in effective cash flow management.
- o **Informed Decision-Making:** Enables better decision-making regarding cash requirements and investments.

##### 4. Improves Internal Control

- o **Accountability:** Enhances accountability by ensuring that all transactions are properly recorded and reconciled.
- o **Operational Efficiency:** Streamlines financial processes and improves operational efficiency by maintaining up-to-date records.

##### 5. Compliance and Auditing

- o **Regulatory Compliance:** Helps comply with regulatory requirements by maintaining accurate financial records.
- o **Audit Trail:** Provides a clear audit trail for external auditors, simplifying the auditing process.

##### 6. Prepares for Financial Reporting

- o **Accurate Financial Statements:** Ensures that financial statements accurately reflect the company's financial position.
- o **Transparency:** Enhances transparency and reliability of financial information provided to stakeholders.

A Bank Reconciliation Statement is crucial for maintaining the integrity and accuracy of a company's financial records. It plays a vital role in error detection, fraud prevention, effective cash management, improving internal controls, ensuring compliance, and preparing accurate financial statements. Regular reconciliation helps businesses maintain accurate records, make informed decisions, and provide transparent financial information to stakeholders.

**Example**

Suppose the bank statement shows a balance of ₹10,000, while the cash book shows ₹9,500. After comparing the two, you identify the following:

- Outstanding checks: ₹1,500
- Deposits in transit: ₹2,000
- Bank error (overcharge): ₹100
- Company error (under-recorded withdrawal): ₹400

**Bank Reconciliation Statement**

Particulars	Amount
Balance as per bank statement	₹10,000
Add: Deposits in transit	₹2,000
Less: Outstanding checks	₹1,500
Add: Bank error	₹100
Less: Company error	₹400
Adjusted cash book balance	₹10,200

**Depreciation and Amortisation**

Depreciation and amortization are accounting methods used to allocate the cost of tangible and intangible assets over their useful lives. These methods help in matching the cost of assets with the revenue they generate over time.

**Depreciation**

Depreciation is an accounting method used to allocate the cost of a tangible asset over its useful life. This systematic allocation helps reflect the usage, wear and tear, or obsolescence of the asset in the company's financial statements.

**Objectives of Depreciation**

- **Match Expenses with Revenue:** Ensures that the cost of an asset is matched with the revenue it generates over time.
- **Reflect True Asset Value:** Provides a more accurate representation of an asset's value on the balance sheet.
- **Financial Planning:** Helps in planning for the replacement of assets by spreading their cost over their useful life.

**Factors Affecting Depreciation**

- **Cost of the Asset:** The initial purchase price and any additional costs necessary to prepare the asset for use.
- **Useful Life:** The estimated period over which the asset will be productive.
- **Residual Value (Salvage Value):** The estimated value of the asset at the end of its useful life.
- **Depreciation Method:** The chosen method of calculating depreciation expense.

**Methods:**

- Straight-Line Method
- Declining Balance Method
- Units of Production Method
- Sum-of-the-Years-Digits Method

**Example:**

1. A company purchases a piece of machinery for \$15,000. The machinery has an estimated useful life of 5 years and a salvage value of \$3,000. Calculate the annual depreciation expense using the straight-line method.

$$\text{Depreciation Expense} = \frac{\text{Cost} - \text{Salvage Value}}{\text{Useful Life}}$$

$$\text{Depreciation Expense} = \frac{15,000 - 3,000}{5} = 2,400$$

2. An asset is purchased for ₹ 25,000 with no salvage value and a useful life of 4 years. Calculate the depreciation expense for the first two years using the double declining balance method.

$$\text{Depreciation Rate} = \frac{100\%}{\text{Useful Life}} \times 2 = \frac{100\%}{4} \times 2 = 50\%$$

**First Year:**

$$\text{Depreciation Expense} = \text{Book Value at Beginning of Year} \times \text{Depreciation Rate}$$

$$\text{Depreciation Expense} = 25,000 \times 50\% = 12,500$$

**Second Year:**

$$\text{Book Value at Beginning of Second Year} = \text{Cost} - \text{Accumulated Depreciation}$$

$$\text{Book Value} = 25,000 - 12,500 = 12,500$$

$$\text{Depreciation Expense} = 12,500 \times 50\% = 6,250$$

The depreciation expenses are ₹12,500 for the first year and ₹6,250 for the second year.

**Amortisation**

Amortization is the process of spreading the cost of an intangible asset over its useful life. This accounting method ensures that the expense related to the intangible asset is matched with the revenue it generates over time.

### Objectives of Amortization

- **Expense Allocation:** Spreads the cost of intangible assets over their useful lives.
- **Financial Accuracy:** Reflects the decline in value of intangible assets over time.
- **Revenue Matching:** Matches the cost of intangible assets with the revenue they help generate.

### Intangible Assets Subject to Amortization

- **Patents:** Exclusive rights to produce or sell an invention.
- **Copyrights:** Exclusive rights to reproduce and sell artistic or literary work.
- **Trademarks:** Rights to use a symbol, name, or logo.
- **Franchise Agreements:** Rights to operate a business using another company's name and systems.
- **Goodwill:** The value of a company's brand name, customer relationships, etc.

### Amortization Methods

- Straight-Line Method:
- Units of Production Method

### Impact of Amortization

- **Financial Statements:** Reduces net income on the income statement and the book value of intangible assets on the balance sheet.
- **Taxation:** Amortization expense is deductible for tax purposes, reducing taxable income.

### Example:

A company acquires a copyright for ₹1,00,000 with a useful life of 20 years and no residual value.

Amortization Expense =  $1,00,000/20 = ₹5,000$  per year

### Questions:

1. What is the main purpose of a Bank Reconciliation Statement?
  - a) To prepare financial statements
  - b) To match the company's cash book with the bank statement
  - c) To record all cash transactions
  - d) To reconcile outstanding invoices
2. Which of the following is an example of a deposit in transit?
  - a) A check issued but not yet cleared
  - b) A bank charge not recorded in the cash book
  - c) A deposit made but not yet credited by the bank
  - d) A loan repayment
3. What should be done if the bank statement shows an overcharge?
  - a) Record the overcharge in the cash book
  - b) Ignore the overcharge
  - c) Adjust the bank statement
  - d) Add the overcharge to the bank reconciliation statement
4. An outstanding check is:
  - a) A check recorded in the cash book but not yet cleared by the bank
  - b) A check that has been cleared by the bank but not recorded in the cash book
  - c) A check that has been issued and cleared
  - d) A check that has been cancelled
5. If the bank reconciliation statement shows an adjusted cash book balance higher than the bank statement balance, which of the following might be true?
  - a) There are outstanding checks
  - b) There are deposits in transit
  - c) The bank has made an error
  - d) The company has made an error
6. What is the primary purpose of depreciation?
  - a) To allocate the cost of an asset over its useful life
  - b) To increase the value of an asset over time
  - c) To match the revenue with the expenses in the same period
  - d) Both a and c
7. Which depreciation method allocates an equal amount of expense each year?
  - a) Declining Balance Method
  - b) Straight-Line Method
  - c) Units of Production Method
  - d) Sum-of-the-Years-Digits Method

8. How is accumulated depreciation reported in the financial statements?
- As an expense on the income statement
  - As a contra asset on the balance sheet
  - As a liability on the balance sheet
  - As a revenue on the income statement
9. What is the primary purpose of amortization?
- To allocate the cost of an intangible asset over its useful life
  - To increase the value of an intangible asset over time
  - To match the revenue with the expenses in the same period
  - Both a and c
10. Which of the following is an example of an intangible asset that would be amortized?
- Building
  - Equipment
  - Patent
  - Land

**Answer:**

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

## Topic

Module 1:  
Basics of Income  
Tax Act

INTERMEDIATE

Group I - Paper-7A

Direct Taxation (DT)

## Residential Status

In the realm of direct taxation, the liability to pay income tax in India does not merely depend on the citizenship of the taxpayer, but crucially on their 'Residential Status' during the relevant previous year. The Income-tax Act, 1961, explicitly establishes the rules for determining this status under Section 6, while Section 5 outlines the scope of total income (incidence of tax) based on this classification. This topic not only serves as the conceptual bedrock for understanding global income taxation but is also heavily tested through complex, case-based practical problems. Let us decode the step-by-step mechanism to determine residential status and its direct impact on taxability.

Determination of Residential status [Sec. 6]

Assessee	Condition to be a Resident	Condition to be an Ordinarily resident
Individual	<p>An individual is said to be a resident in India, if he satisfies any one of the following conditions -</p> <ol style="list-style-type: none"> <li>i) He is in India in the previous year for a period of 182 days or more [Sec. 6(1)(a)]; or</li> <li>ii) He is in India for a period of 60 days or more during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year [Sec. 6(1)(c)]</li> </ol> <p><u>Exceptions</u></p> <p>A. In the following cases, condition (ii) of sec. 6(1) [i.e. sec. 6(1)(c)] is irrelevant:</p> <ol style="list-style-type: none"> <li>a) An Indian citizen, who leaves India during the previous year for employment purpose.</li> <li>b) An Indian citizen, who leaves India during the previous year as a member of crew of an Indian ship.</li> </ol> <p>B. In case of an Indian citizen or a person of Indian origin comes on a visit to India during the previous year, and his total income, other than the income from foreign sources, exceeds ₹ 15 lakhs during the previous year then modified condition (ii) of sec. 6(1) is applicable i.e., he is in India for a period of 120 days or more (but less than 182 days) during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year.</p> <p>If such income does not exceed ₹ 15 lakhs, then condition (ii) of sec. 6(1) is irrelevant.</p> <p>C. If assessee has satisfied all the condition given u/s 6(1A), he is considered as deemed resident. The conditions are:</p> <ol style="list-style-type: none"> <li>a. He is a citizen of India</li> <li>b. His total income, other than the income from foreign sources, exceeds ₹15 lakhs during the previous year;</li> <li>c. He is not satisfying any of the basic conditions given u/s 6(1) [i.e., 182 days or 60 days + 365 days]; and</li> <li>d. He is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.</li> </ol>	<p>If a resident individual satisfies the following two additional conditions, he will be treated as resident &amp; ordinarily resident in India -</p> <ol style="list-style-type: none"> <li>a) He has been resident in India [as per sec. 6(1)] in at least 2 out of 10 previous years immediately preceding the relevant previous year; <u>and</u></li> <li>b) He has resided in India for a period of 730 days or more during 7 previous years immediately preceding the relevant previous year.</li> </ol> <p><u>Note:</u> If the assessee is considered as resident by virtue of 120 days + 365 days criteria or he is considered as deemed resident u/s 6(1A), then he is considered as not ordinarily resident in India.</p>

Assessee	Condition to be a Resident	Condition to be an Ordinarily resident
HUF	Management is wholly or partly situated in India	Karta satisfies both the conditions of sec. 6(6)
Company		
a) Indian company	Always resident	Not applicable
b) Other company	Place of effective management is in India	
Any other person	Management is wholly or partly situated in India	

**Example**

Determine the residential status in the following different cases:

Case	A	B	C	D	E	F	G	H
Citizenship	Foreign	India	India	India	Foreign	Foreign	India	Foreign
Is he person of Indian origin	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No
Total income (excluding income from foreign source) exceeds ₹ 15,00,000	Yes	No	Yes	Yes	Yes	Yes	No	No
Liable to pay tax in other country	No	No	No	Yes	No	No	No	No
Stay in India during the previous year	30	30	30	30	138	185	85	85
Stay in India during 4 years immediately preceding previous year	380	380	380	380	380	180	380	380
Are dual conditions given u/s 6(6) satisfied	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Residential Status	NR	NR	NOR	NR	NOR	ROR	NR	ROR
Note	1	2	3	4	5	6	7	8

1. He is not an Indian citizen, hence sec. 6(1A) is not applicable. Further his stay in India during the previous year does not exceed 120 days.
2. His total income does not exceed ₹ 15,00,000.
3. All conditions of sec. 6(1A) are satisfied.
4. He is liable to pay tax in other country.
5. His stay in India exceeds 120 days (but does not exceed 182 days)
6. He has satisfied one condition of sec. 6(1) [i.e. 182 days criteria] and dual conditions of sec. 6(6)
7. He is not satisfying any of the condition provided in sec. 6(1)
8. He has satisfied one condition of sec. 6(1) [i.e. 182 days criteria] and dual conditions of sec. 6(6)

**Incidence of Tax [Sec. 5]**

The following chart highlights the provisions of tax incidence in brief:

Nature of Income	Tax incidence in the case of		
	Resident & ordinarily resident	Resident but not ordinarily resident	Non resident
Income accrued or deemed to be accrued and received or deemed to be received in India	Taxable	Taxable	Taxable
Income accrued outside India but received or deemed to be received in India.	Taxable	Taxable	Taxable
Income accrued or deemed to be accrued in India but received outside India	Taxable	Taxable	Taxable
Income accrued and received outside India from a business controlled in or profession set-up in India.	Taxable	Taxable	Not taxable
Income accrued and received outside India from a business controlled or profession set-up outside India.	Taxable	Not taxable	Not taxable
Income accrued and received outside India in the previous year (it makes no difference if the same is later remitted to India).	Taxable	Not taxable	Not taxable
Income accrued and received outside India in any year preceding the previous year and later on remitted to India in current financial year.	Not taxable	Not taxable	Not taxable
<b>Note:</b> In case of resident assessee like company, firm etc. (other than Individual and HUF) in which there is no classification as 'Resident but not ordinarily resident', income accrued and received outside India from a business controlled or profession setup outside India shall be taxable.			

**Example**

Ram provides following details of income, calculate the income which is liable to be taxed in India for the A.Y.2026-27 assuming that –

a) He is an ordinarily resident	b) He is not an ordinarily resident	c) He is a non-resident.
Particulars		Amount
Salary received in India from a former employer of UK		1,40,000
Income from tea business in Nepal being controlled from India		10,000
Interest on company deposit in Canada (1/3 <sup>rd</sup> received in India)		30,000
Profit from a business in Mumbai controlled from UK		1,00,000
Profit for the year 2023-24 from a business in Tokyo remitted to India		2,00,000
Income from a property in India but received in USA		45,000
Income from a property in London but received in Delhi		1,50,000
Income from a property in London but received in Canada		2,50,000
Income from a business in Zambia but controlled from Turkey		10,000

**Solution**

Calculation of income liable to be taxed in India of Ram for the A.Y.2026-27

	<b>Resident &amp; ordinarily resident</b>	<b>Resident but not ordinarily resident</b>	<b>Non-resident</b>
Salary received in India from a former employer of UK	1,40,000	1,40,000	1,40,000
Income from tea business in Nepal being controlled from India	10,000	10,000	Nil
<u>Interest on company deposit in Canada -</u> - 1/3 <sup>rd</sup> received in India	10,000	10,000	10,000
- 2/3 <sup>rd</sup> received outside India	20,000	Nil	Nil
Profit from a business in Mumbai controlled from UK	1,00,000	1,00,000	1,00,000
Past Profit from a business in Tokyo remitted to India	Nil	Nil	Nil
Income from a property in India but received in USA	45,000	45,000	45,000
Income from a property in London but received in Delhi	1,50,000	1,50,000	1,50,000
Income from a property in London but received in Canada	2,50,000	Nil	Nil
Income from a business in Zambia but controlled from Turkey	10,000	Nil	Nil
<b>Income liable to tax in India</b>	<b>7,35,000</b>	<b>4,55,000</b>	<b>4,45,000</b>

In conclusion, accurately determining the residential status of an assessee is the indispensable first step before computing their taxable income. The core principle is simple yet profound: a Resident and Ordinarily Resident (ROR) is taxed on their global income, whereas a Non-Resident (NR) is taxed strictly on income sourced or received within India. The intermediate categories, such as Resident but Not Ordinarily Resident (RNOR), demand careful application of the law, especially when evaluating foreign businesses controlled from India or navigating the strict 'Deemed Resident' provisions. For aspiring Cost and Management Accountants, absolute conceptual clarity on Sections 5 and 6 is non-negotiable. A strong command over these provisions ensures not only exam readiness for Paper 7 but also builds the practical acumen required for robust cross-border tax planning and compliance in the corporate world.

## Topic

Module 4:  
Concept of Indirect  
Taxes

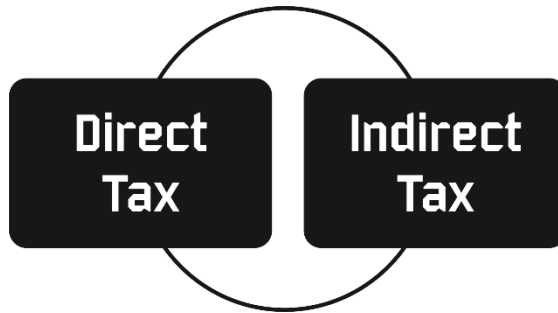
**INTERMEDIATE**

Group I - Paper-7B

Indirect Taxation  
(IDT)

## Concept of Indirect Tax

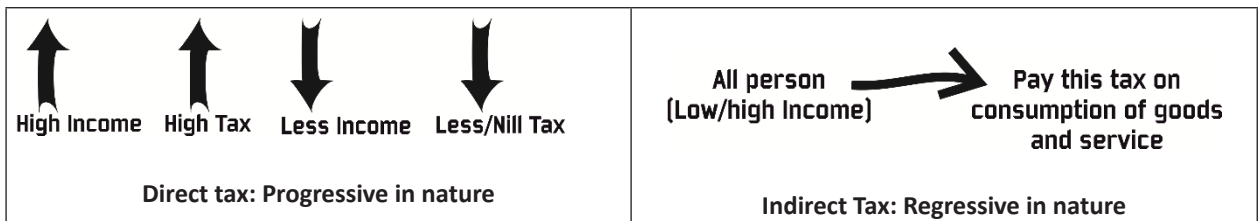
In any robust economy, taxation is the primary engine that drives public welfare and national infrastructure. While direct taxes visibly impact a taxpayer’s earned income, it is the ‘Indirect Tax’ that silently but significantly fuels the government’s revenue stream. Unlike income tax, indirect taxes are levied on the consumption of goods and services, seamlessly shifting the financial burden from the manufacturer or supplier to the ultimate consumer. This article explores the foundational principles, structural features, and the unique socio-economic impact of indirect taxes.



**Type of Taxation**

There are two types of taxes: Direct Tax and Indirect Tax

Tax, of which incidence and impact fall on the same person, is known as Direct Tax, such as Income Tax. On the other hand, tax, of which incidence and impact fall on two different persons, is known as Indirect Tax, such as GST, etc. It means, in the case of Direct Tax, tax is recovered directly from the assessee, who ultimately bears such taxes, whereas in the case of Indirect Tax, tax is recovered from the assessee, who passes such burden to another person & is ultimately borne by consumers of such goods or services.



### Features of Indirect Taxes

Indirect taxes are taxes that are levied on goods and services rather than on income or profits. These taxes are collected by an intermediary (such as a retailer or manufacturer) from the person who ultimately bears the economic burden of the tax (such as the consumer). Here are some key points about indirect taxes:

- ✿ Tax on goods and services: Indirect tax is levied at the time of supply or manufacture or purchase or sale or import or export of goods. Further, it is also levied on supply.
- ✿ Burden: Since the indirect tax is levied on the seller, it is recovered by the seller from the buyer. Thus, one can say that burden of indirect tax is shifted from seller to buyer and ultimately borne by consumers of such goods or services.
- ✿ Inflationary in nature: Cost of goods and services increases due to levy of indirect tax thus indirect taxes promote inflation.
- ✿ Social welfare: It is useful tool to promote social welfare by checking the consumption of harmful goods or sin goods through higher rate of tax.
- ✿ Wider Tax Base: Majority of goods and services are liable to indirect tax with very low threshold limits, so tax base is much wider in case of indirect tax in compare to direct tax.
- ✿ Regressive in Nature: All persons (rich or poor) will bear equal wrath of tax on goods or service consumed by them irrespective of their ability. In other words, indirect tax does not create any difference between rich and poor. Poor people are also required to pay equal percentage of tax on certain goods and service of mass consumption. Thus, it may increase the disparities between rich and poor.

- ✿ No pinch: Seller (the person on which indirect tax is levied) does not perceive a direct pinch of tax as it is recovered by him from the buyer and then he is paying to the Government. On the other hand, since it is inbuilt in the price of the goods, the ultimate payer (i.e., buyer) pay it without knowing that he is paying any tax to the Government.
- ✿ Examples of Indirect Taxes in India:
  - Goods and Services Tax (GST): A comprehensive indirect tax on the manufacture, sale, and consumption of goods and services throughout India, replacing multiple indirect taxes like VAT, excise duty, and service tax.
  - Customs Duty: Levied on goods imported into India, aimed at protecting domestic industries and generating revenue.
  - Excise Duty: Previously levied on the manufacture of goods within India, now largely subsumed under GST. However, Central Excise Duty continues to be levied on specified petroleum products and tobacco, while State Excise applies to alcoholic liquor for human consumption.

### Comparison Chart

Basis	Direct Tax	Indirect Tax
Meaning	Direct tax is referred to as the tax, levied on person's income and wealth and is paid directly to the government.	Indirect Tax is referred to as the tax, levied on a person who consumes the goods and services and is paid indirectly to the government.
Nature	Progressive in nature i.e., higher tax is levied on a person earning higher income and vice versa.	Regressive in nature i.e., all persons will bear equal wrath of tax on goods or service consumed by them irrespective of their ability.
Incidence and Impact	Falls on the same person. Assessee, himself bears such taxes. Thus, it pinches the taxpayer.	Falls on different person. Tax is recovered from the assessee, who passes such burden to another person. Thus, it does not pinch the taxpayer.
Example	Income Tax	GST, Custom Duty
Evasion	Tax evasion is possible	Tax evasion is hardly possible by a consumer as it is included in the price of the goods and services.
Inflation	Direct tax helps in reducing the inflation.	Cost of goods and services increases due to levy of indirect tax thus indirect taxes promote inflation. However, sometimes it is useful tool to promote social welfare by checking the consumption of harmful goods or sin goods through higher rate of tax.
Imposition and collection	Imposed on and collected from the same person	Imposed on and collected from consumers of goods and services but paid and deposited by the assessee.
Burden	Cannot be shifted	Can be shifted
Event	Taxable income of the assessee	Supply of goods and services

### Conclusion

In essence, indirect taxes are the invisible thread connecting everyday consumer transactions to the broader fiscal health of the nation. While they provide the government with a wide, resilient tax base and relative ease of collection, their inherently regressive nature requires policymakers to strike a delicate balance to avoid overburdening the common citizen. For aspiring Cost and Management Accountants, a solid theoretical grasp of how tax incidence and impact operate is much more than just an academic requirement. It is the conceptual bedrock upon which you will build your practical expertise—enabling you to successfully navigate complex GST compliance, optimize supply chain taxes, and drive strategic corporate decision-making in your future professional roles.

## Topic

Module 4:  
Cost Book Keeping

Module 1:  
Introduction to  
Cost Accounting

INTERMEDIATE

Group I - Paper-8

Cost Accounting  
(CA)

## Reconciliation of Cost Accounts with Financial Accounts

This Chapter is very much relevant for all Intermediate Examinations. 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. Sometimes profit as per cost Accounts and Financial Accounts are to be worked out first and thereafter reconciliation statement is to be prepared in the method of absorption of overhead at predetermined rate, their arises the difference between the predetermined amount charged and actual expenses. If the profit shown in Cost Ledger is taken as starting point and the that give rise to differences are added or subtracted from it, the resultant figure would agree with the profit as shown in the Financial Ledger

### Reconciliation of financial accounts and post accounts

In an enterprise which maintains two sets of accounts, financial accounts and accounts. They will not agree each other's profit figure. Because of that reason reconciliation is necessary in order to match these two profit figures. Besides, management is also interested to know the cause of differences in order to check the Arithmetical accuracy of both sides of accounts. Thus, this will facilitate internal control by highlighting the variations causing increase or decrease in profits. Such reconciliation is to be made at regular intervals. The figures of profit either as per cost ledger or as per financial ledger is taken as the starting point for reconciliation. For instance, if profit shown in the cost ledger is taken first, and the amount that gives rise to differences are added or deducted from it, the resultant figure should agree with the profit shown in financial ledgers.

Reasons for variation 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

#### A. Under over absorption

In cost accounts in order to ascertain unit cost of a product, pre-determined rates and charged in respect of overhead. The basis normally used percentage on prime cost, rate per unit, percentage of direct wages, rate level of machine hour. When overhead is recovered on predetermined rates, it may not exactly agree with overhead, 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 posting profit with financial profit, two adjustments with financial profits.:

1. In case of under absorption of overhead, the amount of under absorption overhead will have to be added back to financial profit
2. In case of absorption of overhead, the amount of over absorption, overhead, will have to be deducted from financial profit.

#### B. Adoption of different method of valuation of stock

In financial accounts, the stock is valued based on the principle of cost or market value, whichever is lower. But in cost accounts, the stock of raw materials is valued on the basis of FIFO, LIFO or Aardhaar methods of pricing issues, WIP maybe 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 Hyatt is the profit and vice 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 first accounts, and vice versa.

#### C. Items purely of financial natures.:

There are some items which are of purely financial nature having no counterpart in cost 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. Paid to proprietor in axis at fair for services rendered
4. Damages payable at law
5. Penalties payable.
6. Preliminary expenses on 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, dividend, etc. received on investments.
4. Rent received.
5. Fees or commission received on issue of shares, debentures, etc.
6. Transfer fee received.

**D. Items purely of cost accounts.**

The items which appear only in cost generally are:

1. Interest on capital supplied by the proprietor.
2. Rent on own premises
3. Depreciation on fully depreciated assets

**E. Appropriation of profit not dealt with in the cost's accounts.**

1. Transfer to received or other funds
2. Corporate tax
3. Dividend paid
4. Additional provisions for depreciation, bad debts, etc
5. Appropriation 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 charge to cost accounts and the actual wages booked in the financial accounts.

**Problem:**

Given below is the Trading and Profit and Loss Account of a Company for the year ended 31st March 2025.

To Materials	₹ 2740000	By Sales (60000units )	₹ 6000000
To Wages	1510000	By Stock (2000units)	160000
To Adm. Exp.	382000	By Work in Progress	
To Selling Exp.	450000	Materials -	64000
To Preliminary Exp. W/Off	60000	Wages	36000
		Factory Exp. <u>20000</u>	
			120000
To Net Profit	<u>325600</u>	By Dividend Received	<u>18000</u>
	₹ 6298000		₹ 6298000

The Company manufactures standard units.

In the Cost Accounts:

- 1) Factory Expenses have been allocated to production at 20% of Prime Cost;
- 2) Adm. Expenses at ₹ 6 per unit produced; and
- 3) Selling Exp. At ₹ 8 pr unit sold.

Prepare a Costing Profit And Loss Account o the Company and reconcile the same with the profit disclosed by the Financial Account .

**Solution:**

## Costing Profit and Loss Account

	₹		₹
To Materials (Note 1)	26,76,000	By Sales	60,00,000
To Wages (Note 2)	14,74,000	By Closing Stock(Note6)	1,72,646
To Factory Exp. (Note 3)	8,30,000		
To Adm. Exp. (Note 4)	3,72,000		
To Selling Exp (Note 5)	4,80,000		
To Net Profit	<u>3,40,646</u>		
	61,72,646		61,72,646

## Reconciliation Statement

Particulars	₹	₹
Particulars as per Cost Accounts:		3,40,646
Add:-		
1) Dividend not included in Cost Account	18,000	
2) Factory expenses over absorbed in Cost Accounts (830000 – 810000)	20,000	
3) Selling Overhead Over absorbed in Cost Accounts (480000 – 450000)	30000	
	-----	<u>68,000</u>
		4,08,646
Less :-		
1) Preliminary Exp. not included in Cost Accounts	60,000	
2) Adm. Overhead under-absorbed (382400 — 372000)	10,400	
3) Closing Stock under valued in Cost Accounts (172646 – 160000)	12,646	
	-----	<u>83046</u>
Profit as per Financial Accounts.		3,25,600

## Working Notes :-

- 1) Material = ₹ 27,40,000 – ₹ 64000 = ₹ 26,76,000
- 2) Wages ₹ 1510000 – ₹ 36000 = ₹14,74,000
- 3) Factory Expenses = 20% of Prime Cost = (676000 + 1474000) x 20% = ₹ 830000
- 4) Adm. Expenses = 62000 units x ₹ 6 = 372000
- 5) Selling Exp. = 60000 x ₹ 8 = ₹ 480000
- 6) Closing Stock : [(2676000 + 1474000 + 830000 + 372000) / 62000] x 2000 = Rs.172646

## Topic

Module 2:  
Operations  
Planning

# INTERMEDIATE

## Group II - Paper-9

Operations  
Management  
and Strategic  
Management  
(OMSM)

## Operations Management

### Operation Planning

#### Meaning of Operation Planning

Operation Planning refers to the process of deciding in advance how production or service activities will be carried out to achieve organizational goals efficiently. It involves determining what to produce, how much to produce, when to produce, and with what resources.

In operations management, planning ensures that materials, machines, manpower, and methods are properly coordinated so that products or services are delivered at the right time, cost, and quality.

Operation planning transforms strategic goals of an organization into short-term operational activities.

#### Objectives of Operation Planning

The main objectives are:

1. **Efficient utilization of resources** – ensuring optimal use of labor, machines, and materials.
2. **Meeting customer demand** – producing the required quantity at the right time.
3. **Cost minimization** – reducing production and operational costs.
4. **Maintaining quality standards** – ensuring products meet specifications.
5. **Ensuring smooth workflow** – avoiding bottlenecks and production delays.
6. **Improving productivity** – maximizing output with available resources.

#### Importance of Operation Planning

Operation planning is crucial in both manufacturing and service organizations.

- Coordination of Activities
  - It ensures coordination among procurement, production, inventory, and distribution.
- Reduction of Waste
  - Planning minimizes wastage of materials, time, and resources.
- Better Capacity Utilization
  - Helps use machines and manpower efficiently.
- Improved Customer Satisfaction
  - Timely delivery and quality products enhance customer satisfaction.
- Cost Control
  - Planning helps maintain budgets and control operational expenses.

- Risk Reduction
  - Anticipates potential problems and prepares solutions.

#### Levels of Operation Planning

Operation planning generally occurs at three levels.

- Strategic Planning (Long-term)
  - Time horizon: 3–5 years or more
  - Focus: capacity expansion, technology adoption, plant location
  - Example: Setting up a new manufacturing plant.
- Tactical Planning (Medium-term)
  - Time horizon: 6 months – 2 years
  - Focus: workforce planning, inventory policies, production plans
  - Example: Deciding annual production targets.
- Operational Planning (Short-term)
  - Time horizon: daily, weekly, or monthly
  - Focus: scheduling, dispatching, and shop-floor activities
  - Example: Scheduling workers and machines for daily production.

#### Components of Operation Planning

- Demand Forecasting
  - Predicting future demand for products or services.
  - Methods include:
    - Time series analysis
    - Market surveys
    - Trend analysis
  - Example: A company forecasting monthly demand for energy drinks.
- Capacity Planning
  - Determining the maximum production capability of an organization.
  - Types:
    - Design capacity
    - Effective capacity
    - Actual capacity
  - Example: A factory capable of producing 10,000 units per day.

- Aggregate Planning
  - Developing a production plan for the medium term (3–18 months).
  - Decisions include:
    - Production level
    - Workforce size
    - Inventory levels
  - Example: Planning production for the next financial year.
- Production Scheduling
  - Scheduling determines when each job or activity should start and finish.
  - Types:
    - Master Production Schedule (MPS)
    - Job scheduling
    - Machine scheduling
  - Example: Assigning production orders to specific machines.
- Inventory Planning
  - Ensuring availability of raw materials and finished goods.
  - Tools include:
    - Economic Order Quantity (EOQ)
    - Safety stock
    - Reorder point
  - Example: Maintaining enough raw material to avoid stock outs.
- Workforce Planning
  - Determining the number and skills of workers needed.
  - Activities include:
    - Recruitment
    - Training
    - Shift scheduling
- Tools and Techniques Used in Operation Planning
  - Some common tools include:
    - Gantt Charts – visual scheduling of tasks.
    - PERT (Program Evaluation Review Technique) – planning complex projects.
    - CPM (Critical Path Method) – identifying critical activities.

- MRP (Material Requirement Planning) – planning raw material needs.
- ERP Systems – integrated planning across departments.

### Operation Planning in Service Organizations

Operation planning is equally important in service sectors.

Examples:

Sector	Operational Planning Example
Hospital	Scheduling doctors and nurses
Airline	Flight scheduling and crew allocation
Bank	Staffing and service counter management
Restaurant	Inventory and kitchen workflow

### Challenges in Operation Planning

- Demand uncertainty
- Supply chain disruptions
- Machine breakdown
- Labor shortages
- Rapid technological changes

### Operations Strategy and Competitive Advantage

In modern business, Operations Strategy is the total pattern of decisions that shape the long-term capabilities of an operation and its contribution to overall strategy. It is the engine that converts an organization’s vision into tangible Competitive Advantage—the unique edge that allows a firm to outperform its rivals.

#### 1. The Strategic Hierarchy

Operations strategy does not exist in a vacuum; it must be aligned with the higher levels of the organization:

- **Corporate Strategy:** What business are we in? (e.g., ITC entering the FMCG space).
- **Business Strategy:** How do we compete in this specific market? (e.g., Cost leadership vs. Differentiation).
- **Operations Strategy:** What resources and processes do we need to win? (e.g., Lean manufacturing, high-tech supply chains).

#### 2. The Four Competitive Dimensions

To gain a competitive advantage, an operations manager must excel in one or more of these performance objectives:

- **Cost:** Being the “low-cost producer.” This requires high capacity utilization, lean processes, and waste reduction (e.g., Walmart or IndiGo Airlines).
- **Quality:** Providing products that are “fit for purpose” and error-free. Quality can be a “Qualifier” (minimum needed to enter the market) or an “Order Winner” (the reason a customer buys).

- **Speed (Delivery):** The elapsed time between a customer request and receiving the product. In the FMCG sector, speed to shelf is a massive advantage.
- **Flexibility:** The ability to change what you do, how you do it, or when you do it. This includes volume flexibility (handling surges in demand) and product flexibility (customization).

### 3. Order Winners vs. Order Qualifiers

Coined by Terry Hill, this concept is vital for linking operations to the market:

- **Order Qualifiers:** The basic criteria a product must meet even to be considered by a customer (e.g., a smartphone must have a touch screen).
- **Order Winners:** The specific operational capabilities that actually result in a customer choosing your product over a competitor's (e.g., 100-watt fast charging or a superior camera sensor).

### 4. Strategic Decision Categories

Operations strategy is implemented through two types of decisions:

- **Structural Decisions (The “Hard” Elements)**
  - These are long-term, high-capital decisions that are difficult to change:
  - **Capacity:** How much can we produce? (Lead vs. Lag strategy).
  - **Facilities:** Where should the plants be located? (Near raw materials or near customers?).
  - **Technology:** Should we use manual labor or robotics/AI?
- **Infrastructural Decisions (The “Soft” Elements)**
  - These relate to the systems and people that manage the operations:
  - **Quality Systems:** Implementing Total Quality Management (TQM) or Six Sigma.
  - **Workforce:** Training, compensation, and organizational culture.
  - **Planning & Control:** Using ERP systems (like SAP) for spares and inventory management.

### 5. Achieving Competitive Advantage: The “Fit”

Competitive advantage is achieved through Strategic Fit—when the operations’ capabilities perfectly match the market’s requirements.

- **Example (Cost Advantage):** If a company aims to be the cheapest provider, the operations strategy should focus on high-volume, standardized products and a “Lean” supply chain.

- **Example (Differentiation Advantage):** If a company aims to be the most innovative (like Apple), the operations strategy must prioritize R&D, flexible manufacturing, and high-quality components, even if they cost more.

### 6. The Resource-Based View (RBV)

Modern operations strategy often uses the RBV, which suggests that competitive advantage comes from resources that are V-R-I-O:

- Valuable
- Rare
- Inimitable (Hard to copy)
- Organized to capture value

An automated warehouse system or a patented manufacturing process are examples of operational resources that provide a long-term advantage.

A Trade-off Analysis is central to operations strategy because, in a world of limited resources, a business usually cannot be the best at everything simultaneously. If you focus on being the lowest-cost provider, you often have to sacrifice extreme customization.

The most famous way to visualize this is through the Product-Process Matrix, developed by Hayes and Wheelwright.

#### The Product-Process Matrix

This matrix shows the relationship between the Product Life Cycle (Volume and Variety) and the Process Life Cycle (how the work is organized).

Process Type	Product Variety	Volume	Example
Project	Unique, One-of-a-kind	Very Low	Constructing a bridge or a custom software build.
Job Shop	High Variety, Low Standardization	Low	A custom furniture maker or a boutique print shop
Batch	Multiple Products, Low Volume	Medium	Heavy equipment manufacturing or a bakery
Line (Mass)	Few Major Products, Higher Volume	High	Automobile assembly or appliance manufacturing
Continuous	High Standardization, Commodity	Very High	Oil refineries or a sugar processing plant

For a company to have a Competitive Advantage, it should ideally stay on the diagonal of this matrix.

#### The “Off-Diagonal” Trap:

- Above the Diagonal: A company tries to produce high-variety products using a mass-production line. This leads to massive inefficiencies and high costs because the line has to be stopped and “changed over” constantly.
- Below the Diagonal: A company uses a flexible job shop to produce high-volume, standard products. This is a waste of skilled labor and specialized equipment, making the product too expensive compared to competitors.

#### Strategic Trade-offs:

- **Flexibility vs. Cost:** As we move down the diagonal (toward Continuous processes), our Unit Cost drops significantly due to economies of scale, but our Flexibility to change the product design almost disappears.
- **Quality of Design vs. Quality of Conformance:** Projects and Job Shops focus on “Design Quality” (unique features), while Mass and Continuous processes focus on “Conformance Quality” (making sure every single unit is identical).

#### *[Quality of Design (The “Intent”)*

*This refers to how well the product’s specifications and features meet the needs and expectations of the target market. It is determined before the product is ever manufactured.*

#### *Quality of Conformance (The “Execution”)*

*This refers to how well the actual produced item matches the original design specifications. It is a measure of the manufacturing or service delivery process.]*

#### **Real-World Application:** The “FMCG Shift”

Take a company like ITC.

- In their R&D phase for a new snack, they operate in a Batch or even Job Shop mode to test different flavors and shapes.
- Once a product like Bingo! becomes a market leader, they shift the operations strategy to Mass Production (Line) to drive down costs and ensure every packet tastes exactly the same across India.

Competitive Advantage here comes from knowing exactly when to shift along that diagonal as the product matures.

#### *Suggestions:*

*This lesson could be used as an aid to teaching on Operations Planning by study guide. Clear Concept of this could help operation manager in its real world application. Studying operations planning with deep knowledge on all its components could be developed through supplementary readings by referring resources mentioned in study guide published by the institute.*

*Best Wishes.*

## Topic

Module 1:  
Accounting  
for Shares and  
Debentures

Module 6:  
Basic Concepts of  
Auditing

# INTERMEDIATE

## Group II - Paper-10

Corporate  
Accounting and  
Auditing (CAA)

**Section A: Corporate Accounting**  
**Topic: Accounting for Shares and Debentures**

**Comprehensive Problem 1**

A Co. Ltd issued 6,000 equity shares of ₹ 10 each payable as ₹ 3 per share on Application, ₹ 5 per share (including ₹ 2 as premium) on Allotment and ₹ 4 per share on Call. All the shares were subscribed. Money due on all shares was fully received excepting P, holding 100 shares, failed to pay the Allotment and Call money and Q, holding 200 shares, failed to pay the Call Money. All those 300 shares were forfeited. Of the shares forfeited, 250 shares (including whole of P's shares) were subsequently re-issued to R as fully paid up at a discount of ₹ 2 per share.

Pass the necessary entries in the Journal of the company to record the forfeiture and re-issue of the share.

**Solution:**

**In the books of A Co. Ltd.**

**Journal**

Date	Particulars	Dr. (₹)	Cr. (₹)
	Equity Share Capital A/c (300 × ₹ 10) .....Dr.	3,000	
	Securities Premium A/c (100 × ₹ 2) .....Dr.	200	
	To Equity Share Allotment A/c (100 × ₹ 5)		500
	To Equity Share Call A/c (300 × ₹ 4)		1,200
	To Forfeited Shares A/c		1,500
	(Being forfeiture of 300 equity shares for non-payment of allotment and call money on 100 shares and for non-payment of call money on 200 shares as per Board's Resolution No. ... dated ...)		
	Bank A/c .....Dr.	2,000	
	Forfeited Shares A/c .....Dr.	500	
	To Equity Share Capital A/c		2,500
	(Being re-issue of 125 shares @ ₹8 each as per Board's Resolution No. ... dated ...)		
	Forfeited Shares A/c .....Dr.	700	
	To Capital Reserve A/c		700
	(Being profit on re-issue transferred to Capital Reserve)		

Working Note: (1) Calculation of Amount to be Transferred to Capital Reserve

Amount forfeited per share of P	₹ 3	Amount forfeited per share of Q	₹ 6
Less: Loss on re-issue per share	₹ 2	Less: Loss on re-issue per share	₹ 2
Surplus	₹ 1	Surplus	₹ 1

Transferred to Capital Reserve: P's share (100 x ₹ 1) = ₹100;

Q's share (150 x ₹ 4) = ₹600.

Total ₹700.

**Comprehensive Problem 2**

Mr. M who was the holder of 400 preference shares of ₹100 each, on which ₹75 per share has been called up could not pay his dues on Allotment and First call each at ₹25 per share. The Directors forfeited the above shares and reissued 300 of such shares to Mr. N at ₹65 per share paid-up as ₹75 per share.

Give Journal Entries to record the above forfeiture and re-issue in the books of the company.

**Solution:**

In the books of .....

**Journal**

Date	Particulars	Dr. (₹)	Cr. (₹)
	Preference Share Capital A/c (400 × ₹ 75) .....Dr. To Preference Share Allotment A/c To Preference Share First Call A/c To Forfeited Shares A/c (Being forfeiture of 400 preference shares of ₹75 each called up for non-payment of allotment and first call money as per Board's Resolution No. ... dated ...)	30,000	10,000 10,000 10,000
	Bank A/c (₹65 × 300).....Dr. Forfeited Shares A/c (₹10 × 300).....Dr. To Preference Share Capital A/c (Being re-issue of 125 shares @ ₹8 each as per Board's Resolution No. ... dated ...)	19,500 3,000	22,500
	Forfeited Shares A/c .....Dr. To Capital Reserve A/c (Being profit on re-issue transferred to Capital Reserve)	4,500	4,500

Working Note: (1) Calculation of amount to be transferred to Capital Reserve

Forfeited amount per share = ₹10,000 / 400 = ₹25

Loss on re-issue = ₹75 – ₹65 = ₹10

Surplus per share re-issued ₹15

Transferred to capital Reserve ₹15 × 300 = ₹4,500.

₹25 × 100 = ₹2,500 should be shown as an addition to share capital.

**Section B: Auditing****Topic: Basic Concepts of Auditing****Question: Discuss the Essential Features of Auditing****Answer:**

Auditing is a systematic and disciplined examination of financial information with the objective of enhancing its credibility. The essential features of auditing are discussed below:

**1. Systematic and Scientific Process**

Auditing follows a planned and methodical approach. It involves proper audit planning, risk assessment, execution of audit procedures, and documentation, ensuring that the audit is conducted logically and efficiently.

**2. Examination of Accounting Records and Evidence**

An audit is based on the examination of books of accounts, vouchers, documents, and other relevant evidence. The auditor evaluates whether the accounting records support

the transactions and balances reported in the financial statements.

**3. Conducted by an Independent Person**

A fundamental feature of auditing is independence. The auditor must be independent of the entity being audited to ensure objectivity and impartiality. Independence enhances the reliability of the audit opinion.

**4. Verification of Financial Statements**

Auditing primarily relates to the verification of financial statements such as the Balance Sheet, Statement of Profit and Loss, and Cash Flow Statement to determine whether they present a true and fair view.

**5. Use of Audit Evidence**

Audit conclusions are drawn based on sufficient and appropriate audit evidence. Evidence may be obtained

through inspection, observation, inquiry, confirmation, computation, and analytical procedures.

## 6. Application of Professional Judgment and Scepticism

Auditing requires the application of professional judgment in areas such as materiality, risk assessment, and audit procedures. The auditor also exercises professional scepticism, maintaining a questioning mind and critically assessing audit evidence.

## 7. Reasonable Assurance, Not Absolute Assurance

Auditing provides reasonable assurance that the financial statements are free from material misstatement. Due to inherent limitations such as sampling, use of estimates, and internal control constraints, absolute assurance is not possible.

## 8. Detection and Prevention of Errors and Frauds (Incidental)

While the primary objective of auditing is not the detection of frauds and errors, an audit is designed to provide reasonable assurance that material misstatements due to fraud or error are detected. Prevention is largely a management responsibility.

## 9. Reporting of Audit Findings

The outcome of an audit is the audit report, wherein the auditor expresses an opinion on the financial statements. The report communicates the auditor's conclusions to users of financial statements.

## 10. Compliance with Legal and Professional Standards

Auditing is conducted in accordance with applicable laws and professional standards, such as the Standards on Auditing issued by the Institute of Chartered Accountants of India (ICAI) in India.

The essential features of auditing collectively ensure that the audit process is independent, evidence-based, systematic, and objective, thereby enhancing the credibility and reliability of financial statements for stakeholders.

### Question: Discuss the objectives of Audit with reference to SA 200

**Answer:** SA 200 – *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing* lays down the fundamental purpose and scope of an audit. The objectives of an audit, as envisaged in SA 200, can be discussed as follows:

### 1. Primary Objective of the Auditor

The overall objective of an independent auditor, as per SA 200, is:

- To obtain reasonable assurance about whether the

financial statements as a whole are free from material misstatement, whether due to fraud or error, and

- To express an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Reasonable assurance is a high level of assurance, but not absolute assurance, due to inherent limitations of an audit.

## 2. Reasonable Assurance on Financial Statements

SA 200 emphasizes that:

- The auditor provides reasonable, not absolute, assurance.
- There is an unavoidable risk that some material misstatements may not be detected, even when the audit is properly planned and performed in accordance with SAs.

This objective recognizes the use of:

- Professional judgment
- Sampling techniques
- Limitations of internal control
- Persuasive rather than conclusive audit evidence

## 3. Detection of Material Misstatements

The audit objective includes obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level. This involves:

- Identifying and assessing risks of material misstatement
- Designing and performing audit procedures responsive to those risks
- Considering both fraud and error as potential causes of misstatements

## 4. Expression of Audit Opinion

Based on the audit evidence obtained, the auditor aims:

- To form an opinion on the truth and fairness (or true and fair view) of the financial statements
- To report in accordance with the auditor's findings and the requirements of the applicable Standards on Auditing

The opinion enhances the credibility of financial statements for users.

## 5. Compliance with Ethical Requirements

SA 200 requires the auditor to comply with ethical requirements, including:

- Integrity
- Objectivity
- Professional competence and due care
- Confidentiality
- Professional behavior

In India, these ethical requirements are prescribed by the Institute of Chartered Accountants of India (ICAI).

#### **6. Exercise of Professional Judgment and Scepticism**

To achieve audit objectives, SA 200 mandates:

- Professional judgment in planning and performing the audit
- Professional scepticism, i.e., a questioning mind and critical assessment of audit evidence, especially in areas susceptible to fraud or management bias

#### **7. Conduct of Audit in Accordance with SAs**

The auditor must:

- Comply with all relevant Standards on Auditing
- Achieve the objectives stated in each applicable SA
- Modify the audit approach or opinion if objectives cannot be achieved

In essence, SA 200 defines the audit as a systematic and disciplined process aimed at enhancing the reliability of financial statements. The objectives focus on obtaining reasonable assurance, detecting material misstatements, exercising professional judgment and scepticism, complying with ethical requirements, and ultimately expressing a well-founded audit opinion.

## Topic

Module 2:  
Institutions and  
Instruments in  
Financial Markets

Module 8:  
Introduction to  
Data Science  
for Business  
Decision-making

## INTERMEDIATE

Group II - Paper-11

Financial  
Management and  
Business Data  
Analytics (FMDA)

# Financial Management

## Financial Institutions

### Alternative Investment Funds (AIF):

Alternative Investment Fund or AIF means any fund established or incorporated in India which is a privately pooled investment vehicle which collects funds from sophisticated investors, whether Indian or foreign, for investing it in accordance with a defined investment policy for the benefit of its investors.

#### Legal Structure

An AIF is usually established as a **Trust**, but it can also be a **Company**, a **Limited Liability Partnership (LLP)**, or a body corporate. It is a distinct legal entity that pools capital to be managed by a professional fund manager.

#### Category I AIFs (High growth/Early stage, Socially desirable)

1. **Venture Capital Funds (VCFs):** Invest in early-stage startups.
2. **Angel Funds:** Negen Angel Fund, Pipe Serica Angel Fund, Finvolve Growth Opportunities Fund.
3. **Infrastructure Funds:** Invest in large-scale public projects.
4. **Social Venture Funds:** Invest in businesses with social impact.
5. **SME Funds:** Focus on scaling small/medium enterprises.

#### Category II AIFs (Private Equity, Debt, Funds of Funds)

These do not generally use high leverage.

1. **Private Equity (PE) Funds:** Invest in unlisted, established companies.
2. **Debt Funds:** Sundaram High Yield Debt AIF, Vivriti Diversified Bond Fund.
3. **Real Estate Funds:** Invest in residential/commercial projects.
4. **Funds of Funds (FoF):** Singularity Investments Fund of Fund.
5. **Other Examples:** Unicorn India Ventures Fund, Bharat Value Fund, 360 ONE Asset Early-Stage Fund.

#### Category III AIFs (Hedge Funds, Complex/Leveraged Strategies)

1. **Hedge Funds:** Sameeksha Equity AIF, Negen Undiscovered Value Fund.
2. **PIPE Funds (Private Investment in Public Equity):** Ampersand Growth Opportunities Fund.

3. **Other Examples:** 360 ONE Equity Opportunity Fund, ICICI Equity Opportunities AIF.

#### Alternative Investment Funds (AIFs) and Mutual Funds (MFs): Comparison

Alternative Investment Funds (AIFs) and Mutual Funds (MFs) differ primarily in target audience, risk, and asset types: AIFs require a minimum ₹1 crore investment, focusing on high-risk/high-reward private equity or hedge funds for wealthy individuals. MFs are affordable, diversified, and highly liquid, targeting retail investors with traditional stocks/bonds.

Feature	Alternative Investment Funds (AIFs)	Mutual Funds (MFs)
1. Minimum Investment	High (₹1 Crore+)	Low (₹100-₹500)
2. Target Investor	HNIs & Institutions	Retail Investors
3. Asset Type	Private Equity, Hedge Funds, Real Estate	Stocks, Bonds, Debt
4. Risk Level	High	Moderate to Low
5. Liquidity	Low/Lock-in periods	High/Daily
6. Management	Active (Complex strategies)	Passive/Active (Diversified)

#### Credit Rating - Credit Rating Methods and Rating Agencies in India

A **credit rating** is an evaluation of the credit risk of a prospective debtor (an individual, a business, company or a government). It is the practice of predicting or forecasting the ability of a supposed debtor to pay back the debt or default. The credit rating represents an evaluation from a credit rating agency of the qualitative and quantitative information for the prospective debtor, including information provided by the prospective debtor and other non-public information obtained by the credit rating agency's analysts.

#### Credit rating process of CRISIL

The **CRISIL rating process** follows these specific steps divided between the **Issuer** and the **Rating Agency**:

##### I. Initial Request & Setup

1. **Requests for a Rating:** The company (Issuer) initiates the process by requesting a rating for its financial instrument.

2. **Agreement & Fees:** The Issuer signs a formal rating agreement and provides the necessary information and rating fees.
3. **Team Assignment:** CRISIL assigns an analytical team. Notably, a team is always assigned; a single individual is never assigned to a case alone to ensure objectivity.

## II. Analysis & Evaluation

4. **Information Collation:** The assigned team gathers data and conducts a **preliminary analysis** of the issuer's business and financial health.
5. **Management Interaction:** The analysts meet with the issuer's management to gain deeper insights into operations and future plans.
6. **Rating Committee Presentation:** The team presents its findings to a **Rating Committee**, which includes at least one-third independent members.

## III. Assignment & Acceptance

7. **Rating Communication:** The committee assigns a rating, which is then communicated to the issuer.
8. **Issuer Decision:**
  - (i) **If Accepted ("Yes"):** The rating is published on the CRISIL website as a **rating rationale**.
  - (ii) **If Rejected ("No"):** The issuer can choose to **appeal** by providing additional material facts. If no appeal is made, the details of the unaccepted rating are disclosed on the website.

## IV. Monitoring

9. **Surveillance:** Once a rating is accepted and disseminated, it is kept under **continuous surveillance** for the entire tenure of the instrument to account for any changes in the company's risk profile.

(Source: <https://www.crisil.com/>)

## Major Credit Rating Agencies in India

### 1. CRISIL Ratings Limited:

- The oldest CRA in India (Established in 1987).
- A subsidiary of CRISIL Limited, which is majority-owned by S&P Global.

- It holds a dominant position in the domestic debt market.

### 2. ICRA Limited:

- Established in 1991, its largest shareholder is Moody's Investors Service.
- Specialises in corporate debt, mutual funds, and structured finance ratings.

### 3. CARE Ratings Limited:

- Operational since 1993 and headquartered in Mumbai.
- Provides comprehensive rating services across infrastructure, manufacturing, and financial sectors.

### 4. India Ratings and Research Private Limited (Ind-Ra):

- A 100% owned subsidiary of the Fitch Group.
- Recognised by both SEBI and the RBI for providing credit opinions on financial institutions and corporate issuers.

### 5. Brickwork Ratings India Private Limited:

- Established in 2007 and promoted by Canara Bank.
- Despite previous regulatory challenges, it continues to operate as a SEBI-registered agency, recently serving as a monitoring agency for rights issues as of March 2026.

### 6. Acuité Ratings & Research Limited:

- Formerly known as **SMERA Ratings**, it was originally established to focus on MSMEs.
- It has since evolved into a full-service agency rating bonds and bank loans.

### 7. Infomercials Valuation and Rating Private Limited:

- A SEBI-registered and RBI-accredited agency that evaluates banks, NBFCs, and large corporates.

### 8. Infinitum Ratings (formerly known as Ivy Ratings):

- A more recent entrant among the SEBI-recognised intermediaries

## Business Data Analytics

### Data Transformation

Data transformation is the process of converting raw data from its original format, structure, or values into a clean, standardized, and usable format. It acts as a “data refinery,” ensuring that information from disparate sources (like APIs, databases, and logs) is compatible and high-quality for analysis, reporting, or machine learning.

#### Strategic Objectives of Data Transformation for Business Analytics

- 1. Improve Data Quality & Accuracy:** Removing duplicates, correcting errors, and filling in missing values ensures the final dataset is reliable for high-stakes decision-making.
- 2. Establish a Unified Data View:** Consolidating data from disparate sources (e.g., CRMs, APIs, legacy databases) into a single, cohesive dataset breaks down silos and provides a 360-degree view of operations.
- 3. Enable Advanced Analytics & AI:** Standardizing data is essential for machine learning (ML) and artificial intelligence (AI) models, which require specific formats and consistent scales to perform accurately.
- 4. Enhance Operational Efficiency:** Automating routine data preparation tasks reduces manual effort and minimizes the risk of human error, allowing teams to focus on higher-value analysis.
- 5. Ensure Regulatory Compliance:** Techniques like data anonymization and encryption help organizations protect sensitive information and meet legal standards like GDPR or HIPAA.
- 6. Optimize Data Storage & Performance:** Aggregating and compressing data can reduce its storage footprint and speed up query response times.

#### Types of Data Transformation

- 1. Constructive:** Adding, copying, or replicating data to fill gaps.
- 2. Destructive:** Deleting, filtering, or removing unnecessary data.
- 3. Aesthetic:** Standardizing formats (e.g., date formats, capitalization).
- 4. Structural:** Changing the structure, such as renaming columns or pivoting tables.

#### Process of Data Transformation

The data transformation process typically follows these core steps:

#### 1. Data Collection

This is the first stage where raw facts, figures, and observations are gathered from various sources (surveys, sensors, transactions, or interviews). At this stage, the data is **unstructured** and lacks utility for decision-making.

#### 2. Data Cleaning and Validation

Raw data often contains errors, duplicates, or missing values. In this step, the data is “scrubbed” to ensure accuracy. If the input data is incorrect, the resulting information will be flawed—a concept known as **GIGO** (Garbage In, Garbage Out).

#### 3. Classification and Coding

Data is organized into meaningful categories based on shared characteristics. For example, a company might classify sales data by region, product type, or customer age. Coding involves assigning numerical or alphabetical symbols to these categories to simplify processing.

#### 4. Tabulation and Processing

The cleaned and classified data is then arranged into a systematic format, such as tables or databases. Processing involves performing operations on the data, such as:

- **Calculations:** Totals, averages, or percentages.
- **Sorting:** Arranging data in ascending or descending order.

#### 5. Data Summarization

Since decision-makers cannot digest thousands of individual data points, the data must be condensed. Summarization provides a “big picture” view through descriptive statistics or brief reports, highlighting the most important figures.

#### 6. Analysis and Interpretation

This is the critical stage where **data becomes information**. By applying analytical tools (like trend analysis or correlation), we look for patterns, relationships, and anomalies. This step adds the “why” and “how” to the numbers.

#### 7. Presentation and Communication

The final step is to present the information in a way that is easily digestible for the user. This is often done through **visualisations** like charts, graphs, and dashboards. Information is only «decision-relevant» if the person receiving it can understand it well enough to take action.

## Topic

Module 1:  
Introduction to  
Management  
Accounting

Module 2:  
Activity Based  
Costing

# INTERMEDIATE

## Group II - Paper-12

### Management Accounting (MA)

## Introduction to Management Accounting

### Meaning of Management Accounting

Management accounting comprises two terms – ‘management’ and ‘accounting’. Management provides for planning, organizing, directing and controlling organizational resources to achieve strategic objectives. Accounting provides for measurement and reporting for evaluating performance.

Management accounting may be defined as the process of identification, measurement, accumulation, analysis, interpretation and communication of financial and non-financial information used by management to plan, evaluate and control within an organization.

The Chartered Institute of Management Accountants (CIMA) defines management accounting as the application of accounting and financial management principles to create, preserve and increase value for stakeholders in profit and non-profit organizations. It emphasizes that management accounting is an integral part of management.

Thus, management accounting includes information that may be:

- Financial or non-financial
- Historical or future-oriented
- Actual or estimated
- Detailed or summarized
- Presented in numerical, graphical or descriptive form

Its primary objective is to assist management in improving organizational efficiency and effectiveness.

### Scope of Management Accounting

Management accounting has a broad and extensive scope. It consists of:

- i) **Financial Accounting Data:** Despite being historical, this data serves as the foundation for planning and forecasting.
- ii) **Cost accounting methods:** Such as opportunity cost analysis, standard costing, differential costing, and marginal costing.
- iii) **Budgeting and Budgetary Control:** Creating functional budgets and comparing actual and planned performance.

- iv) **Cost Control Methods:** Variance analysis, labor cost control, and inventory control.
- v) **Reporting:** Using graphs, charts, and statistical tools, prepare reports on a regular basis for management.
- vi) **Tax accounting:** functions related to tax planning and compliance.
- vii) **Internal Financial Control:** Internal auditing and asset protection.
- viii) **Performance Evaluation:** Assessing managerial effectiveness according to goals (management by exception).
- ix) **Strategic Decision Support:** Make-or-buy, pricing, and capital budgeting decisions.

### Evolution of Management Accounting

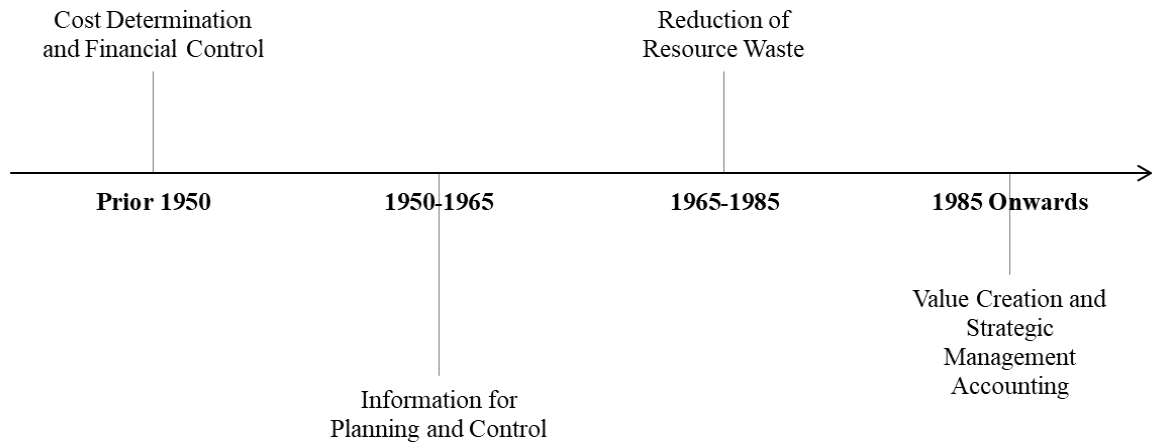
The need for systematic cost determination and resource optimization in large-scale enterprises led to the evolution of management accounting in the UK during the Industrial Revolution.

Its evolution was divided into four phases by the International Federation of Accountants (IFAC):

- i) **Cost Determination and Financial Control Before 1950** – In a comparatively stable production environment, the emphasis was on product costing and financial control.
- ii) **Data for Planning and Control, 1950–1965** – The focus shifted to profitability analysis, standard costing, and responsibility accounting.
- iii) **Resource Waste Reduction, 1965–1985** – Improving operational efficiency and getting rid of non-value-added activities were priorities.
- iv) **Value Creation and Strategic Management Accounting starting in 1985** – The emphasis shifted to long-term value creation, customer profitability, competitive positioning, and strategic analysis.

Management accounting is acknowledged as a strategic partner in the success of organizations in the modern phase.

**Figure 1. Evolution of Management Accounting**



**Relationship Between Management Accounting and Cost Accounting**

The scope of management accounting is broader, and its primary objective is to provide relevant financial and non-financial information to the management for planning, controlling, and decision-making. In the process, management accounting heavily relies on the information generated from financial accounting and cost accounting. Where cost accounting is only concerned with the measurement and control of costs, management accounting takes it to the next level by not only analyzing the information but also providing it in a form that is useful for decision-making. Hence, it could be concluded that cost accounting is a part of management accounting, and management accounting is a broader concept that encompasses the integration of costs with other financial and non-financial information for the efficient management of the organization and the accomplishment of organizational goals.

*Comparison Between Cost Accounting and Management Accounting*

Basis of Comparison	Cost Accounting	Management Accounting
Meaning	Focuses on determination, control, and reduction of costs.	Focuses on providing information to assist managerial decision-making.
Purpose	Determines product or service cost and helps control expenses.	Supports planning, policy formulation, and strategic decisions.
Scope	Relatively limited and focused mainly on cost-related issues.	Much broader as it integrates financial and cost information.
Nature of Information	Mainly quantitative cost data.	Both quantitative and qualitative information.
Role in Decision Making	Limited role, often based on historical cost data.	Major role, using both historical and predictive information.
Relationship	Considered a subset of management accounting.	Acts as a broader system incorporating cost and financial accounting.
Users	Managers, sometimes shareholders and vendors.	Primarily internal management.
Legal Requirement	Cost audit may be mandatory in certain industries.	No statutory requirement for management accounting reports.

**Functions of Management Accountant**

The management accountant plays a crucial role in the process of management. The major functions include:

- **Planning:** Creating capital expenditure plans, forecasts, and budgets.
- **Controlling:** Using variance analysis and standards to keep an eye on performance.
- **Reporting:** Giving pertinent management and timely reports.
- **Coordinating:** Using financial integration to ensure harmony among various departments.
- **Advisory Role:** Helping management make strategic choices.

- **Asset Protection:** Putting risk management and internal controls in place.

### Importance of Management Accounting in Modern Business Environment

Management accounting has taken on a more strategic role in the age of global competition, deregulation, technological advancement, and sustainability concerns. It provides support for:

- Analysis of customer profitability
- Life cycle costing of products
- Cost optimization and lean manufacturing
- Accounting for sustainability and the environment
- Management based on values

Modern management accounting emphasizes value creation and competitive advantage in addition to cost reduction. In conclusion, an essential tool for contemporary management is management accounting. It supports planning, controlling, and decision-making processes by integrating financial and non-financial data. It began as a tool for determining costs and has since developed into a strategic discipline with the goal of increasing organizational value and guaranteeing sustainable growth.

### Multiple Choice Questions (MCQs)

- 1) Management accounting primarily combines the functions of:
  - A. Auditing and taxation
  - B. Management and accounting
  - C. Finance and marketing
  - D. Costing and auditing
- 2) The main objective of management accounting is to assist management in:
  - A. Statutory reporting
  - B. Recording financial transactions
  - C. Planning, controlling, and decision-making
  - D. Preparing tax returns
- 3) According to Chartered Institute of Management Accountants (CIMA), management accounting is concerned with:
  - A. Application of auditing techniques
  - B. Application of accounting and financial management principles
  - C. Preparation of financial statements
  - D. Maintenance of cost records
- 4) Which of the following characteristics correctly describes management accounting information?
  - A. Only financial and historical
  - B. Financial or non-financial, historical or future-oriented
  - C. Only numerical data
  - D. Only summarized reports
- 5) In the scope of management accounting, opportunity cost analysis, standard costing, and marginal costing fall under:
  - A. Financial accounting data
  - B. Budgetary control
  - C. Cost accounting methods
  - D. Strategic decision support
- 6) Which of the following activities is included under internal financial control in management accounting?
  - A. Tax planning
  - B. Internal auditing and asset protection
  - C. Product pricing
  - D. Market forecasting
- 7) The systematic development of management accounting was largely influenced by the:
  - A. Information Technology Revolution
  - B. Agricultural Revolution
  - C. Industrial Revolution
  - D. Communication Revolution
- 8) The four phases of the evolution of management accounting were identified by the:
  - A. World Trade Organization
  - B. International Federation of Accountants
  - C. International Monetary Fund
  - D. Asian Development Bank
- 9) During the phase “Data for Planning and Control (1950–1965)”, emphasis was mainly placed on:
  - A. Environmental accounting
  - B. Standard costing and responsibility accounting
  - C. Customer profitability
  - D. Strategic positioning

- 10) The phase “Resource Waste Reduction (1965–1985)” focused primarily on:
- Increasing product prices
  - Eliminating non-value-added activities
  - Expanding financial reporting
  - Reducing taxation
- 11) In the relationship between cost accounting and management accounting, cost accounting is regarded as:
- An independent system unrelated to management accounting
  - A broader concept than management accounting
  - A component or subset of management accounting
  - A replacement for management accounting
- 12) In modern organizations, management accounting supports decisions such as:
- Make-or-buy and capital budgeting decisions
  - Political policy formulation
  - Government legislation
  - Foreign exchange regulation

**Answer Key**

- 1–B  
2–C  
3–B  
4–B  
5–C  
6–B  
7–C  
8–B  
9–B  
10–B  
11–C  
12–A

**Fill in the blanks**

- Management accounting information may be presented in numerical, graphical, or \_\_\_\_\_ form.
- Functional budgets and comparison between actual and planned performance form part of \_\_\_\_\_ and budgetary control.
- The earliest phase of management accounting emphasized cost determination and \_\_\_\_\_ control.
- Internal auditing and asset protection are elements of \_\_\_\_\_ financial control.
- In modern business, management accounting emphasizes \_\_\_\_\_ creation and competitive advantage.

**Answer Key**

- Descriptive
- Budgeting
- Financial
- Internal
- Value

**State True or False**

- Management accounting integrates both financial accounting data and cost accounting information.
- Management accounting reports are legally mandatory for all organizations.
- Management by exception is a technique used in performance evaluation within management accounting.
- Cost accounting mainly focuses on measurement and control of costs.
- Modern management accounting emphasizes long-term value creation and strategic analysis.

**Answer Key**

- True
- False
- True
- True
- True

## Activity Based Costing

### Traditional Cost System

The conventional costing system primarily uses volume-based metrics like direct labor hours, machine hours, or units produced to allocate factory overheads to products. Prior to being absorbed using a preset overhead rate, overheads are first totaled department-by-department. This method is founded on the idea that production volume and overhead consumption are directly correlated. It is easy to use and reasonably priced, but in contemporary manufacturing, where indirect costs are high and products vary in complexity, it could lead to cost distortion. Low-volume or customized products are frequently underpriced, while high-volume products are frequently overpriced.

These steps in traditional costing are:

- Identify indirect overhead costs, like payroll for maintenance staff and rent for the building.
- Estimate overhead costs for a specific tracking period, such as a calendar month or semi-annually.

- Choose a cost driver that is connected to the production of your product or service.
- Estimate a specific amount for the cost driver. For instance, if you are using man hours (labor hours) for one month, multiply the number of hours worked each week by the number of employees. Then, multiply that total by 52 (the number of weeks in a year) and divide by 12 (the number of months in a year).

$$\text{Overhead Rate} = \frac{\text{Estimated Overheads}}{\text{Estimated Base}} \text{ formula:}$$

- Apply the overhead rate to your product.

*Example:*

To determine the total production cost of Job No. M 626, different overhead absorption methods may be applied. Given total cost centre overhead of ₹62,100 and the relevant production data, the overhead rates under various bases are computed as follows:

Method of Absorption	Basis of Calculation	Computation	Overhead Rate
Rate per Unit of Output	13,800 units produced	₹62,100 ÷ 13,800 units	₹4.50 per unit
Direct Labour Hour Rate	27,000 labour hours	₹62,100 ÷ 27,000 hours	₹2.30 per labour hour
Machine Hour Rate	34,500 machine hours	₹62,100 ÷ 34,500 hours	₹1.80 per machine hour
Percentage of Direct Wages	Direct wages ₹17,250	(₹62,100 ÷ ₹17,250) × 100	360% of direct wages
Percentage of Direct Material Cost	Direct materials ₹49,680	(₹62,100 ÷ ₹49,680) × 100	125% of direct materials
Percentage of Prime Cost	Prime cost ₹66,930	(₹62,100 ÷ ₹66,930) × 100	93% of prime cost

### Introduction to Activity Based Costing

Activity-Based Costing is an improved approach to cost determination, which takes into account activities performed and resources utilized. This approach is based on the fact that products consume activities, and activities consume resources. ABC does not apply a single blanket rate, but instead applies costs to activity cost pools, which are then assigned to products by appropriate cost drivers. This approach is best used in automated, diverse, and multiple-product industries, especially where overheads account for a major proportion of costs.

### Steps in Activity Based Costing

The ABC implementation process consists of the following steps:

1. Identifying major activities such as set-up, inspection, ordering, and handling materials.
2. Development of activity cost pools by grouping costs related to each activity.
3. Identifying appropriate cost drivers, which measure activity usage, such as set-ups and purchase orders.
4. Computation of activity driver rate:

$$\text{Activity Driver Rate} = \frac{\text{Total Activity Cost}}{\text{Total Driver Units}}$$

5. Allocation of activity costs to products based on actual consumption of cost drivers.

$$\text{Cost} = \text{Resources Consumed} \times \text{Activity Driver Rate}$$

This ABC approach will provide a more accurate allocation of overhead costs.

*Example:*

The total cost of inspection-related activities is ₹1,00,000. A batch of products with 10 items in a batch requires 10 inspection activities.

The cost driver rate will be:

$$\frac{₹1,00,000}{10} = ₹10,000 \text{ per batch.}$$

Each product will have an inspection-related cost of ₹1000 (10,000 for a batch of 10 items in a batch). Similarly, the cost of other activities will be charged to the product to determine the total.

### Cost Pools and Cost Drivers

Cost pool is a group of costs associated with a given activity. Examples of cost pools include purchasing cost pool, inspection/machine set-up cost pool, etc. Cost driver is a factor that causes the cost of an activity to vary. Cost drivers can either be volume-based (machine hours) or non-volume-based (number of production runs). ABC systems focus on the non-volume-based cost drivers since many activities are not directly linked to the volume of production.

### Advantages and Limitations of Activity Based Costing

#### Advantages:

- Greater precision in product costs
- Better decisions on prices and product mixes
- Identification of non-value-added activities
- Better control of costs and profits

#### Limitations:

- Complex and expensive to adopt
- Needs extensive data collection
- Not viable if overheads are negligible

### Activity Based Costing and Decision Making

Activity Based Costing can be used in the following decision-making processes:

1. It can help to reduce freight or other logistical expenses and can help offset the cost of new facilities, personnel, or equipment when making decisions like moving or creating a new distribution center.
2. It can pinpoint the precise cost components that are being targeted, giving management a much clearer

picture from which to make decisions and take appropriate action.

3. It supplements Total Quality Management (TQM) and offers quantitative data that helps monitor the financial impact of TQM initiative improvements.
4. By tracing the costs back to the activity and the consumption of resources by each product,
5. It helps to analyze the costs and profits of both new and existing products in a more realistic manner.
6. It can enhance decision support for human resources.
7. It can present several options, including outsourcing, productivity improvements through automation, and determination of employee/revenue ratios.

### Multiple Choice Questions (MCQs):

- 1) Activity-Based Costing is based on the principle that:
  - A. Resources consume products and products consume activities
  - B. Products consume activities and activities consume resources
  - C. Activities consume products only
  - D. Costs are directly related to production volume
- 2) Activity-Based Costing allocates overhead costs primarily through:
  - A. A single blanket overhead rate
  - B. Departmental cost allocation
  - C. Activity cost pools and cost drivers
  - D. Direct labor hours only
- 3) ABC is particularly suitable for industries that are:
  - A. Labor intensive with low overheads
  - B. Automated with diverse and multiple products
  - C. Small-scale and single-product
  - D. Agricultural based
- 4) In Activity-Based Costing, a cost pool refers to:
  - A. The cost of a single product
  - B. A collection of similar costs associated with a specific activity
  - C. The direct labor cost of production
  - D. The selling price of a product

- 5) A cost driver is defined as:
- A factor that causes the cost of an activity to change
  - The total cost incurred in production
  - The price charged to customers
  - The salary of employees
- 6) Which of the following is an example of a non-volume-based cost driver in ABC?
- Machine hours
  - Units produced
  - Number of production runs
  - Direct labor hours
- 7) The activity driver rate in ABC is calculated as:
- Total driver units ÷ Total activity cost
  - Total activity cost ÷ Total driver units
  - Total overhead ÷ Units produced
  - Direct cost ÷ Total activity cost
- 8) Identifying major activities such as inspection, ordering, and set-up is the \_\_\_\_\_ step in implementing ABC.
- Final
  - First
  - Third
  - Fourth
- 9) One major advantage of Activity-Based Costing is:
- Simplification of all cost records
  - Elimination of all indirect costs
  - Greater accuracy in product cost determination
  - Reduction of production volume
- 10) Activity-Based Costing helps management identify:
- Only direct costs
  - Non-value-added activities
  - Only variable costs
  - Government regulations
- 11) Which of the following is a limitation of Activity-Based Costing?
- Lack of accuracy
  - Inability to measure costs
  - Complexity and high implementation cost
  - Inapplicability in large organizations
- 12) Activity-Based Costing can improve decision-making related to:
- Outsourcing and automation
  - Small business with low overhead
  - Agricultural planning
  - Budget allocation

**Answer key**

1–B

2–C

3–B

4–B

5–A

6–C

7–B

8–B

9–C

10–B

11–C

12–A

**Fill in the Blanks**

- Activity-Based Costing assigns costs to products through \_\_\_\_\_ cost pools.
- The factor that causes the cost of an activity to change is known as a \_\_\_\_\_.
- In ABC, the activity driver rate is calculated by dividing total activity cost by total \_\_\_\_\_ units.
- ABC focuses mainly on \_\_\_\_\_-based cost drivers rather than volume-based drivers.
- Grouping costs related to a specific activity forms an \_\_\_\_\_ cost pool.

**Answer Key**

1. Activity
2. Cost driver
3. Driver
4. Non-volume
5. Activity

**State True or False**

1. Activity-Based Costing applies a single blanket overhead rate to all products.
2. ABC recognizes that products consume activities and activities consume resources.

3. Cost pools represent groups of costs associated with specific activities.
4. Activity-Based Costing is inexpensive and easy to implement in all organizations.
5. ABC can assist management in evaluating outsourcing and automation decisions.

**Answer Key**

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

# CMA FINAL COURSE

Syllabus 2022

## Topic

Module 1 :  
The Companies Act,  
2013

FINAL

Group III - Paper-13

Corporate and  
Economic Laws  
(CEL)

## Formation and Types of Company

### Promotion of a company:

As per Companies Act, 2013 persons whose name appears in the prospectus or identified by the company in the annual return, has control directly or indirectly over the affairs of the company either as a shareholder or a director and according to whose direction, advice or instructions the Board of Directors are accustomed to act. A person should not be regarded as a promoter if he/she acts in its personal capacity.

As per the Securities Exchange Board of India (SEBI) persons who are in control of the issuer or are instrumental in the formulation of a plan or programme pursuant to which specified securities are offered to the public. The persons whose name appears in the offer document are known as promoters.

Promoters' Agreement/ Memorandum of Understanding (MOU):

When promoters decide to do a business in the nature of a company, they will be meeting and deciding on various issues and ultimately they will choose to make a Memorandum of Understanding (MOU) though it is not mandatory. Promoters or any of the promoters can make contracts in his own name for the benefit of the proposed company. Once registered, promoter will disclose the contracts. Promoter is also duty bound to disclose any interest in the company to any interested person and will not make any secret profit.

Promoters can also make an agreement which will mention various issues relating to formation of the company and rights and liabilities of the company inter se.

Promoters may decide to prepare and sign a Memorandum of Understanding or Memorandum of Agreement (also called Promoters Agreement) while MOU is not enforceable under the law. Having an MOU or MOA is not mandatory and promoters may decide to prepare two initial documents.

- Memorandum of Understanding (MOU)
- Memorandum of Association (MOA)

The steps which are required to be complied in order to start a company are as follows:

1. application for name
2. memorandum of association and articles of association
3. list of first directors if not mentioned in articles with particulars.
4. an agreement proposed to be entered with the md
5. declaration of compliance
6. affidavit by each director that he has not been convicted.

### Memorandum of Association:

Memorandum of Association of a company is the constitution or charter of the company and contains the powers of the company.

#### Name Clause:

The promoter will make an application for name and three (3) names shall be given to the Registrar of Companies (ROC) under whose jurisdiction, the registered office of the company will be situated. The Registrar of Companies (ROC) will approve the name or can suggest changes in the name. ROC will not approve a name which is considerable. The name so available will be valid for six months by which application for registration should be made by the name of the promoters. In case of public Ltd Company the name should be suffixed with "Ltd" and in case of private company by "Private Ltd". International brands works like National Hindustan Corporation etc are not allowed. Name should be in relation with the object.

#### Situation clause:

Memorandum of Association must mention the name of the state in which the registered office of the company is situated. However within 15 days of registration the full address to be intimated to ROC all communication shall be sent in that address. Every company must have a registered office from the date in which its starts its operation or the date of its incorporation.

#### Object clause: (Main object and other object)

Main object: It is the most important clause in Memorandum of Association. It states the purpose for which the company is formed. It defines the scope of activities of a company and limits the operations of the company. A Company cannot go beyond the Main object.

#### Other object:

The objects which are incidental or ancillary to the main object is called other object. It should be according to the Companies Act, 2013, lawful and well defined.

#### Capital clause:

The companies which are limited by shares should contain this clause in the Memorandum of Association. This clause contains the amount of capital with which the company is registered i.e. the authorized capital.

#### Liability Clause:

This clause mentions the liabilities of the members of the company. The liability of a member is limited to the portion of unpaid share capital.

#### Subscription clause:

Memorandum must be signed by the subscribers. Who are initial shareholders of the company at the time of registration. The subscribers must mention the number of shares registered in their name.

**Articles of association:**

The Articles of Association contains the internal rules and regulation of the company. The provisions of the AOA must not be in conflict with the provisions of the Memorandum of Association. In case such a conflict arises, the MOA will prevail.

Normally, every company has its own AOA. However, if a company does not have its own AOA, the model AOA specified in Schedule I- Table A of the Companies Act, 1956 will apply.

**Certificate of incorporation**

(Conclusive evidence that the company has been formed)

Corporate Identification No. (CIN) will be issued which is to be mentioned on the signboard at the entrance of all offices, stations, letter heads, vouchers, bills and stationaries.

Pvt. Company can commence business on incorporation.

**Types of companies****Govt. Company:-**

As per definition 2(45) of the Companies Act, 2013 a Govt. company means a company in which not less than (minimum) 51% of the paid up share capital is held by Central Govt. or State Govt. or partly by Central Govt. and partly by State Govt. A subsidiary of a Govt. company is also a Govt. company. There are few exemptions available to such companies where some further compliance is also required to be done by such companies. It is a separate legal entity and not a department of Govt. Govt. controls these companies both as a shareholder and also as an administrative ministry.

**Holding and subsidiary company:-**

As per definition in section 2(46) and 2(87) of the Companies Act, 2013 a company shall be considered to be a holding company if the other company controls the composition of the Board or holds more than half of the shares with voting rights. So there are two test of holding subsidiary relationship. In one case, management control is the basis of holding subsidiary relationship, where majority of director can be appointed and removed by the holding company. Such stipulation shall be there in the Articles of Association of the subsidiary company where

**Private / Public**

Serial No	Points of difference	Private	Public
1	shareholders	Min-2, max-3	Min 7, no max.
2	directors	Min-2, max.-15	Min.-3, max.-15 (may be increased with special resolution)
3	Finance	Cannot raise from public	Can raise
4	Transfer of shares	May be restricted	Cannot be restricted
5	Name	Use the suffix Pvt .Ltd.	Suffix "Ltd".
6	Members	2 (Two), Maximum 200 (Two Hundred).	7 (Seven)

it surrenders the right to appoint and remove directors to the other company regardless of shareholding.

**Investment company:**

This is a type of company whose principle business is the acquisition of holding and dealing of shares, stock and other securities.

**Non- profit (Section 8 co.):**

This type of companies are an association as limited company having charitable objects to promote commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment etc. They do not have any word 'Limited' or 'Private Limited' suffixed to their name. Any profit or income derived from this company is used to promote the objects of the company.

**Sectoral companies**

These type of companies both Companies Act and Sector Specific Act applies.at the time of registration, these type of companies need to get clearance / license from Sectoral regulators, like RBI, IRDAI, etc.

**Companies (banking/NBFC/insurance/electricity)**

**Govt. (51% and more)/ Deemed Govt. Company:** Shares of these types of companies are held by Central Govt. /State Govt. singly or jointly. Subsidiary of a Govt. company is also a Govt. company.

**Indian/Foreign:** Registered In India- Indian companies registered outside India and having place of business in India.

**Guarantee company:** Shareholders guarantee to pay more as share capital in case of requirement at the time of winding up.

**Unlimited company:** The companies which are with unlimited liability.

**Small company:** company with paid up capital up to Rs. 4 crore and turnover up to Rs. 40 crore.

**One Person Company:** A single and natural person can incorporate an One Person Company who is a resident and a citizen of India. The company should have minimum of one director. The company can have maximum of 15 directors.

## Topic

Module 1:  
Investment  
Decisions, Project  
Planning and  
Control

FINAL

Group III - Paper-14

Strategic Financial  
Management (SFM)

## Topic: Investment Decisions, Project Planning and Control

### Comprehensive Problem 1

The authority of Kolkata Railway Museum (KRM) has opened a cafeteria for its visitors. Yearly operations of the cafeteria have shown a consistent loss, which is expected to persist, as follows:

	₹	₹
Revenue (in cash)		200000
Expenses for food supplies etc. (in cash)	100000	
Salaries	110000	210000
Net loss		(10000)

The Meta-Vend Company has offered to sell automatic vending machines to KRM for ₹22,000, less a ₹3,000 trade-in allowance on old equipment (which is carried at ₹3,000 book value, and which can be sold outright for ₹3,000 cash) now used in the cafeteria operation. The useful life of the vending equipment is estimated at 10 years, with zero scrap value. Experience elsewhere has led executives to predict that the equipment will serve 50% more food than the cafeteria, with 50% less price. Therefore, the new revenue will probably be ₹150,000. The variety and mix of food sold are expected to be the same as for the cafeteria. A catering company will completely service and supply food and beverages for the machines, paying 10% of revenue to KRM and bearing all costs of food, repairs, and so on. All cafeteria employees will be discharged immediately. Their termination pay will total ₹35,000. However, an attendant who has some general knowledge of vending machines will be needed for one shift per day. The annual cost to KRM for the attendant will be ₹13,000.

For political and other reasons, the railroad will definitely not abandon its food service. The old equipment will have zero scrap value at the end of 10 years.

Using the preceding data, compute the following. Ignore income taxes.

- Use the NPV method to analyse the incremental investment. Assume a required rate of return of 10%. For this problem, assume that the PV of ₹1 at 10% to be received at the end of 10 years is ₹4.00 and that the PV of an annuity of ₹1 at 10% for 10 years is ₹6.000.
- What would be the minimum amount of annual revenue that KRM would have to receive from the catering company to justify making the investment? Show computations.

### Solution:

#### Analysis of Incremental Investment

	Analysis of Cash Flows		
	Present	Proposed	Difference
Revenue	₹200,000	₹15,000*	
Expenses:			
Miscellaneous	₹100,000		
Salaries	110,000	210,000	13,000
Net cash flow from operations	₹ (10,000)	₹ 2,000	₹12,000
Required investment:			
Equipment	₹ -	₹19,000**	
Termination pay	-	35,000	
Total	₹ -	₹54,000	₹54,000

\*  $10\% \times ₹150,000 = ₹15,000$  commission.

\*\* An acceptable alternative would be to show ₹3,000 and ₹22,000, respectively. The incremental investment would still be ₹19,000.

- Present value of ₹12,000 per year for  
10 years at 10% = ₹12,000 × 6.000 ₹72,000  
Required investment 54,000  
Net present value ₹18,000
- The minimum amount of annual revenue that KRM would have to receive to justify the investment would be that amount yielding an incremental net present value of zero. As the initial investment is constant, any change in the incremental net present value is due solely to a change in the amount of revenue. Therefore, the maximum drop in the incremental net present value of ₹18,000 equals the maximum drop in the present value of the revenue stream. This implies a maximum drop of ₹18,000 ÷ 6 = ₹3,000 in *annual* revenue and a minimum amount of annual revenue of ₹15,000 - ₹3,000 = ₹12,000.

Let X = Revenue at point of indifference, where net present value is zero

NPV= PV of (New annual cash flows - Old annual cash flows) – Required investment

$$0 = 6.000[(X - 13,000) - (-10,000)] - 54,000$$

$$0 = 6.000(X - 13,000 + 10,000) - 54,000$$

$$0 = 6.000(X - 3,000) - 54,000$$

$$0 = 6.000X - 18,000 - 54,000$$

$$6.000X = 72,000$$

$$X = 12,000$$

The minimum amount of annual revenue that KRM would have to receive from the catering company to justify making the investment is ₹12,000.

## Comprehensive Problem 2

Mr. Smith, the owner of a seven-hole golf course on the outskirts of a city, is considering a proposal that the course be illuminated and operated at night. Mr. Smith purchased the course in 2024 for ₹480,00,000. Her receipts from operations during the 28-week season were ₹135,00,000. Total disbursements for the year, for all purposes, were ₹84,00,000.

The required investment in lighting this course is estimated at ₹90,00,000. The system will require 300 lamps of 1,000 watts each. Electricity costs ₹8.00 per kilowatt-hour. The expected average hours of operation per night is 5. Because of occasional bad weather and the probable curtailment of night operation at the beginning and end of the season, it is estimated that there will be only 130 nights of operation per year. Labor for keeping the course open at night will cost ₹7,500 per night. Lightbulb cost is estimated at ₹1,50,000 per year; other maintenance and repairs, per year, will amount to 4% of the initial cost of the lighting system. Annual property taxes on this equipment will be about 1.7% of its initial cost. It is estimated that the average revenue, per night of operation, will be ₹42,000 for the first 2 years.

Considering the probability of competition from the illumination of other golf courses, Mr. Smith decides that he will not make the investment unless he can make at least 10% per annum on his investment. Because of anticipated competition, revenue is expected to drop to ₹30,000 per night for years 3–5. It is estimated that the lighting equipment will have a salvage value of ₹35,00,000 at the end of the 5-year period.

Using DCF techniques, determine whether Mr. Smith should install the lighting system.

### Solution:

The initial purchase cost of the golf course and the operating receipts and disbursements for the first season of ownership are irrelevant to the present decision. The relevant annual costs which Mr. Smith should take into consideration are:

Electricity, (300 × 1 KW) × (130 × 5 hrs.) × ₹8.00 per KWH	₹15,60,000
Labor cost, 130 × ₹7500	9,75,000
Light bulb cost	1,50,000
Repairs and maintenance of lighting system, .04 × ₹90,00,000	3,60,000

Property taxes, $.017 \times ₹90,00,000$	1,53,000
Total additional operating expenses	₹31,98,000
Annual revenue from night operations:	
Years 1 and 2: $130 \times ₹42,000$	₹54,60,000
Years 3, 4, and 5: $130 \times ₹30,000$	₹39,00,000
One-time cash flows:	
Present value of initial investment	₹90,00,000
Salvage value, year 5	₹35,00,000

## Cash Flow Analysis

	Revenue	Expenses	Net Flow	PV Factor	PV of Cash Flows
Year 1	₹54,60,000	- ₹31,98,000	= ₹22,62,000	.9091	₹20,56,400
Year 2	54,60,000	- 31,98,000	= 22,62,000	.8264	18,69,300
Year 3	39,00,000	- 31,98,000	= 7,02,000	.7513	5,27,400
Year 4	39,00,000	- 31,98,000	= 7,02,000	.6830	4,79,500
Year 5	74,00,000	- 31,98,000	= 42,02,000	.6209	26,09,000
Present value of cash flows					₹75,41,600

Since the present value of the annual cash flows is ₹14,58,400 less than the initial investment of ₹90,00,000, the proposed lighting system should not be installed.

**Comprehensive Problem 3**

X Ltd. is considering two possible investments, each of which requires an initial investment of ₹36,000. Investment A will provide a cash flow of ₹4,000 at the end of each year for 20 years. Investment B will provide a cash flow of ₹4,500 at the end of each year for 8 years.

1. Determine the payback period for each investment. Which investment is most desirable using the payback method?
2. Compute the NPV of each investment using a required rate of return of 8%. Which investment is most desirable using the NPV method?
3. Explain why the payback method does not lead to an optimal decision for the Stallone Company.

**Solution:**

1. Investment A payback period:  $₹36,000 \div ₹4,000 = 9$  years

Investment B payback period:  $₹36,000 \div ₹4,500 = 8$  years

Investment B has the shorter payback period, so it seems more desirable using the payback model.

2. NPV of A:  $₹4,000 \times 9.8181 - ₹36,000 = ₹39,272 - ₹36,000 = ₹3,272$

NPV of B:  $₹4,500 \times 5.7466 - ₹36,000 = ₹25,860 - ₹36,000 = ₹(10,140)$

Investment A has the higher NPV, so it is more desirable. In fact, investment B has a negative NPV, so it would reduce the value of X Ltd.

3. The payback model does not consider the overall profitability of the two investments. It ignores all cash flows beyond the payback period and gives all cash inflows during the payback period the same value as dollars at time zero, regardless of when received. Although investment B returns its investment in 8 years, it has no additional cash flows. Investment A returns its investment more slowly, but the 12 extra years of ₹4,000 annual cash flows make it more valuable than investment B.

## Topic

Module 1:  
Assessment  
of Income and  
Computation of Tax  
Liability of Various  
Entities

## FINAL

### Group III - Paper-15

Direct Tax Laws  
and International  
Taxation (DIT)

## Guide to Minimum Alternate Tax (MAT) under Section 115JB

### Introduction and Historical Context of MAT

In India's corporate tax framework, Minimum Alternate Tax (MAT) serves as a vital tool to ensure tax equity by bringing "zero-tax companies" into the tax net. At times it may happen that a taxpayer, being a company, may have generated substantial income during the year, but by taking the advantage of various provisions of the Income-tax Law (like exemptions, deductions, depreciation, etc.), it may have reduced its tax liability to a negligible amount, or it may not have paid any tax at all.

The primary objective of the introduction of MAT is to bring these "zero-tax companies" into the tax net. These are companies which, in spite of having earned substantial book profits and having paid handsome dividends to their shareholders, do not pay any tax due to the various tax concessions and incentives provided under the Income-tax Law.

Due to the rapid increase in the number of such zero-tax paying companies, MAT was initially introduced in mid of 80'. Later on, it was withdrawn by the Finance Act, 1990, and was subsequently reintroduced by the Finance (No. 2) Act, 1996, with effect from 1-4-1997. Introduced specifically to prevent the misuse of exemptions and deductions, MAT is now levied under section 115JB on the book profits of a company. Since its reintroduction, several changes have been made to the provisions of MAT, and today it is levied on companies strictly as per the comprehensive provisions of section 115JB. This statutory provision reflects a significant shift from traditional income-based taxation to a profit-based minimum taxation system, playing a critical role in the strategic tax planning and compliance requirements for corporate entities.

### Basic Provisions and the Concept of MAT

As per the core concept of MAT, the final tax liability of a corporate assessee will be the higher of two specific computations:

- 1. Normal Tax Liability:** The tax liability of the company computed as per the normal provisions of the Income-tax Law. This means the tax computed on the taxable income of the company by applying the regular tax rate applicable to that specific company. Tax computed in this manner can be termed as the normal tax liability or regular tax liability.
- 2. MAT Liability:** The tax computed at the rate of 15%<sup>1</sup> on the "book profit" of the company. The tax computed by applying this 15% rate on the book profit is called the Minimum Alternate Tax (MAT).

Therefore, a company has to pay the higher of the normal

tax liability or the liability calculated as per the MAT provisions.

**Concessional Rate for IFSC Units:** It is important to note an exception to the standard 15% rate. MAT is levied at a concessional rate of 9% (as increased by applicable surcharge and cess) in the case of a company that is a unit of an International Financial Services Centre (IFSC) and derives its income solely in convertible foreign exchange.

### Applicability and Non-Applicability of MAT

As per section 115JB, every taxpayer being a company is liable to pay MAT if the income-tax payable on the total income, computed as per the normal provisions of the Income-tax Act in respect of any year, is less than 15% of its book profit.

However, to promote certain alternative tax regimes and specific business sectors, the provisions of MAT are strictly not applicable to the following entities:

- Domestic companies which have explicitly opted for the concessional tax regimes under section 115BAA or section 115BAB.
- Any income accruing or arising to a company from the life insurance business referred to in section 115B.
- A shipping company, provided the income of such company is subject to tonnage taxation.

**Exemptions for Foreign Companies:** Further, as per Explanation 4 to section 115JB, it is clarified that MAT provisions shall not be applicable, and shall be deemed never to have been applicable, to an assessee being a foreign company, if:

- The assessee is a resident of a country or a specified territory with which India has an agreement referred to in section 90(1), or the Central Government has adopted any agreement under section 94A(1), and the assessee does not have a permanent establishment in India in accordance with the provisions of such agreement; or
- The assessee is a resident of a country with which India does not have an agreement of the nature referred to above, and the assessee is not required to seek registration under any law for the time being in force relating to companies.

Additionally, as per Explanation 4A to section 115JB, MAT provisions shall not be applicable to a foreign company whose total income comprises profits and gains arising from businesses referred to in section 44AB, 44BB, 44BBA, or 44BBB, provided such income has been offered to tax at the rates specified in those respective sections.

<sup>1</sup> As increased by applicable surcharge and cess

## Computation of Book Profit

The entire MAT mechanism revolves around the correct calculation of “Book Profit.” As per Explanation 1 to section 115JB(2), “book profit” for the purposes of section 115JB means the net profit as shown in the statement of profit and loss, prepared in accordance with Schedule III to the Companies Act, 2013. This base net profit is then strictly increased and decreased by certain statutory items prescribed in this regard.

### A. Additions to Net Profit

The following items must be added back to the net profit if they have been debited to the statement of Profit and Loss:

- Income-tax paid or payable, and the provision thereof.
- Amounts carried to any reserves, by whatever name called (other than a reserve specified under section 33AC).
- Provisions for unascertained liabilities.
- Provisions for losses of subsidiary companies.
- Dividends paid or proposed.
- Expenditure related to incomes which are exempt under section 10 (excluding section 10AA), section 11, and section 12.
- The amount or amounts of expenditure relatable to income, being the share of the taxpayer in the income of an association of persons or body of individuals, on which no income-tax is payable in accordance with the provision of section 86.
- The amount or amounts of expenditure relatable to income accruing or arising to a taxpayer, being a foreign company, from the capital gains arising on transactions in securities, or the interest, dividend, royalty, or fees for technical services chargeable to tax at the rates specified in Chapter XII (if the income-tax payable on the above income is less than the rate of MAT).
- The amount representing notional loss on the transfer of a capital asset, being a share of a special purpose vehicle to a business trust in exchange for units allotted by that trust referred to in section 47(xvii), or the amount representing notional loss resulting from any change in the carrying amount of said units, or the amount of loss on transfer of units referred to in section 47(xvii).
- Expenditure relatable to income by way of royalty in respect of a patent chargeable to tax under section 115BBF.
- Amount of depreciation debited to the Profit & Loss Account.

- Deferred tax and the provision thereof.
- Provision for diminution in the value of any asset.
- The amount standing in the revaluation reserve relating to a revalued asset on the retirement or disposal of such an asset, if not credited to the statement of profit and loss.
- The amount of gain on the transfer of units referred to in section 47(xvii) computed by taking into account the cost of the shares exchanged with units referred to in the said clause, or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through the statement of profit and loss, as the case may be.

### B. Deductions from Net Profit

The following items must be reduced from the net profit if they have been credited to the statement of profit and loss:

- Amount withdrawn from any reserve or provision.
- Incomes which are exempt under section 10 (excluding section 10AA), section 11, and section 12.
- Amount of depreciation debited to the statement of profit and loss (excluding the depreciation on revaluation of assets).
- Amount withdrawn from the revaluation reserve and credited to the statement of profit and loss, to the extent it does not exceed the amount of depreciation on the revaluation of assets.
- The amount of income, being the share of the taxpayer in the income of an association of persons or body of individuals, on which no income-tax is payable in accordance with the provisions of section 86.
- The amount of income accruing or arising to a taxpayer being a foreign company, from capital gains arising on transactions in securities, or interest, dividend, royalty, or fees for technical services chargeable to tax at the rates specified in Chapter XII (if the income-tax payable on the above income is less than the rate of MAT).
- The amount representing notional gain on the transfer of a capital asset, being a share of a special purpose vehicle to a business trust in exchange for units allotted by that trust referred to in section 47(xvii), or notional gain resulting from any change in the carrying amount of said units, or gain on transfer of units referred to in section 47(xvii).
- Income by way of royalty in respect of a patent chargeable to tax under section 115BBF.
- Aggregate amount of unabsorbed depreciation and loss brought forward in specific cases, such as a company whose Board has been suspended

under section 241 of the Companies Act, 2013, or a company against whom an application for the corporate insolvency resolution process has been admitted under section 7, section 9, or section 10 of the Insolvency and Bankruptcy Code, 2016.

- Amount of brought forward loss or unabsorbed depreciation, whichever is less as per the books of account (applicable in the case of a company other than a company undergoing insolvency proceedings).
- Profits of a sick industrial company till its net worth becomes zero or positive.
- Deferred tax, if credited to the statement of profit and loss.

### Understanding the MAT Credit Mechanism

MAT was introduced to limit tax deductions and exemptions so that companies pay a “minimum” amount as tax to the government. However, to maintain fairness, the MAT framework operates with a “MAT credit” carry-forward mechanism. This mechanism allows a company to carry forward the “excess” tax paid due to MAT (as against its normal tax liability) in a tax year, to be utilized in the future as a credit to offset its regular tax liability.

If in any year the company pays tax liability as per MAT, then it is legally entitled to claim credit of the MAT paid over and above the normal tax liability in the subsequent years. The precise provisions relating to the carry forward and adjustment of MAT credit are given in section 115JAA.

A company is entitled to claim MAT credit (i.e., the excess of MAT paid over the normal tax liability), and this credit can be utilized by the company in subsequent years. The credit can be adjusted strictly in the year in which the liability of the company as per the normal provisions is more than its MAT liability. The set-off in respect of brought forward MAT credit shall be allowed in the subsequent years to the extent of the difference between the tax on its total income as per the normal provisions and the tax as per the MAT provisions.

It is crucial to note that the MAT credit can be carried forward only for a maximum period of 15 years, after which it will lapse. In other words, if MAT credit cannot be utilized by the company within a period of 15 years (immediately succeeding the assessment year in which such credit was originally generated), then such credit will permanently lapse. Furthermore, no interest is paid by the government to the taxpayer in respect of such MAT credit.

### Compliance and Other Statutory Provisions

Every company to whom the provisions of section 115JB apply is required to comply with specific reporting standards. The company shall upload a report in the prescribed form, which is Form No. 29B, from an accountant. This report certifies that the book profit has been computed strictly in accordance with the provisions of this section, and it must be uploaded one month prior to the due date of the filing of the return of income under section 139.

Finally, it should be noted that all other provisions of the Income-tax Act, such as the requirements for paying Advance Tax, the levy of interest, etc., shall continue to apply to every company mentioned in this section.

### Conclusion

Minimum Alternate Tax (MAT) plays a crucial and undeniable role in ensuring that companies with substantial book profits contribute a fair and equitable share of taxes to the exchequer, even if they avail of various legitimate exemptions and deductions under the Income-tax Act. By mandating a minimum tax based strictly on book profits, MAT vigorously promotes equity among corporate taxpayers and actively prevents the phenomenon of “zero-tax companies”. Consequently, companies and their financial advisors must carefully consider MAT provisions in their overall tax planning and corporate financial decision-making processes.

## Topic

Module 1:  
Introduction to  
Strategic Cost  
Management

# FINAL

## Group III - Paper-16

### Strategic Cost Management (SCM)

## Cost Control & Cost Reduction

### Meaning of Cost Control:

Cost Control is the process of planning and regulating costs so that they remain within predetermined limits and are incurred efficiently in achieving organizational objectives.

It involves:

- Setting cost targets
- Monitoring actual performance
- Comparing with planned figures
- Taking corrective action

### Objectives of Cost Control:

- Ensure efficient use of resources
- Minimize wastage and losses
- Maintain costs within planned limits
- Improve operational efficiency
- Fix responsibility for cost incurrence

### Steps in Cost Control:

1. Setting Targets
  - Establish cost targets using budgets, forecasts, or past data
2. Assigning Responsibility
  - Allocate responsibility to departments or managers
  - Define cost centres or responsibility centres
3. Recording Actual Performance
  - Collect data on actual costs incurred
  - Use proper accounting and reporting systems
4. Comparison
  - Compare actual costs with planned or budgeted costs
5. Analysis of Deviations
  - Identify and analyze differences between actual and planned costs
  - Determine causes of inefficiencies or excess costs
6. Corrective Action
  - Take necessary steps to control costs
  - Improve processes and eliminate inefficiencies

### 7. Continuous Review

- Regular monitoring and feedback
- Revise targets and methods when required

### Tools of Cost Control:

- Budgetary Control
- Standard Costing
- Responsibility Accounting
- Marginal Costing
- Management Reporting Systems

### Meaning of Cost Reduction:

Cost Reduction is the process of achieving a real and permanent decrease in unit cost without affecting the quality, efficiency, or suitability of the product or service.

### Objectives of Cost Reduction:

- Reduce cost per unit permanently
- Improve profitability
- Eliminate waste and inefficiencies
- Optimize use of resources
- Enhance competitiveness

### Features of Cost Reduction:

- It is a continuous process
- Ensures no compromise in quality
- Focuses on innovation and improvement
- Results in permanent savings

### Techniques of Cost Reduction:

1. Value Engineering
  - Examination of product design at the planning stage
  - Aims to eliminate unnecessary costs before production begins
2. Process Improvement
  - Simplification and improvement of production methods
  - Better workflow and efficiency
3. Technology Upgradation
  - Use of advanced machinery or automation
  - Reduces cost through higher productivity

4. Waste Reduction
  - Elimination of material wastage, idle time, defects, etc.
5. Efficient Purchasing
  - Better sourcing, supplier negotiation, bulk buying
6. Work Study
  - Improves labour efficiency through method and time study
7. Value Analysis
  - Examination of existing products and processes
  - Aims to reduce cost after production has started

#### Cost Control vs Cost Reduction:

Basis	Cost Control	Cost Reduction
Objective	Maintain costs within limits	Reduce costs permanently
Nature	Preventive	Corrective and progressive
Focus	Following plans	Improving processes
Time Frame	Short-term	Long-term
Approach	Based on targets	Challenges existing methods
Example	Ensuring material cost does not exceed ₹100 per unit (as per budget)	Finding a new supplier to bring cost down to ₹85 per unit permanently

#### Relationship Between Cost Control and Cost Reduction:

- Cost control is the foundation for cost reduction
- Cost reduction begins where cost control ends

- Both aim at improving efficiency and profitability
- Cost control maintains costs within limits, while cost reduction lowers those limits
- They are complementary, not alternative concepts

In practice, organizations first control costs, then look for ways to reduce them further

#### Case Study: Toyota Motor Corporation

A well-known example is Toyota Motor Corporation, which implemented lean manufacturing and continuous improvement techniques

#### Background:

Toyota Motor Corporation developed an efficient production system to remain competitive in the global automobile industry.

#### Measures Taken:

##### Cost Control:

- Use of budgeting and production planning
- Monitoring costs at each stage of production
- Maintaining efficiency in operations

##### Cost Reduction:

- Adoption of Kaizen (continuous improvement)
- Elimination of waste (lean manufacturing)
- Efficient inventory management (Just-in-Time)
- Continuous process innovation

##### Results:

- Reduction in production costs
- Improved product quality
- Higher operational efficiency
- Strong global competitive position

## Topic

Module 9:  
Basics of  
Management Audit

Module 14:  
Internal Control and  
Internal Audit

FINAL

Group IV - Paper-17

Cost and  
Management Audit  
(CMAD)

## Cost and Management Audit

### MANAGEMENT AUDIT

Management Audit is a systematic and independent evaluation of managerial performance, policies, and decision-making processes to assess efficiency, effectiveness, and economy in achieving organizational objectives.

Management audit is important because it evaluates managerial efficiency, decision-making quality, and overall organizational performance beyond mere financial accuracy. It helps identify weaknesses in planning, coordination, and control systems, thereby improving productivity and strategic alignment. By reviewing policies and operational effectiveness, management audit strengthens accountability and corporate governance mechanisms (Gupta, 2020). It also supports optimal resource utilization and long-term sustainability through performance appraisal and corrective recommendations. Management audit acts as a tool for continuous improvement and enhances organizational competitiveness in dynamic business environments (Mishra & Puri, 2019). Hence it can be construed that it goes beyond financial verification and focuses on **quality of management functions**.

#### Advantages of Management Audit

Management audit offers several strategic and operational advantages to an organization:

- 1. Improves Managerial Efficiency:** It evaluates managerial performance and identifies inefficiencies in planning, organizing, directing, and controlling functions.
- 2. Enhances Decision-Making:** By reviewing policies and procedures, it supports informed and rational decision-making at top management levels.
- 3. Strengthens Corporate Governance:** Management audit promotes transparency, accountability, and ethical conduct within the organization.
- 4. Better Resource Utilization:** It ensures optimum use of financial, human, and physical resources, reducing wastage and improving productivity.
- 5. Identifies Weaknesses and Risks:** The audit highlights operational gaps and potential risks, enabling timely corrective action.
- 6. Promotes Strategic Alignment:** It assesses whether organizational activities align with long-term objectives and mission.
- 7. Facilitates Continuous Improvement:** Recommendations provided help in modernizing systems and improving overall organizational effectiveness.

- 8. Supports Growth and Competitiveness:** By improving performance and control systems, it enhances sustainability and competitive advantage.

#### Scope

- Organizational structure
- Strategic planning
- Production and operations
- Human resource management
- Financial management
- Marketing performance
- Risk management

#### Key Features

- Forward-looking approach
- Focus on performance improvement
- Analytical and diagnostic in nature
- Covers both financial and non-financial areas

#### Advantages

- Enhances managerial efficiency
- Strengthens accountability
- Improves resource utilization
- Supports strategic decision-making

### INTERNAL CONTROL

#### Meaning

Internal Control is a system of policies, procedures, and mechanisms designed to provide reasonable assurance regarding:

- Reliability of financial reporting
- Effectiveness and efficiency of operations
- Compliance with laws and regulations
- Safeguarding of assets

#### Objectives

- Prevent fraud and errors
- Ensure accuracy of accounting records
- Protect company assets
- Promote operational efficiency
- Ensure regulatory compliance

## Components of Internal Control

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring Activities

## Types of Internal Controls

Internal controls are mechanisms established by management to ensure operational efficiency, reliability of financial reporting, and compliance with laws and regulations. According to the Committee of Sponsoring Organizations of the Treadway Commission (COSO, 2013), internal controls are embedded within organizational processes and may be classified as follows:

### Preventive Controls

These controls are designed to prevent errors or fraud before they occur. Examples include segregation of duties, authorization procedures, access controls, and approval hierarchies. Preventive controls reduce the likelihood of irregularities and are considered proactive in nature (Arens, Elder, & Beasley, 2020).

### Detective Controls

Detective controls identify errors or irregularities after they have occurred. Examples include bank reconciliations, internal audits, physical stock verification, and variance analysis. These controls help detect and correct misstatements in a timely manner (COSO, 2013).

### Corrective Controls

Corrective controls are implemented to rectify identified errors and prevent recurrence. Examples include backup recovery systems, disciplinary actions, and process revisions (Gupta, 2020).

### Manual Controls

These are performed by individuals, such as supervisory reviews, physical verification, and approval signatures.

### Automated (IT) Controls

These controls operate through information systems, such as password protections, system validations, and automated transaction processing. They enhance reliability and reduce human intervention risks (Arens et al., 2020).

### Administrative and Accounting Controls

Administrative controls relate to operational efficiency and policy compliance, while accounting controls focus on safeguarding assets and ensuring accurate financial records.

## Limitations

Despite its advantages, management audit has certain inherent limitations:

**Subjectivity in Evaluation:** Assessment of managerial performance often involves qualitative judgment, which may vary depending on the auditor's experience and perspective.

**Lack of Standardized Procedures:** Unlike statutory audit, management audit does not follow universally prescribed standards, leading to variations in scope and methodology.

**Resistance from Management:** Managers may perceive it as interference in their decision-making authority, resulting in non-cooperation or incomplete disclosure.

**Cost and Time Intensive:** Conducting a comprehensive management audit requires significant time, expertise, and financial resources.

**Difficulty in Measuring Efficiency:** Managerial effectiveness is difficult to quantify, especially in areas such as leadership, motivation, and strategic thinking.

**Not Legally Mandatory in Most Cases:** Since it is generally voluntary (except in special investigations), organizations may not implement recommendations seriously.

**Possibility of Bias:** Internal evaluators may lack complete independence, while external auditors may not fully understand organizational culture.

**Implementation Gap:** Recommendations may not be effectively implemented, reducing the practical impact of the audit.

Thus, while management audit is a valuable tool for performance improvement, its effectiveness depends largely on objectivity, cooperation, and management commitment.

## INTERNAL AUDIT

**Institute of Internal Auditors defined Internal Audit as** - "It is an independent, objective assurance and consulting activity designed to *add value and improve an organisation's operations*. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control and governance process."

It evaluates:

- Internal controls
- Risk management processes
- Governance systems

**Objectives**

- Evaluate adequacy of internal controls
- Assess risk management effectiveness
- Ensure compliance with policies
- Detect and prevent fraud
- Improve operational efficiency

**Characteristics**

- Independent within organization
- Continuous process
- Advisory role to management
- Risk-based approach

**Difference Between Management Audit, Internal Control & Internal Audit**

Management audit, internal control, and internal audit are integral components of modern corporate governance frameworks. A management audit evaluates managerial efficiency, strategic effectiveness, and policy implementation to enhance organizational performance (Sharma, 2018). Internal control refers to structured processes designed to ensure operational efficiency,

reliability of financial reporting, and compliance with laws; the widely recognized framework developed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO, 2013) identifies five core components of internal control. Internal audit, as defined by the Institute of Internal Auditors (IIA, 2020), provides independent assurance and consulting services to improve risk management, governance, and control systems.

The legal position of management audit, internal control, and internal audit in India is primarily governed by the Companies Act, 2013. Internal control has statutory recognition under Section 134(5)(e), which requires directors to establish adequate internal financial controls and ensure their effectiveness. Section 143(3)(i) mandates statutory auditors to report on the adequacy and operating effectiveness of such controls. Internal audit is compulsory for specified classes of companies under Section 138 and the Companies (Accounts) Rules, 2014. In contrast, management audit is not universally mandatory but may be directed by the Central Government under Section 210 in cases of investigation. Thus, internal control and internal audit have explicit legal backing, whereas management audit is situational and investigative in nature.

Basis	Management Audit	Internal Control	Internal Audit
Nature	Evaluation of management performance	System of checks & procedures	Independent review function
Legality	Optional	Stipulated by Companies Act 2013	
Objective	Improve managerial efficiency	Prevent errors & fraud	Evaluate and improve controls
Scope	Strategic & operational	Organization-wide	Risk-based review
Responsibility	External/Independent team	Management responsibility	Internal audit department
Focus	Effectiveness & performance	Safeguarding & compliance	Assurance & advisory

**RELATIONSHIP AMONG Management Audit, Internal Control and Internal Audit**

- **Internal Control** is the system.
- **Internal Audit** evaluates the system.
- **Management Audit** evaluates managerial performance and overall effectiveness.

Together, it strengthens:

- Corporate governance
- Risk management
- Organizational accountability

## Topic

Module 1:

Specific Accounting Standards

Module 2:

Valuation of Shares (including Determination of Goodwill, Post-valuation of Tangible and Intangible Assets)

FINAL

Group IV - Paper-18

Corporate Financial Reporting (CFR)

## Topic: Specific Accounting Standards

### Comprehensive Problem 1

A Ltd. has leased equipment over its useful life that costs ₹14,93,10,200 for a three-year lease period starting from 01.04.2025. After the lease term the asset would revert to the Lessor. You are informed that:

The estimated unguaranteed residual value would be ₹2 lakh only.

The annual lease payments have been structure in such a way that the sum of their present values together with that of the residual value of the asset will equal the cost thereof.

Implicit interest rate is 10%.

Ascertain (i) the annual lease payment and (ii) the unearned finance income P.V. factor @10% for years 1 to 3 are 0.909, 0.826 and 0.751 respectively.

#### Solution:

##### (i) Calculation of Annual Lease Payment

	₹
Cost of the equipment	14,93,10,200
Unguaranteed Residual Value	2,00,000
PV of unguaranteed residual value of 3 years @ 10% (₹2,00,000 × 0.751)	1,50,200
Fair value to be recovered form Lease Payment (₹14,93,10,200 – ₹1,50,200)	14,91,60,000
PV Factor for 3 years @ 10%	2.486
Annual Lese Payment (₹14,91,60,000/ PV Factor for 3 years @10% i.e., 2.486)	6,00,00,000

##### (ii) Unearned Finance Income

	₹
Total lease payments [₹6,00,00,000 × 3]	18,00,00,000
Add: Residual value	<u>2,00,000</u>
Gross Investments	18,02,00,000
Less: Present value of Investments (₹14,91,60,000 + ₹1,50,200)	<u>(14,93,10,200)</u>
Unearned Finance Income	<u>3,08,89,800</u>

### Comprehensive Problem 2

P Ltd. acquired a machine on 1st April, 2017 for ₹7 crores that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 2021, the carrying value of the machine was reassessed at ₹5.10 crores and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended March 2023, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only ₹0.79 crores. The company had followed the policy of writing down the revaluation surplus by the increased charge of deprecation resulting from the revaluation.

You are required to calculate the loss on impairment of the machine and show how this loss is to be treated in the books of P Ltd.

**Solution:****Statement Showing Impairment Loss**

		(₹ in crores)
Carrying amount of the machine as on 1 <sup>st</sup> April 2017		7.00
Depreciation for 4 years i.e., 2017-18 to 2020-21 [(7 crores/7 years) × 4 years]		<u>(4.00)</u>
Carrying amount as on 31.03.2021		3.00
Add: Upward Revaluation (credited to Revaluation Reserve account)		<u>2.10</u>
Carrying amount of the machine as on 1 <sup>st</sup> April 2021 (revalued)		5.10
Less: Depreciation for 2 years i.e., 2021-22 & 2022-23 [(5.10 crores/3 years) × 2 years]		<u>(3.40)</u>
Carrying amount as on 31.03.2023		1.70
Less: Recoverable amount		<u>(0.79)</u>
Impairment loss		0.91
<b>Less: Balance in revaluation reserve as on 31.03.2023</b>		
Balance in revaluation reserve as on 31.03.2021	2.10	
Less: Enhanced depreciation met from revaluation reserve		
2021-22 & 2022-23 = (1.70 - 1.00) × 2 years	<u>(1.40)</u>	
Impairment loss set off against revaluation reserve balance as per para 60 of Ind AS 36, Impairment of Assets		<u>(0.70)</u>
Impairment Loss to be debited to Profit and Loss Account		<u>0.21</u>

**Topic: Valuation of Shares****Multiple Choice Questions – Numerical**

Normal dividend expected on equity shares of A Ltd. is 8%. The profit available to equity shareholders is ₹ 7,66,250 and value of net asset for equity shareholders is ₹81,64,000. Calculate value of each equity share under fair value method if number of outstanding equity share is 2,00,000 and face value is ₹10.

- A. ₹ 44.36  
 B. ₹ 46.26  
 C. ₹ 47.89  
 D. None of the above

**Solution:**

Breakup value per share = ₹ 81,64,000/2,00,000 = ₹ 40.82

Yield on Equity Share = (7,66,250/20,00,000) \* 100 = 38.3125%

Value per share on yield basis = (38.3125/8) \* ₹10 = ₹47.89

Fair value per share = ₹ (40.82 + 47.89)/2 = ₹ 44.36

So, the correct option is (A)

**Comprehensive Problem 1**

Following is the Balance Sheet of X Ltd. as at 31<sup>st</sup> March, 2024:

Particulars	Amount (₹)
<b>Assets</b>	
<b>Non-current Assets</b>	
Property, Plant and Equipment	26,60,000
Goodwill	4,00,000
Patent	2,00,000
Investments (at face value)	8,40,000
<b>Current Assets</b>	
Inventories	2,00,000
Trade Receivables (Sundry debtors)	14,00,000
Cash and cash equivalent	2,00,000
<b>Total</b>	59,00,000
<b>Equity and Liabilities</b>	
<b>Equity</b>	
Equity Share Capital of ₹10 each, fully paid	11,00,000
Equity Share Capital of ₹10 each, ₹9 paid	9,00,000
8%, Compulsorily Convertible Preference Shares (₹100)	8,00,000
General Reserve	7,20,000
Retained Earnings	5,00,000
<b>Non-current Liabilities</b>	4,00,000
10% Debentures	
<b>Current Liabilities</b>	10,80,000
Trade Payables (Sundry creditors)	4,00,000
Bank overdraft	
<b>Total</b>	59,00,000

**Additional information:**

- (i) PPE are worth 25% above their actual book value. Depreciation on appreciated value of PPE is not to be considered for valuation of goodwill. Patent is valueless.
- (ii) 70% of the Investments are non-trading and the balance is trading. All investments are to be valued at 20% above cost. Dividend at uniform rate of 20% is earned on all investments.
- (iii) Goodwill is to be valued based on super profit which is likely to be sustained for next 3 years. The discount rate is 10%. Profit (after 40% tax) are as follows:

Year	₹
2021-2022	6,40,000
2022-2023	5,80,000
2023-2024	6,20,000

(iv) In 2021-2022, one item of machinery with W.D.V. of ₹40,000 was sold at ₹40,000 but wrongly taken to revenue from operation. No effect has been given yet to rectify the same. Depreciation is charged on machinery @ 10% p.a. under diminishing balance method.

(v) In similar businesses, return on capital employed is 10%. The P/E ratio is 8.

(vi) Applicable weights for calculation of weighted average profits are 1, 2 and 3 for 2021-22, 2022-23 and 2023-24.

Find out the net asset backing value of each fully and partly paid equity share.

**Solution:**

(1) Average trading profit after taxes of the last 3 years:

Particulars	2021-22	2022-23	2023-24
	₹	₹	₹
Profit after tax @ 40%	6,40,000	5,80,000	6,20,000
Less: Sale proceeds of machine wrongly charged to revenue (40,000×60%)	24,000	---	---
Add: Depreciation at 10% on machinery less tax 40%	2,400	2,160	1,944
Add: Interest on debenture (400000 × 10% × 60%)	24,000	24,000	24,000
Less: Income from non-trading investments, net of tax @ 40% (8,40,000 × 70% × 20% × 60%)	(70560)	(70560)	(70560)
	5,71,840	5,35,600	5,75,384

Weighted average trading profit after taxes will be: ₹(5,71,840 × 1 + 5,35,600 × 2 + 5,75,384 × 3)/6 = ₹5,61,532

(2) Average trading capital employed on 31.03.2024:

Particulars	₹
PPE (26,60,000 - 40,000 × 90% × 90% × 90%) × 125%	32,88,550
Goodwill	4,00,000
Patent	Nil
Trade Investments (8,40,000 × 30% × 120%)	3,02,400
Inventories	2,00,000
Trade Receivables	14,00,000
Cash and cash equivalent	2,00,000
	57,90,950
Less: Current liabilities	4,00,000
Bank o/d	10,80,000
Trade Payables	
Trading capital employed on 31.03.2024	43,10,950
Less: ½ of current year's trading profit after taxes (5,75,384 × 1/2)	2,87,692
Average trading capital employed on 31.03.2024	40,23,258

Value of goodwill:

Particulars	₹
Weighted average annual maintainable trading profit after taxes	5,61,532
Less: Normal return on average capital employed (40,23,258 × 10%)	4,02,326
Super profit	1,59,206

Goodwill = Super profit × PVIFA (10%, 3) = ₹ 1,59,206 × 2.486 = ₹ 3,95,786

#### Valuation of Equity Shares (Net Asset Method)

Particulars	₹
Trading capital employed on 31. 03. 2022	43,10,950
Add: Computed Goodwill	3,95,786
Market value of non-trading investments (8,40,000 × 70% × 120%)	7,05,600
	54,12,336
Less: Purchased goodwill as per balance sheet	4,00,000
Less: 10% debentures	4,00,000
Net assets available for business	46,12,336
Less: Preference share capital	8,00,000
	38,12,336
Add: Notional Call (1,00,000 × 1)	1,00,000
Net assets available for equity shares	39,12,336

Value per fully paid shares = 39,12,336 ÷ 210000 = ₹18.63

Value per partly paid shares = ₹18.63 – Rs.1.00 = ₹17.63

## Topic

Module 1:  
Supply under GST -  
A Refresh

FINAL

Group IV - Paper-19

Indirect Tax Laws  
and Practice (ITLP)

## Supply Under GST

The taxable event in GST is the supply of goods or services or both. Various taxable events like manufacture, sale, rendering of service, purchase, entry into a territory of state etc. have been done away with in favour of just one event i.e. supply. The constitution defines “Goods and Services Tax” as any tax on supply of goods, or services or both, except for taxes on the supply of alcoholic liquor for human consumption. To capture the broad scope of this regime, the GST law provides an inclusive definition of “supply”.

### The Six Parameters of Supply

The meaning and scope of supply under GST can be understood in terms of the following six parameters, which can be adopted to characterize a transaction as supply:

- **Supply of goods or services:** Supply of anything other than goods or services does not attract GST.
- **Consideration:** Supply should be made for a consideration.
- **Business Purpose:** Supply should be made in the course or furtherance of business.
- **Taxable Person:** Supply should be made by a taxable person.
- **Taxable Supply:** Supply should be a taxable supply.
- **Taxable Territory:** Supply should be made within the taxable territory.

While these six parameters describe the concept of supply, there are a few exceptions to the requirement of supply being made for a consideration and in the course or furtherance of business. Any transaction involving the supply of goods or services without consideration is not a supply, barring a few exceptions, in which a transaction is deemed to be a supply even without consideration. Further, the import of services for a consideration, whether or not in the course or furtherance of business is treated as supply.

### Defining “Goods” and “Services”

Goods as well as services have been defined in the GST Law.

- **Exclusions:** The securities are excluded from the definition of goods as well as of services. Money is also excluded from the definition of goods as well as services, however, activities relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a separate consideration is charged are included in services.

- **Schedule II Clarifications:** Schedule II to the CGST Act, 2017 lists a few activities which are to be treated as supply of goods or supply of services. For instance, any transfer of title in goods would be a supply of goods, whereas any transfer of right in goods without transfer of title would be considered as services.

### The Negative List (Schedule III)

Further Schedule III to the CGST Act, 2017 spells out activities which shall be treated as neither supply of goods nor supply of services or outside the scope of GST. This includes:

- Services by an employee to the employer in the course of or in relation to his employment.
- Services of funeral, burial, crematorium or mortuary including transportation of the deceased.
- Sale of land and sale of building where the entire consideration has been received after the completion certificate is issued or after its first occupation.
- Actionable claims other than specified actionable claims.

### The Role of Consideration

Consideration has specifically been defined in the CGST Act, 2017. It can be in money or in kind. It is immaterial whether the payment is made by the recipient or by any other person.

- **Subsidies and Deposits:** Any subsidy given by the Central Government or a State Government is not considered as consideration. A deposit given in respect of the supply of goods or services or both shall not be considered as payment made for such supply unless the supplier applies such deposit as consideration for the said supply.
- **Barter Transactions:** Further, when there is barter of goods or services, the same activity constitutes supply as well as a consideration. When a barber cuts hair in exchange for a painting, hair cut is a supply of services by the barber. It is a consideration for the painting received.

### Deemed Supply (Schedule I)

However, there are exceptions to the requirement of ‘Consideration’ as a pre-condition for a supply to be called a supply as per GST. As per schedule to the CGST Act, 2017, activities as mentioned below shall be treated as supply even if made without consideration:

- Permanent transfer or disposal of business assets where input tax credit has been availed on such assets.

- Supply of goods or services or both between related persons or between distinct persons as specified in section 25, when made in the course or furtherance of business. However, gifts not exceeding ₹ 50,000 in value in a financial year by an employer to an employee shall not be treated as supply of goods or services or both.
- Supply of goods— (a) by a principal to his agent where the agent undertakes to supply such goods on behalf of the principal; or (b) by an agent to his principal where the agent undertakes to receive such goods on behalf of the principal.
- Import of services by a taxable person from a related person or from any of his other establishments outside India, in the course or furtherance of business.

### Course or Furtherance of Business

GST is essentially a tax only on commercial transactions. Hence, only those supplies that are in the course or furtherance of business qualify as supply under GST. Any supplies made by an individual in his personal capacity do not come under the ambit of GST unless they fall within the definition of business as defined in the Act. Sale of goods or service even as a vocation is a supply under GST. However, there is one exception to this 'Course or Furtherance of Business' rule i.e., import of services for a consideration.

### Supply by a Taxable Person

A supply to attract GST should be made by a taxable person. Hence, a supply between two non-taxable persons does not constitute supply under GST. A "taxable person" is a person who is registered or liable to be registered under section 22 or section 24. Hence, even

an unregistered person who is liable to be registered is a taxable person. Similarly, a person not liable to be registered but has taken voluntary registration and got himself registered is also a taxable person.

It should be noted that GST in India is State-centric. Hence, a person making supplies from different States needs to take separate registration in each State. A person who has obtained or is required to obtain more than one registration, in respect of each such registration, shall be treated as distinct persons for the purposes of GST. Hence, a supply between these entities constitutes supply under GST.

### Taxable Supply and Taxable Territory

- **Taxable Supply:** For a supply to attract GST, the supply must be taxable. Taxable supply has been broadly defined and means any supply of goods or services or both which, is leviable to tax under the Act. Exemptions may be provided to the specified goods or services or to a specified category of persons/entities making supply.
- **Taxable Territory:** For a supply to attract GST, the place of supply should be in India. The place of supply of any goods or services is determined based on Sections 10, 11, 12 and 13 of the IGST Act 2017.

### Conclusion

In summary, supply under GST encompasses a wide range of transactions, and its correct interpretation is crucial for businesses to comply with GST regulations and ensure smooth operations. Understanding the concept of supply is crucial for businesses to ensure compliance with GST regulations and proper tax planning.

## Topic

Module 1:  
Introduction to  
Performance  
Management

Module 5:  
Fundamentals of  
Business Valuation

## ELECTIVES

### Paper-20A

Strategic  
Performance  
Management and  
Business  
Valuation (SPMBV)

## Performance Management

### Introduction to Performance Management:

Performance management is a continuous process of identifying, measuring and developing the performance of individuals and teams and aligning their performances with the strategic goals of an organization.

Let's consider the definition's *two main components*: -

1. **Continuous process.** Performance management is ongoing. It involves a process of setting goals and objectives, observing performance, and providing guidance & direction and receiving feedback.
2. **Alignment with strategic goals.** Performance management requires that managers ensure that employees' activities and outputs are congruent with the organization's goals and, consequently, help the organization gain a competitive advantage.

Performance management therefore creates *a direct link* between employee performance and organizational goals and makes the employees' contribution to the organization explicit.

However, we must distinguish between *performance management and performance appraisal*. A system that involves employee evaluations once a year without an ongoing effort to provide feedback and coaching so that performance can be improved is not a true performance management system. Instead, this is only a performance appraisal system. Performance appraisal is the systematic description of an employee's strengths and weaknesses. *Thus, performance appraisal is an important component of performance management whilst performance management is much wider in scope.*

Following *essential elements* of Performance management, thus, crystal out and may be summarized as:

- *setting clear and measurable goals,*
- *implementing meaningful actions, and*
- *imposing rigorous consequences & expectations.*

A performance management system should *help change people's mind-set*, and the organization should also become truly performance oriented. Every manager should understand *that performance as per pre-set standards* is a critical aspect of working and this guiding philosophy is to be communicated in many ways throughout the organization. Performance management systems that do not make explicit the employee contribution to the organizational goals are not true performance management systems. Making an explicit link between employees' performance objectives and the organizational goals also serves the purpose of establishing a *shared understanding* about what is to be achieved and how it is to be achieved.

In essence, well-designed and well-implemented performance management systems make substantial contributions to the organization.

*Some real-life instances by research & observations may be narrated-*

A recent survey of almost 1,000 HR management professionals in Australia revealed that 96% of Australian companies currently implement some type of performance management system. Similarly, results of a survey of 278 organizations, about two-thirds of which are multinational corporations, from 15 different countries, indicated that about 91% of organizations implement a formal performance management system. Moreover, organizations with formal and systematic performance management systems are 51% more likely to perform better than the other organizations regarding financial outcomes, and 41% more likely to perform better in the areas of customer satisfaction, employee retention and other related metrics. Based on these results, it is not surprising that senior executives of companies listed in the Sunday Times list of best employers in the United Kingdom believe that *performance management is one of the top two most important HR management priorities* in their organizations.

### Performance Management Contributions

Following are the major contributions-

1. **Motivation to perform is increased.** Receiving feedback about one's performance increases the motivation for future performance. Knowledge about how one is doing and recognition about one's past successes provide the fuel for future accomplishments. This improves team performance and group synergy.
2. **Self-esteem is enhanced.** Receiving feedback about one's performance fulfils a basic human need to be recognized and valued at work. This, in turn, is likely to increase employees' self-esteem and their attachment to the organization.
3. **Managers gain insight about subordinates.** Direct supervisors and other managers gain new insights about the person being appraised. Gaining new insights into a person's performance and personality will help the manager build a better relationship with that person. Also, supervisors gain a better understanding of each individual's contribution to the organization.
4. **The understandings of a job criteria are better clarified.** The job of the person being appraised may be clarified and defined more clearly so that employees gain a better understanding of their

performance and results expected of a specific position. Employees also gain a better insight of what it takes to be a successful performer (i.e., what are the specific criteria that define a job success).

5. **Administrative actions can be fairer and more appropriate.** Performance management systems provide valid information about performance that can be used for administrative actions such as merit rating, promotions, and transfers as well as terminations. Thus, a performance management system helps ensure that rewards are distributed on a fair and credible basis as such decisions are based on a sound performance management system that further lead to improved interpersonal relationships and enhanced supervisor-subordinate understandings.
6. **Organizational goals are made clear.** Since a good performance management system helps to focus on clarity of organizational goals, the employees understand what they can do about the organizational success. This ensures organizational goals cascade down to individual employees. This further help improve employees' acceptance of the organizational wider goals when an organization expands & diversifies.
7. **Employees become more competent over time.** An obvious contribution is that employee performance is improved. In addition, there is a solid foundation for helping employees become more successful by establishing suitable training & mentoring plans for employees.
8. **Employee misconduct is minimized.** Employee misconduct is an increasingly pervasive phenomenon that has received widespread media coverage. Such misconduct includes accounting irregularities, churning customer accounts, abusing overtime policies, giving inappropriate gifts to clients / potential clients and using company resources for personal use. Although some individuals are more likely to engage in misconduct compared to others based on individual differences in personality and other attributes, having a good performance management system in place provides an early check on these issues.
9. **There is better and more timely differentiation between good and poor performers.** Performance management systems allow for a quicker identification of good and poor performers. Also, it helps supervisors to address performance problems on a timely basis to initiate possible correctional steps.
10. **Supervisors' views of performance are communicated more clearly.** Performance

management systems allow managers to clearly communicate their opinions to the subordinates regarding their performance. Thus, there is greater transparency as to how managers discuss performance expectations and provide necessary feedback.

11. **Organizational change is facilitated.** Performance management systems can be a useful tool to drive organizational change. For example, when an organization decides to change its culture to give top priority to product quality and customer service. This is precisely what IBM did in the 1980s when it wanted to switch focus to customer satisfaction and brought significant changes in the employee mindset,
12. **There is better protection from lawsuits.** Data collected through proper performance management systems help various legal compliance with applicable Rules & Regulations; thus, legal accountability is enhanced.
13. **Employee engagement is enhanced.** A good performance management system leads to enhanced employee engagement. Employees who are engaged feel involved, committed, passionate, and empowered. Employee engagement is an important predictor of organizational performance and this is an important contribution of a good performance management system.
14. **Significant improvement in Functional & Group productivity, efficiency and effectiveness is achieved.** Another important contribution of a good performance management system is to *enhance productivity, efficiency and effectiveness of a team / group vis a vis the functions / processes / activities that are linked to their responsibilities*. The sum total of the efficiency and effectiveness of the group and the team across an organization significantly brings the overall efficiency and functional effectiveness in an organisation *by removing functional bottlenecks, duplication and deficiencies*.

#### **Disadvantages / Dangers of Poorly Implemented Performance Management Systems**

Following instances may be stated: -

1. **Increased employee turnover.** If the process is not seen as fair, employees may become upset and leave the organization. They can leave physically (i.e., quit) or withdraw psychologically (i.e., minimize their effort until they are able to find a job elsewhere).
2. **Use of misleading information.** If a standardized system is not in place, there are multiple opportunities for fabricating information about an employee's performance.
3. **Lowered self-esteem.** Self-esteem may be lowered

if feedback is provided in an inappropriate and inaccurate way. This, in turn, can create employee resentment and destroy team work and group synergies.

4. **Wasted time and money.** Performance management systems cost money and time. These resources are wasted when systems are poorly designed and implemented.
5. **Damaged relationships.** As a consequence of a deficient system, the relationship among the individuals involved may be damaged, often permanently.
6. **Decreased motivation to perform.** Motivation may be lowered for many reasons, including the feeling that superior performance is not translated into meaningful & tangible (e.g., pay increase) or intangible (e.g., personal recognition) rewards.
7. **Employee burnout and job dissatisfaction.** When the performance assessment instrument is not seen as valid and the system is not perceived as fair, employees are likely to feel increased levels of job burnout and job dissatisfaction. As a consequence, employees are likely to become increasingly irritated destroying discipline and organisational culture.
8. **Increased risk of litigation.** Expensive lawsuits may be filed by individuals who feel they have been appraised unfairly.
9. **Varying and unfair standards and ratings.** Both standards and individual ratings may vary across the various units of an organization and be unfair.
10. **Unclear ratings system.** Poor communication is an inevitable outcome of a poorly designed performance system and employees may not know how their ratings are generated and how the ratings are translated into rewards or reprisals.

## FUNDEMENTALS OF BUSINESS VALUATION

### Purpose

Valuation is an essential prerequisite in choosing investments for a portfolio, in deciding on the appropriate price to pay or receive in a takeover, and in making investment, financing and dividend choices while running a business. Valuation is required throughout the life cycle of a company from the time a company is incorporated and needs infusion of funds to its liquidation.

### Valuation is a critical requirement at various stages of a company.

Some of the common purposes of valuation are:

Issue of shares or other securities by the company (e.g. private investors, employee stock options, rights issue, and sweat equity shares)

- Initial public offering and listing of equity shares in stock exchanges
- Mergers and acquisitions including Leveraged Buyouts (LBO)
- Buyback of shares
- Business restructuring such as slump sale
- Shareholders' disputes settlement
- Purchase / sale of a business interest and takeovers & acquisitions
- Non-arm's length transactions
- Disgruntled minority shareholders' actions
- Damage claims
- Estate planning
- Insolvency proceedings and company liquidation

Some of the regulations that commonly require business valuation to be mandatorily made are :

- The Companies Act, 2013 (including Insolvency and Bankruptcy Code, 2016)
- Securities and Exchange Board of India (SEBI) Regulations
- Foreign Exchange Management Act (FEMA)
- Income Tax Act & Rules, etc., etc.

### Valuation Premise

The valuation approach, inputs and assumptions applied are highly dependent on the selected premise of value. The premise of value is driven by the purpose of the valuation and basis of value used. A premise of value describes the circumstances of how an asset or liability is applied in a given case. Different bases of value may require a particular premise of value or require the consideration of multiple value premises.

### Some common premises of value are:

- (a) **Highest and best use:** Highest and best use (HABU) is the use, that would produce the highest value for an asset. The highest and best use must be physically possible (where applicable), financially feasible, legally allowed and should result in the highest value.
- (b) **Current use/existing use:** Current use/existing use, also known as "as-is-where-is" is the current way an asset, liability, or group of assets and/or liabilities is used. The current use may be, but not necessarily, the highest and best use.

- (c) **Orderly liquidation:** An orderly liquidation describes the value of a group of assets that could be realised in a liquidation sale, given a reasonable period of time to find a purchaser (or purchasers), with the seller being compelled to sell on an as-is-where-is basis. The reasonable period of time to find a purchaser (or purchasers) may vary by asset type and market conditions.
- (d) **Forced sale:** The term “forced sale” is often used in circumstances where a seller is under compulsion to sell and when a proper marketing period is not possible and buyers may not be able to undertake adequate due diligence.
- (e) **Going concern:** Going concern value is the value of a business that is expected to continue to operate in the future. The intangible elements of Going Concern Value result from factors such as having trained work force, an operational plant, the necessary licenses, marketing systems and procedures in place, etc. Usually, businesses are valued using Going Concern premise. In cases where businesses are under stress, they may be valued on Liquidation or Forced Sale premise. Tangible assets are usually valued using any of the premises except for Going concern. Further, the bases and premises of value do not consider the transaction cost to either the buyer or the seller.

### Valuation Approaches

Valuers may apply one or more valuation approaches to valuation to arrive at the value in accordance with the basis of value. The principal valuation approaches are:

- (a) Market Approach
- (b) Income Approach
- (c) Cost Approach

Each of these valuation approaches includes different methods of valuation. It should be remembered that ascertaining the appropriate value is the primary goal of the valuation exercise. A valuer should select the appropriate valuation approach or a set of approaches and methods as there may not be a single approach or method that is best suited for valuation in every situation.

### Market Approach

The market approach provides an indication of value by comparing the assets with identical or comparable (or similar) assets for which price information is available. This approach is also known as Relative Valuation approach.

#### When should Market approach be applied?

The market approach should be applied under the following circumstances: -

- (a) the subject asset has recently been sold in a

transaction appropriate for consideration under the basis of value,

- (b) the subject asset or substantially similar assets are actively publicly traded,
- (c) there are frequent and/or recent observable transactions in substantially similar assets.

In some instances, a valuer may consider using other valuation approaches instead of Market Approach or in combination with Market Approach, such as:

- (a) the business to be valued and its market comparables are not traded in the active market;
- (b) where the business has fewer identical or comparable assets (market comparable);
- (c) sufficient information on the comparable transaction is not available;
- (d) there is no recent transaction either in the business or in the market comparables; or
- (e) there are material differences between the business to be valued and the market comparables, which require significant adjustments.

### Methods of Valuation under Market Approach:

#### (a) Market price method

Market price is the best judge of value. For assets that are frequently traded in an active market, the market prices may be considered as representative of value.

#### (b) Comparable Companies Multiple Method

Comparable Companies Multiple Method involves valuation of an asset based on valuation multiples of comparable assets that are traded in active market.

#### (c) Comparable Transactions Method

Comparable Transactions Method, also known as ‘Guideline Transaction Method’, involves valuing an asset based on transaction multiples derived from prices paid in transactions of asset to be valued / market comparables (comparable transactions).

Usually, companies in specialised business where there may not be exchange-traded comparables, but comparable assets are having transactions in over-the-counter (private transactions), the valuation multiples may be taken from such transactions. It is important to consider recent and orderly transactions to avoid significant biases in valuation.

### Income Approach

Income approach provides an indication of value by converting future cash flow to a single current value. Under this approach, the value of an asset is determined by reference to the value of income, cash flow or cost savings generated by the asset.

### When to apply Income approach?

The income approach should be applied under the following circumstances:

- (1) where the asset does not have any market comparable or comparable transaction;
- (2) where the asset has fewer relevant market comparables, or
- (3) where the asset is an income producing asset for which the future cash flows are available and can reasonably be projected.

Income approach should be used when the income producing ability of the asset is the critical element affecting value from participant's perspective.

Also, a valuer considers Income approach along with other approaches, when:

- the timing and amount of future income is uncertain
- there is lack of access to information
- the asset has not yet begun generating income but is projected to do so

### Methods of Valuation under Income Approach:

#### (a) Discounted Cash Flow Method (DCF)

The Discounted Cash Flow (DCF) Method is arguably the most preferred method of valuation among all stakeholders. Fundamentally, the DCF method attempts to prove that the value of an asset is the present value of its future cash flows. Accordingly, this method involves discounting of future cash flows expected to be generated by an asset over its life using an appropriate discount rate to arrive at the present value.

DCF method applies the concept of Net Present Value (NPV). It requires three key inputs viz, Cash Flows, Discount Rate and Terminal Value, and each of these inputs are very critical in the valuation process.

#### Cash Flows

Free cash flow is the actual cash that would be available to the company's investors after making all investments necessary to maintain the company as an ongoing enterprise. These are internally generated funds that can be distributed to the company's investors (e.g., shareholders and bondholders) without impairing the value of the company. The cash flow can be pre-tax or post-tax.

Free Cash Flows generally represent the after-tax cash generated by the business, available for all the investors (stockholders and banks), excluding any impact of the financial structure. In case of Discounted Cash Flow based valuation, we assess the Free Cash Flow for an explicit forecast period (usually 5 years and in some cases, up to 10 years).

### Discount Rate (Cost of Capital)

The Free Cash flows should be discounted to its present value using a Discount Rate that is usually the Cost of Capital. Cost of Capital represents the cost of funds used for financing the business. It is the rate of return that the suppliers of capital, bondholders and owners require as compensation for their contributions to capital.

If business is financed solely through Equity, cost of capital is the same as Cost of Equity

If business is financed solely through Debt, cost of capital is the same as Cost of Debt

Usually, companies use a mix of Debt and Equity while financing their business, thus, the overall cost of capital is derived from a weighted average of cost of all capital sources, known as the Weighted Average Cost of Capital (WACC). Cost of capital represents a minimum benchmark rate that a company must overcome before it can generate value for its financiers.

### Terminal Value

Terminal value is the value of an asset, business, or project beyond the explicit forecast period when future cash flows can be estimated. Terminal value may assume that a business will grow at a set growth rate forever after the forecast period. In case the business is expected to mature at the end of the explicit forecast period, the terminal value may assume that the Free Cash Flows will continue for an infinite period thereafter. Terminal value often comprises a large percentage of the total assessed value. Terminal Value calculation uses the concept of Perpetuity calculation (with or without a constant growth rate).

### (b) Profit Earning Capitalised Value (PECV) or Capitalisation of Earnings Method

PECV or Capitalisation of Earnings Method is a simplified application of Income Approach. In case where the Free Cash Flows cannot be calculated and the valuer does not have access to future projections, PECV serves as a proxy for DCF method. However, this assumes that Profits are like Free Cash Flows and the company is in a stable stage.

Valuers often use the past years' profits (adjusted for extraordinary or exceptional items) and assign them weights based on current scenario. This weighted profit is assumed to accrue over an infinite period and is then discounted using a suitable capitalisation rate.

### Cost Approach

Cost approach is a valuation approach that reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost). This approach provides an indication of value using the economic principle that a buyer will

pay no more for an asset than the cost to obtain an asset of equal utility.

### When to apply Cost Approach?

- (i) Where income or market approach cannot be used
- (ii) An asset can be quickly recreated with substantially the same utility as the asset to be valued:
- (ii) An asset can be quickly recreated with substantially the same utility as the asset to be valued;
- (iv) When liquidation value is to be determined

Also, Cost Approach can be used along with other approaches when:

- (i) The asset hasn't started generating income.
- (ii) An asset of substantially the same utility as the asset to be valued can be created but there are regulatory or legal hurdles.
- (iii) The asset was recently created.

### Methods of Valuation under Cost Approach:

#### (a) Replacement Cost Method

Replacement cost is relevant to determining the price that a participant would pay as it is based on replicating the utility of the asset, not the exact physical properties of the asset.

#### (b) Reproduction Cost Method

Reproduction cost indicates value by calculating the cost of recreating a replica of an asset.

Reproduction cost is appropriate in circumstances such as:

- (i) The cost of a modern equivalent asset is greater than the cost of recreating a replica of the subject asset, or
- (ii) The utility offered by the subject asset could only be provided by a replica rather than a modern equivalent.

#### (c) Net Asset Value or Book Value method

While not specifically mentioned in the Valuation Standards, Net Asset Value or the Book Value method serves as a common method of valuation of private companies where the detailed information is not available. This method relies on the financial statements (Balance Sheet) and assumes that the values reflected in the Balance Sheet are reflective of true and fair value of the business.

Where the financial statements are prepared using historical cost convention (e.g. Land, Building and investments are recorded at cost but their values may have increased over time), valuers may identify the fair values of these assets and adjust them to arrive at their fair values. Valuers must keep in mind that under Ind

AS (applicable to all listed companies and some large privately held companies), various assets and liabilities are to be recorded at Fair Values.

### Fundamentals of Valuation - Risk & Return

Harry Markowitz, the father of modern finance was first to quantify risk and used the same in portfolio decision making. Based on risk-return criteria, he suggested ways to identify optimal portfolio. Markowitz has made two important assumptions. First, an investor is risk averse. Second, an investor would prefer higher amount of wealth than the lower one. The reason is higher wealth leads to the possibility of higher consumption. Given two possible portfolios with similar risk profile, the one with higher expected return will be preferred. These two assumptions are most integral part of a valuation exercise. The Primary objective of any investor is to maximise return from a given investments, subject to various constraints, primarily the associated risks in a given context.

#### Return

Return may be realised or expected. The rate of return is total return the investor receives during the holding period stated as a percentage of the purchase price of the investment at the beginning of the holding period.

#### Risk

Risk can be defined as the chance that the actual outcome from an investment will differ from the expected outcome. Risk and return go hand in hand considering investments and market dynamics. Risk and returns are directly related to each other.... higher the risk, higher is the expected return.

A commonly accepted measure of risk is volatility and is usually measured in terms of Standard Deviation

Risk can be reasonably diversified in respect of any class of assets by prudent investment strategies, thereby, increasing the value of the assets or group of assets. Hence, in valuation identifying the potential risks and future or probable risks are highly significant and the how prudently such perceived risks are diversified to minimise its impact in a given situation, assumes considerable importance.

#### TYPES OF RISK affecting a business valuation-

- **Interest Rate Risk** - variability in security's return due to adverse changes in the interest rates.
- **Market Risk** - variations in return due to fluctuations in the securities market.
- **Inflation Risk** - risk due to adverse changes in prices of all commodities.
- **Business Risk** - risk associated with the different activities undertaken by the enterprise.

- **Financial Risk** - risk resulting from the existence of debt in the capital structure of the company.
- **Liquidity Risk** - risk associated with the secondary market in which the security is traded

The above risks can be summarized under the following two categories:

- (a) **Systematic Risk** - Systematic risk is the risk that affects the entire market and hence, the firm too. It is also called non-diversifiable risk.
- (b) **Unsystematic Risk** - Unsystematic Risk is the variability in the security's return on account of the firm specific risk factors. It is also called diversifiable or avoidable risk.

In the process of Business Valuation, apart from many business documents, records, information and data the importance of accurate and properly structured Financial Statements (FS) is utmost. Proper analysis & interpretation of the FS by a valuer indeed results into a reasonably acceptable valuation number in most cases.

#### **Market value and Enterprise Value in Business Valuation –**

**Market value (MV)** – It is the estimated value for which

an asset or a liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction after undertaking adequate marketing diligence where the parties have acted prudently and without compulsion. The market value represents transaction between unrelated parties, each acting independently with proper marketing prudence.

**Enterprise value (EV)** – It covers value of all asset claims and ownership interests arising from debt and equity. EV is considered to be the actual cost of purchasing a company before a takeover is considered. In fact, it is the minimum value that an entity would pay to acquire a company. However, in M & A, the acquirer generally pays the enterprise value but would have access to cash of the target company, thus, we often subtract cash and cash equivalents in the calculation of EV.

Thus:

$EV = (\text{Common shares} + \text{Preferred shares} + \text{Minority interest}) + \text{Market value of Debts} - \text{Cash}$

EV enables business entities to find the worth (economic value) of a target company or a business entity.

The above narrative covers the entire spectrum of Business Valuation from its fundamental perspective.

## 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

Banks occupy a central position in every modern economy. They mobilize savings, provide credit to individuals and businesses, facilitate payments, support trade, and promote economic growth. Because of this pivotal role, the stability and sound functioning of banks are extremely important. However, banking activities inherently involve uncertainty and exposure to various kinds of risks. Lending may not always be repaid, investments may lose value, systems may fail, and economic conditions may change unexpectedly. Consequently, managing risk has become one of the most fundamental responsibilities of banking institutions.

Risk management in banking refers to the structured process through which banks identify, assess, monitor, and control risks that may threaten their financial health, operational efficiency, and reputation. It is a continuous and systematic function embedded in strategic planning, daily operations, and regulatory compliance. Over time, risk management has evolved from a basic control mechanism into a comprehensive management discipline that supports informed decision-making and sustainable growth.

International banking standards developed by the “Basel Committee on Banking Supervision” emphasize that effective risk management is essential for the stability of both individual banks and the financial system as a whole. These standards guide banks in establishing sound governance, adequate capital, and robust risk monitoring mechanisms.

**a) Concept of Risk in Banking:** In the banking sector, risk can be defined as the possibility of financial loss or adverse outcomes resulting from uncertain events. Since banks deal with money, investments, credit, and financial markets, uncertainty is present in almost every activity they undertake. For example, when a bank lends money to a borrower, there is always a possibility that the borrower may default. Similarly, fluctuations in interest rates or exchange rates can affect the value of financial assets.

Risk does not necessarily imply negative outcomes alone. It is closely related to the concept of return. In finance, higher returns are generally associated with higher levels of risk. Therefore, banks must carefully balance risk and reward while making business decisions. Excessive risk-taking may lead to financial distress, while excessive caution may reduce profitability and competitiveness.

Risk management helps banks maintain this balance. It provides a structured framework for understanding the nature of risks, estimating their potential impact, and implementing measures to reduce or control them. Through effective risk management, banks can pursue profitable opportunities while maintaining financial stability.

**b) Objectives of Risk Management in Banks:** The primary objective of risk management in banking is to safeguard the financial strength and sustainability of the institution. However, several specific goals are associated with this broader objective.

One important objective is the protection of depositors’ funds. Depositors place their trust in banks by entrusting them with their savings. Risk management ensures that these funds are protected through prudent lending, investment decisions, and internal controls.

Another key objective is maintaining financial stability. Banks operate in an interconnected financial system, and problems in one institution can spread quickly to others. Effective risk management reduces the likelihood of bank failures and contributes to the stability of the entire financial sector.

Risk management also supports profitability and efficient use of capital. By identifying and measuring risks accurately, banks can allocate resources to activities that offer the best risk-adjusted returns. This improves long-term performance and competitiveness.

Regulatory compliance is another important objective. Banks must adhere to various guidelines issued by central banks and supervisory authorities. In India, the Reserve Bank of India plays a crucial role in establishing prudential norms and ensuring that banks follow sound risk management practices.

Finally, risk management strengthens public confidence in the banking system. When customers and investors trust that banks are well managed and financially secure, the overall financial system becomes more stable.

**c) Importance of Risk Management in Modern Banking:** The importance of risk management in banking has increased significantly in recent decades. Several developments in the financial sector have made banking activities more complex and risk-prone.

One major factor is financial globalization. Banks today operate across national borders and participate in international markets. Economic disturbances in one country can quickly affect banks elsewhere. Effective risk management helps institutions cope with such global interconnections.

Technological advancements have also transformed banking operations. Digital banking, mobile payments, and online financial services have improved efficiency and convenience. However, they have also introduced new vulnerabilities such as cyber threats, system failures, and data breaches. Banks must therefore adopt advanced risk monitoring systems to manage technological risks.

All these developments highlight the growing importance of a comprehensive and proactive approach to risk management in banking.

**d) Types of Risks in Banking:** Banks face a wide range of risks arising from both internal operations and external economic conditions. Understanding these risks is the first step in effective risk management.

**Credit Risk** is one of the most significant risks in banking. It arises when borrowers fail to repay loans or meet contractual obligations. Poor credit assessment, economic downturns, or business failures can increase loan defaults, affecting the financial health of banks.

**Market Risk** refers to potential losses resulting from changes in market variables such as interest rates, foreign exchange rates, and equity prices. Banks involved in trading and investment activities are particularly exposed to market fluctuations.

**Operational Risk** results from failures in internal processes, human errors, fraud, or technological breakdowns. With increasing digitization, cybersecurity threats have become a major component of operational risk.

These various risks are interconnected, and effective risk management requires a holistic approach that considers their combined impact.

**e) Risk Management Process in Banks:** The process of risk management in banks typically follows several systematic steps. The first step is risk identification. Banks must identify potential risks associated with their activities, products, and business environment. This involves analysing internal operations as well as external economic conditions.

The **second step** is risk measurement or assessment. Once risks are identified, banks evaluate their likelihood and potential impact. Quantitative models, statistical tools, and scenario analysis are often used to estimate possible losses.

The **third step** is risk monitoring. Continuous monitoring ensures that risk exposures remain within acceptable limits set by the bank's management and regulatory authorities. Monitoring systems provide early warning signals when risk levels increase.

The **fourth step** is risk control and mitigation. Banks adopt various strategies to reduce or manage risks. These may include diversification of loan portfolios, collateral requirements, hedging through financial instruments, internal controls, and insurance.

The **final step** is risk reporting and review. Regular reports are submitted to senior management and regulatory

authorities to ensure transparency and accountability. Internal audits and supervisory reviews help evaluate the effectiveness of risk management systems.

**f) Role of Technology in Risk Management:** Technology has become an essential component of modern risk management in banking. Advanced software systems allow banks to collect and analyse large volumes of financial data in real time. These systems help identify trends, detect irregularities, and forecast potential risks.

Data analytics, artificial intelligence, and machine learning are increasingly used to improve credit assessment, fraud detection, and predictive risk modelling. Automated monitoring tools also enhance the efficiency and accuracy of risk reporting.

At the same time, technology itself introduces new risks such as cyberattacks, system outages, and data privacy concerns. Banks must therefore invest in strong cybersecurity measures and resilient digital infrastructure.

**g) Emerging Trends in Banking Risk:** The landscape of banking risks continues to evolve. Climate change, geopolitical tensions, digital currencies, and fintech innovations are creating new uncertainties for financial institutions. Banks are increasingly incorporating environmental, social, and governance (ESG) considerations into their risk frameworks.

Cybersecurity has become a top priority as digital banking expands rapidly. Financial institutions must continuously upgrade their systems to protect sensitive data and maintain customer trust.

Another emerging trend is integrated or enterprise-wide risk management, which considers all types of risks collectively rather than in isolation. This approach provides a comprehensive understanding of the bank's overall risk exposure.

### To Sum Up

Risk management is an indispensable component of modern banking. Given the complexity and uncertainty inherent in financial activities, banks must adopt systematic approaches to identify, measure, and control risks. Effective risk management protects depositors, ensures regulatory compliance, enhances profitability, and strengthens public confidence in the banking system.

As financial markets continue to evolve, banks must continuously refine their risk management frameworks, adopt advanced technologies, and foster a strong risk culture. Institutions that successfully manage risks will not only safeguard their stability but also contribute to the resilience and growth of the broader economy.

## Risk Management in Insurance: Introduction to Insurance Business

Insurance is one of the most important pillars of modern financial systems. It provides financial protection against unexpected events such as accidents, natural disasters, illness, death, or property loss. Individuals, businesses, and governments rely on insurance to reduce financial uncertainty and recover from unforeseen risks. Because the core function of insurance is to deal with uncertainty, risk management lies at the heart of the insurance business.

Risk management in insurance refers to the systematic process through which insurance companies identify, evaluate, control, and finance risks associated with their operations and the policies they underwrite. Unlike banks, which mainly manage credit and financial risks, insurance companies specialize in assuming and spreading risk across a large pool of policyholders. By collecting premiums from many individuals and compensating only those who experience losses, insurers make risk manageable and predictable.

**a) Concept and Nature of Insurance:** Insurance is essentially a financial arrangement through which the risk of potential loss is transferred from an individual or business to an insurance company in exchange for a premium. The insurer agrees to compensate the insured if a specified event occurs within the policy period.

The concept of insurance is based on several fundamental principles. One of the most important is the **principle of risk pooling**, where many individuals exposed to similar risks contribute premiums into a common fund. Losses suffered by a few are then paid from this fund. Another key concept is the **law of large numbers**, which allows insurers to estimate expected losses with reasonable accuracy when a large number of similar exposure units are involved.

Insurance also operates on the principle of **utmost good faith**, meaning both the insurer and the insured must disclose all relevant information honestly. Other principles include insurable interest, indemnity, contribution, and subrogation, which together form the legal and operational foundation of insurance contracts.

Through these principles, insurance provides financial security and helps individuals and organizations plan for the future with greater confidence.

**b) Meaning of Risk in Insurance:** Risk in the insurance context refers to the uncertainty regarding the occurrence of a loss. It may arise from natural events, human activities, economic conditions, or technological failures. Insurance companies exist to assume these risks in exchange for premiums and manage them in a way that ensures profitability and long-term sustainability.

However, insurers themselves face numerous risks. If losses are higher than expected, or if investments perform poorly, an insurance company may experience financial

distress. Therefore, insurers must adopt effective risk management practices to maintain stability.

Risk management in insurance involves identifying potential exposures, analysing the probability and severity of losses, designing appropriate insurance products, setting premiums, and maintaining sufficient reserves to meet claims. It is a continuous process that combines actuarial science, financial analysis, and regulatory compliance.

**c) Objectives of Risk Management in Insurance:** Risk management in the insurance business serves multiple objectives that are essential for both insurers and policyholders.

One major objective is **financial stability**. Insurance companies must ensure that they have enough funds to meet claims even during catastrophic events. Effective risk management helps maintain solvency and operational continuity.

Another objective is **policyholder protection**. Customers rely on insurers to provide compensation when losses occur. Sound risk management practices ensure that claims can be paid promptly and fairly.

**Profitability and sustainability** are also important goals. Insurance companies must balance premium income with expected claims, administrative costs, and investment returns.

Risk management also helps insurers **comply with regulatory requirements**. Regulators impose strict guidelines regarding capital adequacy, reserve levels, and risk exposure.

**d) Importance of Risk Management in Insurance:** Risk management plays a crucial role in ensuring the smooth functioning of the insurance industry. Since insurers assume risks from thousands or even millions of policyholders, poor risk management can lead to severe financial consequences.

One reason risk management is important is the unpredictable nature of losses. Natural disasters, pandemics, and large-scale accidents can result in massive claims. Without proper risk assessment and reinsurance arrangements, insurance companies may struggle to meet these obligations.

Another factor is the increasing complexity of modern risks. Cybercrime, climate change, global supply chain disruptions, and technological failures are creating new forms of exposure. Insurers must constantly update their risk models and underwriting practices.

**e) Types of Risks Faced by Insurance Companies:** Insurance companies face a variety of risks that can affect their financial health and operational efficiency.

**Underwriting Risk** is one of the most significant risks. It arises when insurers incorrectly assess the likelihood or

cost of claims. If premiums are too low relative to claims, the insurer may incur losses.

**Market Risk** occurs due to fluctuations in interest rates, stock markets, or other financial variables that affect the value of insurers' investment portfolios. Since insurance companies invest large sums of money, market volatility can significantly impact profitability.

**Credit Risk** arises when reinsurers, brokers, or other counterparties fail to meet their financial obligations.

**Operational Risk** results from failures in internal systems, processes, or human actions. Fraud, technological failures, and administrative errors fall into this category.

**Liquidity Risk** occurs when an insurer does not have enough liquid assets to meet claim payments or operational expenses.

**Catastrophic Risk** refers to the possibility of extremely large losses caused by events such as earthquakes, hurricanes, floods, or pandemics.

**f) Risk Management Process in Insurance:** The risk management process in insurance follows a structured approach designed to identify, analyse, and control risk exposures.

The first step is **risk identification**. Insurers examine the various types of risks they face, including those arising from policyholders, investments, operations, and external environments.

The second step is **risk evaluation and measurement**. Actuarial analysis, statistical models, and historical data are used to estimate the probability and severity of losses.

The third step is **risk control**. Insurance companies adopt several strategies to manage risk, such as underwriting guidelines, diversification of policy portfolios, and safety incentives for policyholders.

The fourth step is **risk financing**, which involves arranging financial resources to cover potential losses. This includes maintaining reserves, purchasing reinsurance, and allocating capital effectively.

The final step is **risk monitoring and review**. Continuous monitoring ensures that risk levels remain within acceptable limits and that corrective actions are taken when necessary.

**g) Role of Underwriting in Risk Management:** Underwriting is one of the most critical functions in the insurance business. It involves evaluating the risk associated with insuring a particular individual, asset, or activity. Underwriters analyse various factors such as age, health condition, occupation, financial status, location, and historical data to determine the level of risk.

Based on this assessment, the insurer decides whether to accept the risk, modify the coverage, impose conditions, or reject the proposal. Proper underwriting ensures that premiums reflect the level of risk and that the insurer's portfolio remains balanced.

#### **h) Role of Reinsurance in Risk Management:**

Reinsurance is another important tool used by insurance companies to manage risk. Through reinsurance, insurers transfer a portion of their risk to other insurance companies known as reinsurers. This arrangement helps spread large risks and protects insurers from catastrophic losses.

Reinsurance allows insurance companies to underwrite larger policies, stabilize their financial performance, and maintain solvency during major claim events. It also promotes global risk sharing across international markets.

#### **i) Regulatory Framework of Insurance Risk Management:**

Insurance is a highly regulated industry because it involves safeguarding public funds and maintaining financial stability. Regulatory authorities establish guidelines to ensure that insurers manage risks responsibly.

In India, the Insurance Regulatory and Development Authority of India supervises insurance companies, monitors solvency margins, approves products, and ensures that policyholders' interests are protected.

#### **j) Emerging Trends in Insurance Risk Management:**

The insurance industry is undergoing rapid transformation due to technological, environmental, and economic changes.

Digital technologies such as artificial intelligence, big data, and predictive analytics are improving risk assessment and fraud detection. Insurers can now analyse large datasets to understand customer behaviour and anticipate potential losses.

Climate change has emerged as a significant risk factor. Increasing frequency of floods, storms, and wildfires is affecting insurance claims worldwide. Insurers are incorporating environmental risk models into their decision-making.

Cyber insurance is also becoming an important area as businesses seek protection against data breaches and cyberattacks.

#### **To Sum Up:**

Risk management forms the backbone of the insurance business. The primary purpose of insurance is to provide financial protection against uncertainty, and achieving this goal requires careful assessment, control, and distribution of risk. Through underwriting, diversification, reinsurance, and prudent financial management, insurers are able to fulfil their obligations to policyholders while maintaining profitability and stability.

A well-developed risk management framework not only safeguards insurance companies but also contributes to economic resilience and social security. By effectively managing risk, the insurance industry continues to play a vital role in supporting individuals, businesses, and societies in the face of uncertainty.

## Topic

Module 1:  
Entrepreneurial Skill  
Sets

## ELECTIVES

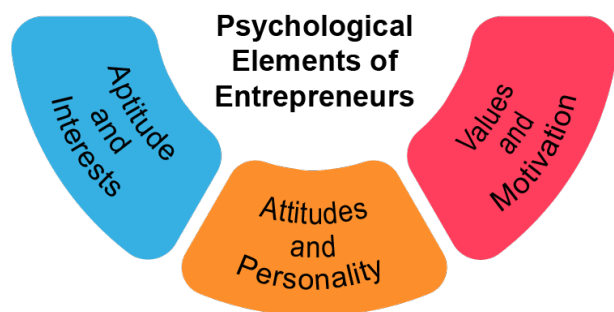
Paper-20C

Entrepreneurship  
and Start Up (ENTS)

## Entrepreneurial Psychology

### Entrepreneurial Psychology

The psychology of entrepreneurship relates to understanding the relationship between successful business leadership and the mental techniques and characteristics that thriving entrepreneurs possess. Psychological theories of entrepreneurship put emphasis on the emotional and mental aspects of the individuals that drive their entrepreneurial activities.



Source: <https://myoer.oum.edu.my/2022/02/08/the-psychological-elements-of-entrepreneurs-2/>

### Aspects of Entrepreneurial Psychology

- 1. Need for Achievement:** Driven by internal satisfaction to set and reach challenging goals.
- 2. Internal Locus of Control:** Believing they directly influence success/failure, rather than external factors.
- 3. High Tolerance for Ambiguity:** Ability to function effectively in uncertain, rapidly changing environments.
- 4. Resilience (Grit):** Capacity to persevere despite setbacks, failure, or slow progress.
- 5. Passion & Vision:** Deep enthusiasm for their venture that inspires others

### Psychological Drivers of Success

- 1. Entrepreneurial Passion:** Positively impacts work engagement and, indirectly, business performance.
- 2. Internal Locus of Control:** The belief that they can influence events (rather than relying on luck) distinguishes founders from managers.
- 3. Tolerance of Ambiguity:** High ability to function without clear rules.
- 4. Goal Setting & Persistence:** Combining «hope» with the perseverance to find alternative paths.

### Relationship between Entrepreneurial psychology and Performance

Entrepreneurial psychology profoundly influences business performance, with high psychological capital

(resilience, optimism, hope, and self-efficacy) directly boosting venture success. Key traits like passion, need for achievement, internal locus of control, and risk-tolerance drive innovation, persistence, and strategic decision-making, which in turn improve financial performance and adaptability.

### Aspects of Entrepreneurial Psychology & Performance

- 1. Psychological Capital (PsyCap):** Entrepreneurs with high PsyCap (confidence, optimism, hope, and resilience) are better at coping with challenges, managing resources, and driving business success.
- 2. Entrepreneurial Passion:** Harmonious or compulsive passion fuels persistence, stimulates creativity, and enhances performance by triggering positive emotions and motivation.
- 3. Core Traits:** Successful entrepreneurs often exhibit a strong need for achievement, an internal locus of control (belief in influencing outcomes), risk-taking propensity, and tolerance of ambiguity.
- 4. Well-being and Performance:** Mental health and work-life balance are critical; positive mental health provides the emotional resources necessary to enhance business performance.
- 5. Cognitive Adaptability:** The ability to pivot, innovate, and recognize new opportunities is essential for maintaining a competitive edge.

### Impact on Business Outcomes

- 1. Enhanced Decision-Making:** Strong psychology leads to better, more confident decisions in high-stress, uncertain environments.
- 2. Increased Persistence:** High-grit entrepreneurs stay committed, navigating through failures and setbacks, which leads to long-term survival.
- 3. Resource Management:** Positive psychological traits enable better allocation of resources to cope with entrepreneurial challenges

### Examples:

1. Elon Musk's, as well as Steve Jobs' (Apple) and Oprah Winfrey's (OWN Network), successes are rooted in extreme passion, vision, and the ability to navigate high uncertainty.
2. Entrepreneurs at Batik Boutique and Komuniti Tukang Jahit (KTJ) in Malaysia focused on solving poverty, using their passion to empower marginalized communities, which in turn created a sustainable business model.
3. Bill Gate's internal locus of control and belief in the

future of personal computing led him to drop out of Harvard and build a global software leader despite widespread skepticism.

4. **Ritesh Agarwal (OYO)** exemplifies high risk-taking and the ability to pivot, starting young to scale a technology-enabled hospitality network.
5. **Bhavish Aggarwal (Ola)** demonstrates high proactiveness and, and, ambition in the mobility sector, challenging traditional transportation models.

### Entrepreneurial Discipline

Self-discipline is a practice, a habit, a skill, a philosophy, and a way of life. Those who are disciplined make their lives easier as their skill sets increase. Self-discipline for entrepreneurs is a unique brand of perseverance, wrapped in tenacity, and driven by a relentless pursuit of their vision. Self-discipline for entrepreneurs is a unique brand of perseverance, wrapped in tenacity, and driven by a relentless pursuit of their vision.

It's not just about scheduling and following a to-do list, it's about the grit to stay on course when doubts creep in, setbacks occur, or the road to success becomes steep and winding. An entrepreneur can become their best self, focus on their goals, remove temptations, and consistently make choices that align with their business objectives.

#### 1. Discipline of Goal Setting

A successful entrepreneur must have a clear vision. This involves setting SMART (Specific, Measurable, Achievable, Relevant, and Time-bound) goals. By practicing the habit of writing down daily, monthly, and yearly objectives, an entrepreneur stays focused on the «big picture» without getting lost in trivial details.

#### 2. Discipline of Time Management

Time is an entrepreneur's most valuable resource. This discipline involves prioritizing tasks—often using tools like the **Eisenhower Matrix**—to focus on high-impact activities rather than just staying “busy.” It requires the habit of starting the day with a planned schedule and sticking to it.

#### 3. Discipline of Financial Prudence

Managing cash flow is the lifeblood of any venture. This involves the practice of **rigorous budgeting**, monitoring expenses, and ensuring that capital is reinvested wisely. Successful entrepreneurs avoid personal extravagances at the cost of business growth.

#### 4. Discipline of Continuous Learning

The market is constantly evolving. A disciplined entrepreneur views learning as a **philosophy**, constantly upgrading their skill sets through reading,

attending workshops, and seeking mentorship. This keeps the business competitive and innovative.

#### 5. Discipline of Persistence (Resilience)

Entrepreneurship is filled with setbacks. The discipline here lies in the habit of getting back up after a failure. It's the mental toughness to view «no» as a «not yet» and to keep refining the business model until it works.

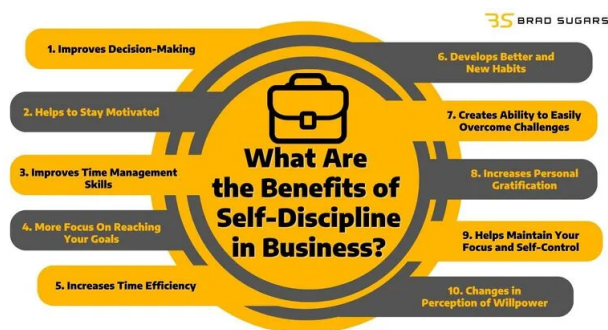
#### 6. Discipline of Health and Vitality

As the quote suggests, self-discipline is a “way of life.” To lead a company, an entrepreneur must maintain their physical and mental health. Regular exercise, proper sleep, and stress management are essential habits that provide the energy required to sustain a high-performance career.

#### 7. Discipline of Networking and Relationship Building

Success is rarely achieved alone. This discipline involves the consistent practice of building and nurturing **professional relationships**. It requires the skill of active listening and the integrity to follow through on promises, which builds trust with partners, employees, and customers.

### Benefits of self-discipline in business



Source: <https://bradsugars.com/self-discipline/>

### Entrepreneurial Self-discipline with Practice

In the actual daily practice of being an entrepreneur, discipline acts as the “operating system” that runs the business. Without it, even the most brilliant idea remains just a dream. discipline makes life easier as “skill sets increase.” Here is how discipline specifically functions in the day-to-day practice of an entrepreneur.

#### 1. It Converts Strategy into Execution

Most entrepreneurs fail not because of a bad plan, but because of poor execution. Discipline is what moves a project from a whiteboard to the market.

- **In Practice:** While others are waiting for «inspiration,» a disciplined entrepreneur follows a **Standard Operating Procedure (SOP)**. They

show up and execute the 24 steps of the MIT framework methodically, ensuring no critical stage (like market validation) is skipped due to laziness or excitement.

## 2. It Protects Your “Core” (The Power of No)

In the MIT framework, Step 10 is defining your **Core**—your unique advantage. Discipline is the practice of saying “no” to everything else.

- **In Practice:** Discipline provides the mental filter to reject opportunities that don’t align with your core mission, preventing «mission creep» that drains resources.

## 3. It Regulates “Emotional Volatility”

The practice of entrepreneurship is a roller coaster of extreme highs and lows.

- **In Practice:** Discipline provides a steady baseline. It separates your professional actions from your temporary emotions.

## 4. It Builds “Compound Trust” with Stakeholders

Investors, employees, and customers don’t just buy your product; they “buy” your reliability.

- **In Practice:** Discipline means you meet your deadlines, pay your vendors on time, and deliver a consistent quality of service. This builds a reputation for reliability, which eventually becomes a competitive advantage that “makes your life easier” because people *want to do business with you*.

## 5. It Facilitates Data-Driven Pivots

Often, entrepreneurs get “romantically involved” with their first idea and refuse to change even when it’s failing.

- **In Practice:** Discipline involves the rigorous habit of tracking metrics. If the data says your “Beachhead Market” isn’t responding, the disciplined entrepreneur has the emotional control to pivot based on facts rather than ego.

## Invitation to Contribute Articles for CMA Student E-Bulletin - Showcasing Your Expertise!

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### Submission Guidelines:

- ⦿ **Article Length:** Please prepare articles ranging between 1200 to 1500 words.
- ⦿ **Topic:** The articles can cover a wide spectrum of subjects, including but not limited to advancements in finance, industry insights, case studies, personal experiences and emerging trends in the field.
- ⦿ **Originality:** We encourage you to share your unique perspectives and experiences. Ensure that your submission has not been published elsewhere.

**Submission Deadline:** We kindly request you to submit your article by 20<sup>th</sup> of the previous month of publication. This will allow us ample time to review and prepare the upcoming issues of the CMA Student E-Bulletin.

**Submission Process:** Please send your article to [studies.ebulletin@icmai.in](mailto:studies.ebulletin@icmai.in) with the subject line "CMA Student E-Bulletin Submission - [Your Name, Registration No.]". Include a brief author bio and a high-resolution photograph to be featured alongside your article.

**Recognition and Rewards:** Selected articles will be featured prominently in the CMA Student E-Bulletin, providing you with a valuable platform to showcase your expertise. Additionally, authors of published articles will be acknowledged and the top contributors may be eligible for special recognition and rewards.

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Best Regards,

**Team DoS**

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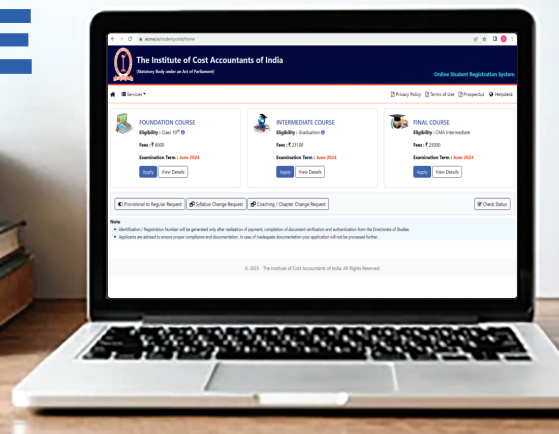


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- Passed CMA Foundation Examination
- Graduates of any discipline (Students awaiting final result also apply on provisional basis)
- Qualified CAT Level - I of The Institute of Cost Accountants of India
- Qualified CA Intermediate
- Qualified Engineers/ Qualified CS

### Course Fees

**Foundation - ₹6,000/-**

**Intermediate - ₹23,100/-\***

**Final - ₹25,000/-\***

\*Installation facility available

### Financial Aids & Scholarship Schemes

- Fees waiver scheme for Meritorious Students for CMA Foundation Course
- Fees waiver scheme for Economically Challenged-cum Meritorious Students for CMA Intermediate Course
- Revised Scholarship Scheme for Physically Challenged/ Differently Aabled Students for Intermediate and Final Course (for more than 40% disability)
- CMA National Scholarship Scheme 2024 - 2025 for Graduate and Post-Graduate Rank Holders (applicable for Intermediate Course)

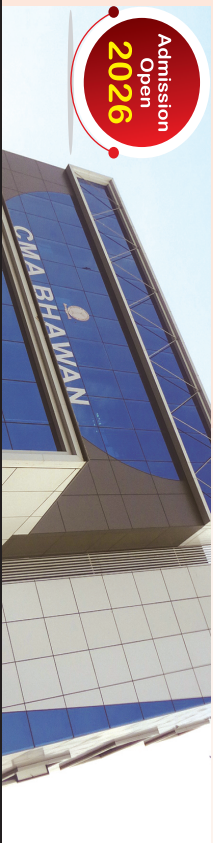
For details, please visit: [https://icmai.in/studentswebste/financial\\_Aids.php](https://icmai.in/studentswebste/financial_Aids.php)

### National Accreditation Policy

A strategic initiative of The Institute of Cost Accountants of India to strengthen accredited partnerships with Govt./ Govt. affiliated or sponsored or approved Educational Institutions/ State University or Central University or UGC or AICTE affiliated Educational Institution/ Deemed or Deemed to be Universities /CBSE or CISCE or any State School Board/Council affiliated Schools.

For details, please mail to: [studies.accreditation@icmai.in](mailto:studies.accreditation@icmai.in)

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### Headquarters

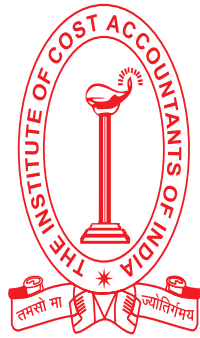
CMA Bhowan, 3 Institutional Area, Lodi Road, New Delhi-110008

011-24622156

Kolkata Office

CMA Bhowan, 12, Sunder Street, Kolkata-700016

033-40364743/40364735



# 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](http://www.icmai.in)

### Headquarters

CMA Bhawan, 3, Institutional Area, Lodhi Road, New Delhi - 110003

Ph: 011-24622156

### Kolkata Office

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