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❑ to develop the Cost and Management Accountancy profession ❑ to develop the body of members and properly equip them for functions ❑ to ensure sound professional ethics ❑ to keep abreast of new developments.

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Editorial

One can please everybody!

Union budget making is always a tight rope walk. More so, when it is likely to be the last budget before election (with strong speculation of an early poll). Yet, the finance minister (FM) has performed an outstanding job in balancing economic objectives with political compulsions to make everybody happy in such a crucial juncture.

The first challenge before the FM was to give a massive booster to the somewhat sagging consumer product market and the manufacturing sector. For this, on the one hand he has put more disposable income at the hand of the salaried people by way of raising basic exemption limit of personal income tax to Rs. 1.50 lakhs for men below 65, Rs. 1.80 lakhs for women below 65 and Rs. 2.25 lakhs for senior citizens. The slab limits were doubled: 10% tax up to Rs.3 lakhs, 20% up to Rs. 5 lakhs and 30% beyond that; deduction for medical insurance was provided for an extra Rs. 20000 for providing medical insurance to senior citizen parents and the streams of monthly income of senior citizens from reverse mortgage treated as tax free.

On the other hand, there were cuts in indirect taxes: a general 2% cut in CENVAT (from 16% to 14%) for all goods with deeper cuts for specific goods like, pharmaceuticals (reduced to 8% from 16% while anti AIDS drugs were totally exempted), buses and their chassis (12% from 16%), small cars (12% from 16%), two wheelers and three wheelers (12% from 16%), paper & paper board (8% from 12%), wireless data card, composting machine, tea & coffee mixers, packaged coconut drink, puffed rice etc (reduced to 0%) and similar cuts in many other products. Customs duty was also reduced on many items: project imports (5% from 7.5%), steel melting and aluminium scrap (nil from 5%), specified life saving drugs and bulk drugs used in their manufacture (5% from 10% with total exemption from excise duty and counterveiling duty), specified parts of set-top boxes and specified raw materials for IT/ electronic hardware industry (fully exempt) etc, etc.

Yet, the investors did not react favourably and SENSEX nose dived as the short term capital gains tax, increased from 10% to 15%, hurt them while banking shares plummeted following the waiver of agricultural loans advanced by banks to the tune of Rs. 60 thousand crores. Moreover, there were no change in corporate taxation rates and surcharge although double taxation on dividend distribution was removed by allowing a parent company to set off dividend received from a subsidiary against dividend distributed by the parent company and the shackles of FBT was somewhat loosened by keeping beyond its purview items like expenditure on company guest house and crèche, organizing sports events for employees and sponsorship of employee-sportsmen etc.

Of course, the big news is the agricultural loan waiver and debt relief to the tune of Rs. 60 thousand crores. It was a socio-economic and political inevitability with a faltering agricultural system having poor growth and loan repayment incapability that led to suicide of farmers all over the country. But who is going to take the hit – banks or the government? It is not clear in the budget, hinting at a massive off-budget exercise that will of course increase the total deficit by at least more than 1% of GDP with government compensating the banks on this count. Add to it the impact of 6th Pay Commission that may have a liability of Rs. 40 thousand crores – not specifically provided in the Budget, meaning another increase of deficit by around 0.8% of the GDP.

A bright side of the Budget is its massive emphasis on health, education and social sectors. But again success of such massive outlay reaching the grassroot of the society to elevate the economy to a new height essentially require control based on meticulous cost-benefit analyses for which Cost & Management Accountants have a massive role to play.

• President's Communique •

My dear Professional Colleagues,

Perform your prescribed duty, for doing so is better than inaction. One cannot even maintain one's body without action.

-Bhagavad Gita 3.8

By the time this communiqué reaches you will be well aware of the provisions of Union Budget 2008, particularly those relevant to the profession of CMA and the major impact the Budget will bring on the national economic scene. The world is eagerly watching every step of India, particularly in the economic domain that will also have a lasting impact on the world, more so because; India has emerged as a global power. And in this venture CMAs have played and will continue to play a very major role.

Meeting with Secretary MCA : Synchronous with the great strides our country is making the Council has drawn the road map for the development of the Institute and the profession. In this context, myself along with the Vice President had a very fruitful meeting on 14 February 2008 with Shri Anurag Goel, Secretary to the Government of India, Ministry of Corporate Affairs. The meeting was very cordial and interactive where we made a presentation on the Strategic Plan for the Institute and the profession explaining what steps the new Council has taken to improve the image of the profession. We also highlighted the new syllabus that has been introduced, the compulsory training system for students and the global alignment of the profession. Shri Goel highly appreciated the steps that the new Council has taken and wished to have another meeting with the Institute at a later date.

Eastern India Regional Cost Conference : The Eastern India Regional Conference was held at Gopalpur-on-sea, Orissa from 8th-10th February 2008. This is the first grand event organized by the South Orissa Chapter in cooperation with EIRC after the Notification constituting the Chapter. Shri Chandrashekhar Sahu, Hon'ble Union Minister of State for Rural Development inaugurated the Conference. In his inaugural address the Hon'ble Minister highly appreciated the role of CMAs. I had the opportunity to interact with the distinguished gathering on this occasion. In the conference deliberations in the technical session on Valuation Management and other sessions were acclaimed very much. Shri B B Goyal, Adviser, Cost Audit Branch, Government of India also participated in the Conference and spoke on Restructuring of PSUs. He also deliberated on the scope of the profession vis-à-vis Valuation Management and the emerging issue of Predatory Pricing was covered by me. The conference was a grand success and I congratulate the organizers for the success of such a beautiful event.

ICWAI-XLRI Jameshedpur Joint Programme : A joint programme was organized by the Institute with XLRI on 10th February 2008 at Jamshedpur on the theme "Managing Business risks- A global perspective". I had the privilege of delivering the Inaugural Address as the Guest of Honour. Shri G N Venkataraman Chairman CEP Committee coordinated the programme and presented a paper from the Institute side. Many of our members from the eastern part of the country participated in the programme.

• President's Communique •

SIRC Programme : Our Southern India Regional Council organized a Programme on Strategic Leadership where all the Chairmen and Secretaries of Chapters of Southern Region participated. In my inaugural address I had the opportunity to explain the various steps that we have taken for bringing excellence to the Institute and the profession highlighting the need for skill development. Mr G Srinivasan Chairman Cum Managing Director, United India Insurance Company Limited and our Member was the Chief Guest and spoke in detail about the strategy to be adopted to update our professional skills and face global challenges in the near future. Professor M B Athreya, Management Guru emphasized the need for taking steps to be taken at the Chapter and Regional level to improve the image of the profession. The programme was well attended. Further, Shri Balasubramanian, Mangement Consultant and our member also exhorted the members to be more proactive in their professional approach to be the global leaders.

Meeting with Chairman SEBI : Shri C B Bhave has assumed the office as Chairman SEBI on 18th February 2008 and I had an opportunity to meet him along with Shri V C Kothari CCM and Shri P V Wandrekar Chairman WIRC on 19th February 2008. We had fruitful discussions and we had explained the role of Cost and Management Accounting Profession for the good Enterprise Governance. Further, a presentation will be made shortly before him on the role of our profession on behalf of our Institute.

NACAS Meeting : The National Advisory Committee on Accounting Standards (NACAS) met on 19th February 2008 at Mumbai and the Committee inter alia discussed the implementation of International Financial Reporting System (IFRS). With the implementation of IFRS there will be a shift in the focus from historical cost to the current cost. It was brought to the notice of the Committee that Cost and Management Accounting profession is well equipped and can play significant role in ascertaining the fair value. We have already constituted a Task Force under the Chairmanship of Shri S C Vasudeva, Govt Nominee to suggest the ways and the role of our members under the new scenario.

To sum up, the Institute is now buzzing with fruitful activities to bring excellence and I invite you once again to join the march for excellence that will continue forever.

Wishing you happiness, prosperity and success in your personal and professional life.

Chandra Wadhwa

President

Tariff Methods-Transportation of Natural Gas

This article is basically focused on the major gas pipeline tariff methods presently being used in natural gas sector in the context of Petroleum & Natural Gas Regulatory Board Act. There are mainly two types of tariff methods being practiced in gas sector I) Discounted Cash Flow method and II) Cost of service method. In discounted cash flow method, tariff is worked out by discounting the net cash flows over a period of expected life so as to get the required rate of return. In cost of service method required revenue is worked based on the cost of providing the services i.e. operating expenses, capital recovery and return on capital employed and tariff is worked out by dividing the Net present value of required revenue by net present value of volumes over the life of the pipeline. Focus is also given on various tariff design like Postage Stamp: Point to Point: Zonal: and Entry-Exit: Tariff under this option comprises of separate entry charges and exit charges and both are independent.

Neeraj Pasricha*

Introduction:

Now a days energy security is most talked about topic in the country in fact to meet the target growth rate of 8%-9% GDP over next five years, growth in energy basket plays important role. In the total energy basket gas is playing crucial role particularly with major finds in eastern coast of the country. Recently with the objective to bring competition and efficiency in this area and make available the energy to different part of the country Government has introduced The Petroleum and Natural Gas Regulatory Board Act. One of the major aspect, which this Act deals with, is regulation of natural gas pipeline, this is the area generally considered as natural monopoly. By regulating the Gas pipeline, Govt. objective is to promote investment from public and private sector in this area and to provide open access on non-discriminatory basis to all the players and thereby promote competition. Act has given very broad framework to determine tariff for gas pipelines. This article is basically focused on the major gas pipeline tariff methods being presently used in natural gas sector.

In India up to 2006 major method used for working out the tariff was based on Discounted cash flow, however in 2006 Tariff Commission has worked out the tariff for biggest existing gas pipeline i.e. Hajira-Vijaipur-Jagdispur, of the country based on the Cost of Service method.

Tariff methods: Following are the two main methods being used in different countries with some modifications as per their local requirements.

Discounted Cash Flow Method: In Discounted Cash Flow Method, cash outflows on account of expected capital expenditure, working capital, operating expenses are considered, cash inflows based on the expected volume throughput and tariff is worked out by discounting the net cash flows so as to give the allowed rate of return over the expected life of the assets. Cost of the asset to lay the pipeline and other facilities to provide transportation services are considered under capital expenditure and estimated cost of future Investments for maintaining/expanding the Pipeline system may also be considered. Apart from India, Germany, Switzerland, Libya, Thailand are also using this method to work out tariff.

Levelized tariff is worked out over a period of expected life as shown below:

Cost of Service Method:

Under this method annual cost of providing the transmission services are divided into three parts (i) Operating Cost,(ii) Capital recovery (Depreciation) and (iii) Return on Capital employed. Sum of the above three is called as annual revenue requirement and to work out tariff net present value of annual revenue requirement is divided by the net present value of volume throughput over expected period of life, as explained below:

Year	-1012345							
Capital Cost	(A)							
Working Capital	(B)							
Operating Expenses	(C)							
Revenue	(D=Z * X)							
Net Cash Flow	(D-A-B-C)	x	x	x	x	x	x	x
Volume -	Z							
Tariff	X							
Tariff - Where NPV	1 of Net cash flows (at allowed rate of return) is equal to zero.							

*AICWA

However, to review in between the variable factors like expected capital cost, inflations, volume throughput, etc tariff can be worked out over small period i.e. over five years or so. In some of the European countries tariff is charged in two parts i.e. capacity charge and commodity charge. To work out the Capacity charge and commodity charge required revenue is split into two parts fixed and variable. Fixed cost is divided by maximum capacity of the pipeline and the charge so worked out is called capacity charge and variable cost is divided by expected throughput to work out commodity charge. Capacity charge is payable for capacity booked by shipper and commodity charges are payable for actual volume throughput of shipper. Rate of allowed return is considered for working out the net present value.

Most of the European countries are using this principal with certain modifications. In India power transmission tariff are also worked out based on the above principles with certain customization.

Comparison: In both the methods, inputs are same i.e. capital cost, operating expenses etc. However, in DCF method the capital recovery and return are recovered over a period of expected life in consolidated manner whereas in Cost of service method return on Capital employed and Capital recovery are separately worked out and can be monitored separately. Therefore, cost of service method is considered as simple method particularly where review mechanism is in place. In Cost of service method annual capital recovery is worked out considering equal recovery over a period of life of the asset, whereas in DCF capital recovery of the year is the balance left out amount after deducting operating cost and return on capital employed from the total annual revenue. But Cost of service method gives lower tariff as compare to DCF as cost of service method does not provide any return over equity during construction period.

Year		1	2	3	4	5
Annual Capital Recovery (Capital cost/5(assumed life)	(A)	a	a	a	a	a
Operating Expenses	(B)	b	b	b	b	b
Return on Capital Employed	(C)	c	c	c	c	c
Total Revenue Requirement	(A+B+C)	x	x	x	x	x
Volume =		z	z	z	z	z

Tariff - NPV (at the allowed return) of Total Revenue Requirement For five years

NPV (at the allowed return) of annual Volume over five years

Tariff Design: Tariff working is actually a two stage exercise under stage one what is to be charged is worked, which is explained above and under stage two how is to be charged is actually a tariff design. Tariff designs commonly employed in gas sectors are as follows:

Postage Stamp: Tariff is uniform for all infrastructures with in the given area.

Point to Point: In this design option tariff is linked directly from source to destination and generally followed in simple linear network.

Zonal: Tariff is designed by reference to movement between zones and to some extent linked with distance from source of each zone.

Entry-Exit: Tariff under this option comprises of separate entry charges and exit charges and both are independent. This type of tariff suited to complex network.

Most of the countries are using mix of the above designs based on the nature of pipeline networks in their country.❑

LETTER TO EDITOR

Anti-Dumping Duty

A company has applied for imposition of Anti-Dumping Duty on import of same product on account of which Anti-Dumping Duty has been imposed on its import and there has been increase in sales volume and per unit sales realisation of that product after the imposition of Anti-Dumping Duty.

Now, so many factors contribute to increase in sales volume and per unit sales realisation which interalia include the efforts of Marketing Department, Production Department, Purchase Department, Maintenance Department, Utility Department, Costing Department etc.

So, is it possible for the company to quantify increase in sales volume and increase in per unit sales realisation due to imposition of Anti-Dumping Duty on import of same product?

Professional colleagues can share their views.

Regards,
Rajesh Kapadia
AICWA-13882

Quantifying financial risk

The federal government's Accountability Act, combined with the Modern Comptrollership initiative, have necessitated a new approach to estimating costs for future expenditures. As CMA Michael Lionais explains, Agriculture and Agri-Food Canada has implemented a very successful process to do just this.

Michael Lionais*

Due to cost overruns across government in the 1990s, the Treasury Board of Canada instituted an initiative called Modern Comptrollership, which has evolved to include a requirement that Chief Financial Officers (CFO) of departments must personally attest to the reasonableness of financial information presented to the Government for decision making. Recently, the Government passed the Accountability Act, which makes the Deputy Minister (senior public servant) the Accounting Officer of a government department, thereby making this executive personally accountable for financial information presented to Government.

These changes underlined the need for an arms-length process by which CFOs can confirm that cost estimates in business cases are reasonable before they are presented by the Department. Agriculture and Agri-Food Canada (AAFC), for instance, has adopted a very successful arms-length process, which will be described in this article.

The validation process

All validations start with the expectation that the cost estimate developed by the project team is reasonable given the information available. The validation is carried out to review the proposal for consistency in applying departmental standards, and to ensure conformity with the spirit or intent of applicable statutes and policies. An arms-length review process also ensures that all cost elements have been properly identified and considered. Through the risk assessment process and the use of simulated risk-adjusted costs, AAFC is able to develop a stable planning figure for use by planning staff in the development of longer-term strategic considerations.

One of the main challenges in assessing financial risk is ensuring that the costs presented are a reasonable estimate at a given time in the approval process. The ultimate objective in performing this analysis is to enable the Director General of Finance to provide an objective recommendation to the CFO as to whether financial attestation should be provided with or without observation.

Potential conflicts

There are well documented human behavioural tendencies in management. Typically, research has indicated that managers are optimistic and tend to overestimate revenues, underestimate costs and think short-term. These tendencies are usually attributed to group think, bandwagon effects and consequential behaviour when one is committed to a project. This can be exacerbated in a government environment that is not constrained by profit. Additionally, there is usually a great deal of pressure to create programs for Canadians as quickly as possible for the lowest incremental cost possible. As such, project managers operate under the pressure of a cost ceiling and delivery deadlines.

Further, managers, in all industries, typically pad their numbers to allow some contingency to address the uncertainty of their cost estimate. Despite this padding, cost overruns still occur routinely. In large part, this has to do with the quality of the financial information used to build the cost estimate of a program under development. Typically, the program structure and delivery mechanisms are refined as the funding estimate is developed concurrently. As such, the funding proposal may not match perfectly with the program design. Further compounding this issue is that the financial estimate will be based on the best information available, but the reliability of information underlying the financial estimate isnâ•™t always identified. Rather, itâ•™s usually assessed intuitively by the reader of the business case.

To address these issues, Treasury Board has mandated CFOs to develop the "most reasonable" estimate so that the most likely project costs can be identified to reduce the likelihood of cost overruns. This is significant because cost overruns typically have to be absorbed within a department's assigned resources, which means that reduced services (internal or external) or compensation must be provided to Canadians should cost overruns occur. As a last resort, a department can request additional funding from the Government. Remember, it's illegal to exceed the appropriation (budget) that Parliament has assigned to a government department and that by personally attesting to the reasonableness of the financial information the Deputy Minister and CFO assume a personal accountability to Parliament.

Probabilistic model

The probabilistic model is based on providing a reasonably independent assessment of the quality of the information underlying the financial

*Manager of Strategic Costing, Department of Agriculture and Agri-Food Canada

Table 1: Data integrity scale and categories

Data integrity confidence level	Appropriate contingency ranges	Cost categorization	Risk weight	Criticality
Very low	> 40%	ROM	Very substantial	Vey substantial
Low	31-40%	Indicative / ROM	Substantial	Substantial
Medium	21-30%	Indicative	Significant	Significant
High	11-20%	Sub / indicative	Insignificant	Insignificant
Very high	0-10%	Substantive	Very insignificant	Very insignificant

estimate. This is the foundation of the procedure because if the data underlying a decision is potentially flawed, executives need to factor this into their decision. Individuals preparing the cost estimate aren't in a position to provide an arms-length assessment of the validity of the data underlying the financial information as it is difficult to challenge a program that you have been championing for the previously mentioned reasons. As such, the data integrity assessment is the foundation of the model.

The model itself is derived from documentation produced by the RAND institute, NASA and the U.S. Department of Defense (U.S. Naval Post Graduate School and Defence Acquisition University). The data integrity scale is similar to those in the NASA Cost Estimating Handbook, Cost Readiness Levels (2004) and in a published article by the Association for the Advancement of Cost Estimating (R.B. Lorance and R.V. Wending. â•œBasic Techniques for Analyzing and Presentation of Cost Risk Analysis," 1999).

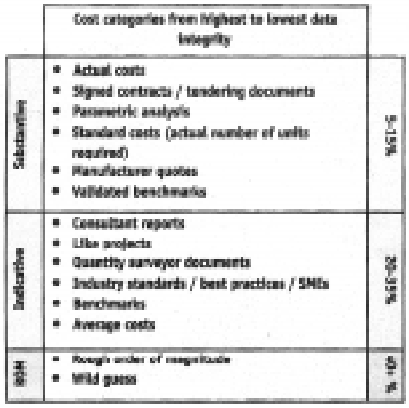
The costing validation procedure starts with a check to ensure that all appropriate cost components have been included in each cost element. If so, this is deemed to be the most likely cost. If not, the cost element is adjusted as required to determine the most likely cost. The data underlying the most likely cost estimate is fit against the data integrity scale in Table 1. Data is categorized into three broad categories: rough order of magnitude (ROM), indicative or substantive. An appropriate contingency range has been assigned for each category. The analyst will make an assessment of an appropriate contingency rating considering the categorization of the costing data, the type of costing information being considered and the information provided by the Business Case sponsor to substantiate the cost estimate in the business case.

This is a subjective assessment however, it's common in cost estimating techniques. All data integrity assessments are fully identified, described and defended in the report of the findings, which is factored into the managerial approval process.

Figure 1 depicts a practical scale of how various cost data is rated from highest to lowest data quality. Again, with this information a model is created which identifies lower, most likely and upper bounds for each cost element. The lower boundary range is typically 20% of the appropriate contingency range from the table above. This accounts for the tendency to overestimate revenue and underestimate costs. Also, a triangular distribution that is skewed to the right is typically used because the model's purpose is to ascertain the uncertainty associated with the financial estimate, not to recreate the financial estimate itself. The distribution is skewed to the right to account for the behavioural tendencies previously identified.

Identifying the appropriate bounds is the most difficult part of the process and requires collaboration with the team who developed the case. It's essential that the contingency amounts imbedded in the funding requirements identified by the project sponsor be removed to prevent overstating the potential financial risk by double counting uncertainty. Once the base value is determined, the data sources for determining it are identified and matched to the scale in Figure 2. This step can only be accomplished through discussion with the team who developed the case. It is the foundation for determining an appropriate contingency range for the cost estimate. If, for some reason, the business case sponsor is game planning, there are other techniques that can be used to model the costs. One example is to have the sponsor identify a cost for which there is only a 1 in 10 chance that the actual cost will be lower, and then identify a cost for which there is only a

Figure 1: Practical scale for rating data quality



10% chance that the actual cost will be higher.

The model is then simulated using a Microsoft Office Excel Add-In. Several Excel Add-Ins exist to enable the application of stochastic techniques to an Excel spreadsheet. Two examples of these Excel Add-ins are Crystal Ball and @risk. The model is run using Monte Carlo simulation to a 95% confidence level to determine the probability of exceeding the identified cost estimate and the amount of funding required at a specific confidence interval.

For programs in which public funding is disbursed to Canadians, a 95% confidence interval is used. A lower confidence interval, typically 80%, is used for internal purposes. The higher confidence interval is used for disbursements to Canadians because the department must ensure that it's able to deliver on the Government's commitments to Canadians; whereas, the department is willing to accept more risk on internal decisions. This is because the data sources underlying internal decisions are typically more refined than the data sources supporting the financial estimate of external programs.

Results

To demonstrate this technique, a simple spreadsheet model is provided below (Figure 2). This spreadsheet is an example of a fictitious program in which the Government will provide $1,000 to each eligible Canadian. In this case, based on Statistics Canada data, it is anticipated that there will be 60,000 eligible recipients. Using standard cost metrics, it will cost $1,345,980 for Direct Program Administration Costs and another $2,430,490 in Indirect Program Delivery Costs for a Total Program Cost of $63,776,470.

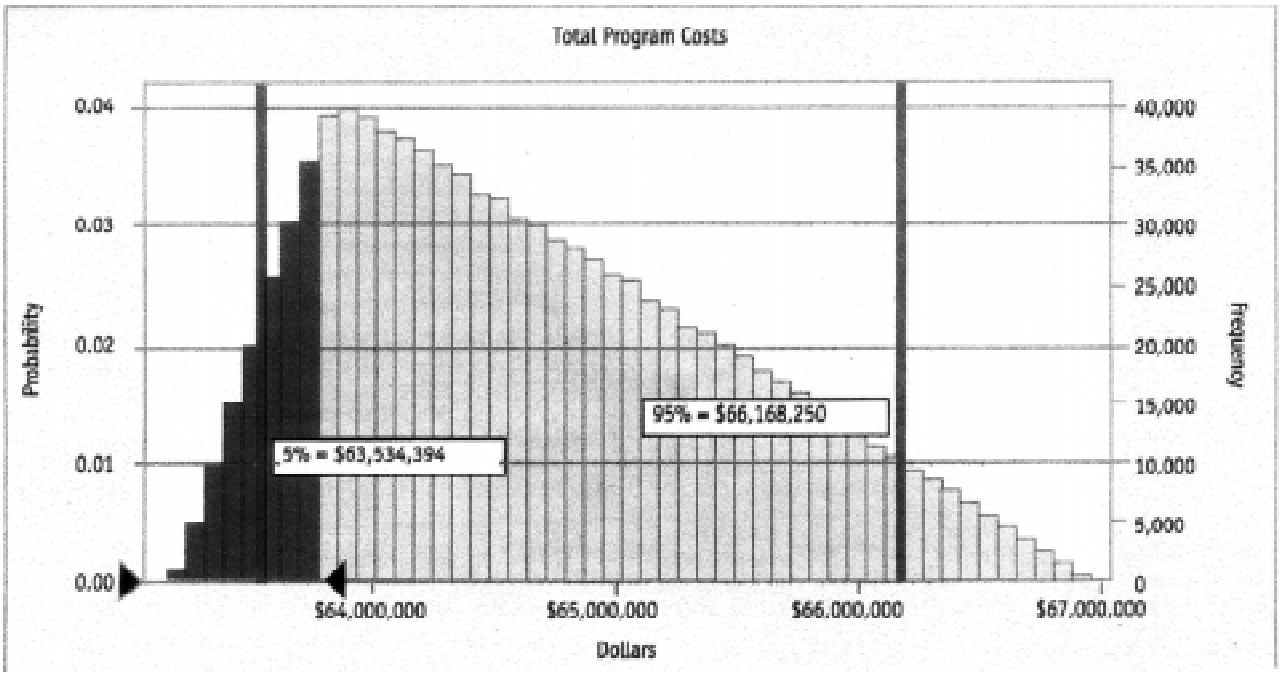
In this model, tan squares are links or standard ratios, yellow are data integrity factors, green are assumptions and blue are forecasts. The key to the model are the data integrity factors. In order to better understand the model, several of the data integrity factors will be briefly expanded:

- Amount: This amount is fixed — as such, a data integrity factor of 0% is applied;
- Number of claimants: This estimate is based on Statistics Canada information, which is considered to be very good. As such, the highest data integrity factor of 5% is applied;

Figure 2: Financial risk assessment model of a fictitious program

Cost element	Cost driver	Data integrity factor	Most likely	Lower bound	Upper bound	Assumption	Forecast	Totals
Projected grant funding								
Amount	$ 1,000	0%						
Number of claimants	60,000	5%	60,000	59,400	63,000	$60,000	$60,000,000	$60,000,000
Direct program delivery costs								
Full-time equivalents	15							
Generic full-time salary	$ 69,000	10%	$ 69,000	67,620	75,900	$ 69,000	$1,035,000	
Allowances	$ 1,600	10%	$ 1,600	1,568	1,760	$ 1,600	$ 24,000	
Employee benefit package	$ 13,800	0%					$ 207,000	
Training	$ 997	20%	$ 997	957	1,196	$ 997	$ 14,955	
Telecommunications	$ 100	20%	$ 100	96	120	$ 100	$ 1,500	
Computers	$ 535	20%	$ 535	514	642	$ 535	$ 8,025	
Travel	$ 1,050	40%	$ 1,050	966	1,470	$ 1,050	$ 15,750	
Accomodations	$ 1,200	20%	$ 1,200	1,152	1,440	$ 1,200	$ 18,000	
Other supplies and services	$ 1,000	10%	$ 1,000	980	1,100	$ 1,000	$ 15,000	
Office furniture and equipment	$ 450	20%	$ 450	432	540	$ 450	$ 6,750	
Total direct program delivery costs								$ 1,345,980
Direct program costs								$ 61,345,980
Total indirect program delivery costs								$ 2,430,490
Total program costs								$ 63,776,470

Figure 3: Probability distribution for total program costs of fictitious program



- Generic full-time salary: This estimate is considered to be a weak substantive estimate. As a result a data integrity factor of 10% is applied;
- Training: This amount is based on a benchmark that is considered indicative, and a data integrity factor of 20% is applied; and
- Travel: The number of trips and locations were known, but the timing and duration were not, so the estimate is considered to be rough order of magnitude and a data integrity factor of 40% is applied.

When the model is simulated, the distribution in Figure 3 is produced.

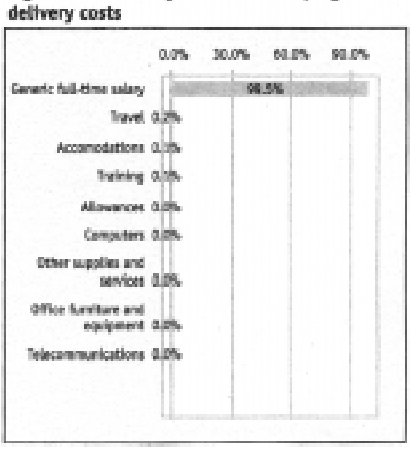
This distribution indicates that there is an 85% likelihood that the identified funding of $63,776,470 will be insufficient to deliver the program based on the data integrity assumptions modeled. Moreover, it indicates that there is a potential unfunded liability of $2,391,750 at the 95% confidence interval. This allows CFOs to study the results to determine whether they are willing to accept the indicated financial risk. If so, the CFO is in a position to develop cash management strategies, as the amount of potential financial risk has been quantified. The level of risk should be reassessed as the information underlying the financial estimate is improved over time.

If the CFO isn't willing to accept the financial risk as modeled, the simulation identifies the relative importance of the cost elements from a risk perspective. The model shows which elements have the most influence on the cost estimate. In this example, it is obvious that the number of eligible recipients presents the most financial risk; yet the data integrity factor indicates the source of the estimate is considered high quality. Consequently, it is likely prohibitively expensive from both cost and time perspectives to refine this source of data further.

However, within the direct program costs, the cost elements can be broken down in a sensitivity chart (Figure 4) to determine whether the data underlying the financial estimate can be improved to reduce the financial risk associated with the program. Furthermore, an estimate can be made of the cost of improving the data integrity to determine if the benefit of refining the information further outweighs the costs of doing so.

In this example, moving from generic to position-specific salary estimates would address 99.5% of the

Figure 4: Sensitivity — total direct program delivery costs



uncertainty in the direct program cost category. This, in itself, shouldn't be either an overly onerous or expensive process, and the reduced financial risk that would result would likely be worthwhile.

The cost elements that represent the greatest financial risk can be specifically identified and targeted to reduce the financial uncertainty associated with the data source used to create the financial estimate. As such, in the event that the CFO refuses to attest to the reasonableness of the financial estimate, the sponsoring executive is informed of the reasons why and what specific cost elements need to be refined to reduce the financial risk to a more acceptable level. Moreover, this analysis can serve as the basis for the development of risk mitigation strategies as the relative importance of the cost elements from a financial perspective has been quantified.

Impact on business

This procedure has been in place at AAFC since October 2006. Several significant proposals have been reviewed, ranging in value from $100 million to $10 billion. In several instances, the funding requested in the business case was adjusted (up and down) following validation to reflect the most reasonable estimate of the cost implications, considering the reliability of the information upon which the financial estimate is based. Cash management strategies are also being developed to address the potential unfunded liability of proposals that have been attested to as reasonable in situations in which the department is able to accept the potential unfunded liability.

The procedure is reaping intangible benefits as well. Financial risk is being concretely considered in the development of the business case, whereas previously this type of risk wasn't necessarily a focus during a proposal's development. This has led to more fiscally informed decision making at AAFC. Also, by quantifying the financial risk in proposals, the fiscal environment is stabilized, which permits executives to focus on strategic outcomes rather than urgent cash management issues. This increased fiscal awareness increases the chances that the business case will be accepted as proposed and reduces the likelihood that Treasury Board will impose financial terms and conditions on business cases submitted.

In turn, increasing Treasury Board's confidence in the stewardship of a government department may lead it to increase the authority delegated to the department, which will increase the department's autonomy and enable it to better serve Canadians by allowing it to be more responsive to Canadians' needs. Additionally, greater fiscal stability in government departments will enable the Government to better project its financial situation, thereby facilitating better governance of Canada.

Conclusion

The procedure described predicts the chance of exceeding an identified budget and quantifies the potential financial obligation between the identified project cost and the predicted cost of the business case at a specific confidence interval. This process is iterative; it can be updated as the quality of the data underlying the cost estimates is updated. This determination of the potential unfunded liability supports the Government of Canada's Modern Comptrollership initiative and permits the CFO to make an informed attestation to the Deputy Minister of the department that the financial information presented is a reasonable estimate of the projected costs of the business case at the time of the analysis.

In closing, the procedure itself:

- is a scientific methodology based on identified and defensible assumptions;
- is scalable to fit information and time available;
- addresses the optimistic nature of program managers;
- provides a meaningful assessment of the total cost implications of the business case and any potential unfunded liability associated with the proposal;
- demonstrates due diligence as required under Modern Comptrollership; and
- reduces executives' reliance on intuition.

This procedure was reviewed by a panel of judges and deemed to be the best financial application of the nominations received for the inaugural 2007 Monte Carlo Simulation Award sponsored by Decisoneering, a subsidiary of Oracle, and the makers of Crystal Ball.

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Six Levels of Financial Knowledge

Here's a framework that management accountants can use to help their organizations reach new heights of financial understanding and become more profitable

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In the October 2003 issue of *Strategic Finance*, Paul Sharman made the case for management accounting. This topic couldn't have been more timely then, and it's even more critical now. To the extent that the financial community can engage both itself and line management in a soul-searching look at what they really know about their businesses, the case for management accounting can be made emphatically. With the appropriate framework to shape financial knowledge, the management accounting function should become an organization's principal decision-support platform.

Few line managers or financial executives are satisfied with the current state of decision support because it's too heavily driven by the financial accounting template and cost systems motivated by overhead allocation. But dissatisfaction usually leads businesses to take a hard look at themselves and set some tough goals relative to acquiring more profound knowledge. What this engagement process requires is a solid but easily communicated framework for self-evaluation and planning, which I'll propose. With this self-evaluation vehicle, any company can face brutal reality and begin the journey toward reaching new levels of financial understanding.

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The framework recognizes that we're on a cusp of decades of development coming together in cost measurement and estimation, data management, business process modeling, enterprise resource modeling and planning, mathematical optimization, raw computing power, electronic visualization, application software development, and more. As they said on The Six Million Dollar Man, "We can rebuild him. We have the technology."

I term my proposed framework "the levels of financial knowledge." As you read the description of each level, I expect you to ask, "Where is my business?" Any reasonably sized business may find itself with elements of more than one level operating simultaneously—depending on the function, location, or business unit. Nevertheless, the framework should be quite prescriptive for evaluation and planning.

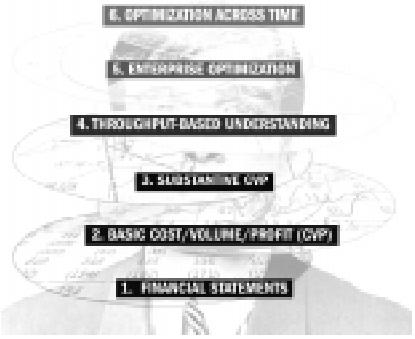
Levels of Financial Knowledge

The framework consists of six levels of financial knowledge, and the word "financial" is most operative here. I mean dollars and sense; this is much more than data and information—I'm talking about knowledge. First let's take a look at a synopsis of each level (see Figure 1), and then I'll go into more detail about each one.

Level 1: The business can count and keep score in the aggregate sense (business unit/corporate) by tracking cash, accounts receivables, payables, etc., and it can generate periodic financial statements.

Level 2: The business has a traceable measure of output volume and readily identifies fixed and mvariable costs. It has internalized the basic vocabulary of cost/volume/profit (CVP).

Figure 1: Levels of Financial Knowledge



Level 3: The business has a well-defined breakdown of CVP elements and understands how these more detailed elements relate to working capital behavior as well as to both Level 1 and Level 2 templates. It can fundamentally assess the business profitability drivers and can generate appropriate policy statements relative to spending money to make money.

Level 4: Throughput, as opposed to output, has become the focus of operational and financial knowledge. The fundamental engineering/economic recipes of input/throughput/output (ITO) are known. The primary transformation constraints are known, and this knowledge is a principal factor in planning and resource allocation.

Level 5: At least in a planning sense, but, more importantly, operationally, the business can optimize simultaneously across multiple inputs/costs/recipes/constraints/outputs. Fed by the decision-support system, the methodology of marginal economics has moved from the theoretical to the practical.

Level 6: The business can optimize simultaneously across multiple inputs/costs/recipes/constraints/outputs and time periods. Managing periodic slack resources, capacity, and inventory across time is accomplished with profound knowledge.

Knowledge acquisition is a journey that requires the appropriate modes of transportation: systems, structures, and processes. It's a journey that an entire business must take, not just certain subsystems of it. Most of us are familiar with businesses that have subsystems that possess significant knowledge, but until that knowledge is integrated into the company's overall financial knowledge, the system's financial knowledge remains at lower levels.

Let's thoroughly investigate the levels by concentrating on the vocabulary and significant knowledge concepts and constructs of each one.

Level 1 Financial Knowledge

Too many users of accounting information think of it as "the incompetent reporting the irrelevant to the indifferent," but financial accounting is the language of business. If you don't have the knowledge to understand the language and speak it credibly, then you can't communicate with those who are the source of capital. Thus, the Level 1 knowledge base connects a business to the outside world.

Since financial accounting constitutes Level 1 knowledge, every business must pass through Level 1 to move through the other levels. This is simply because any level of financial knowledge must possess the systems to tie back to the financial accounting templates—the standard P&L, balance sheet, and cash flow statement.

The principal concepts behind Level 1 knowledge are derived primarily from ratio analysis, which facilitates comparing financial performance and financial potential independently of industry or asset base. The significance of return on equity (ROE), Economic Value Added (EVA®), and other Level 1 concepts, should never be underestimated. These concepts constitute the basic analysis toolkit for the suppliers of capital and, thus, for the ultimate indices of executive performance and reward.

Level 2 Financial Knowledge

While Level 1 knowledge tells us about a business's profitability, it tells us very little about the *business*. In order to move to a more fundamental understanding, a business must establish a traceable measure of output (output unit), a vital stopover on the journey to knowledge acquisition even for the multiproduct business.

An output unit could be a case, a ton, a foot, an invoice, a gallon, customer count, a transaction—it depends on the business—but each firm building its knowledge base has such a construct. Knowledge really begins to grow when the business can make reliable assessments of how total costs behave as a function of changes in output. To do this, the business must attach variable cost to a single unit of output—a giant step on the journey.

Table 1: Differences in Level 1 and Level 2 Profitability Templates

Level 1 P&L Template	Level 2 P&L Template
Sales	Sales
Less: Cost of Sales	Less: Variable Cost
Gross Profit	Contribution Margin
Less: SG&A	Less: Fixed Costs
Operating Profit	Operating Profit

When you have output volume and variable cost per output unit, you have the basis for Level 2 vocabulary. The first important concept is Level 2's profitability template, which is contrasted with Level 1's profitability template in Table 1.

Although these profitability templates appear similar, they're remarkably different because of increased knowledge. As the phrase "contribution margin" replaces the phrase "gross profit" in a business, knowledge has grown considerably.

Additional key concepts at Level 2 flow from the P&L template, variable and fixed costs, and contribution margin. The first is breakeven, the second is operating leverage, and the third is the idea of decreasing unit (average) cost as a function of volume. As the business internalizes these concepts, its knowledge increases enormously. The business prices and sources more intelligently, it makes funding decisions more intelligently, it negotiates more intelligently, and it evaluates opportunities more intelligently. Simply, it's smarter.

Level 3 Financial Knowledge

When a business transitions to Level 3, it has learned that return on assets (ROA) must be employed as the enterprise's guiding profitability gauge. (And, rest assured, EVA is a form of ROA.) First, business activity and profitability require funding, and a competitive return must be generated on those funds.

Second, the business has learned that it must expand the basic CVP categories to capture more robust activity descriptors. Not only does it require knowledge of variable costs, but the business needs to know how they vary per unit or per dollar and whether or not they are inventoried (manufacturing or SG&A). Not only does it require knowledge of fixed costs, but it also needs to know whether they're inventoried or not and whether they represent noncash (depreciation) or not. The business also requires knowledge about how many times a cost is inventoried, so categories such as raw materials are imperative for breaking out. Table 2 illustrates the "minimum spec" categories for Level 3 knowledge.

Third, the business ties these more robust CVP categories into elements of assets—-particularly current assets—by applying asset turnover constructs.

Table 2: Level 3 Minimum Spec CVP Categories

1. **Unit volume.** The number of units of output produced and sold (as in Level 2).
2. **Gross price.** The average gross price per unit of volume.
3. **Materials costs per unit.** For the average manufacturing firm, this might constitute all materials. For firms with one primary material (pulp for paper making, for instance), we might have two materials categories.
4. **Variable labor costs per unit.** Getting a reliable measure on what portion of direct labor is variable can be challenging but is often critical.
5. **Variable processing costs per unit.** This could include a variety of dimensions, but energy and water are prime examples.
6. **Fixed manufacturing costs.** This measure would include all cash expenses that don't generally vary with changes in output.
7. **Revenue-variable S&A expenses.** This measure includes all expenses that vary with dollars of revenue (as opposed to units). Sales commissions and royalties are examples. It is important to distinguish here how expenses are actually incurred vs. how they are budgeted.
8. **Unit-variable S&A expenses.** This includes all variable S&A expenses that vary with units sold, such as freight charges. (The reader should grapple with understanding that separating revenue-variable from unit-variable expenses has enormous pricing and other business-knowledge implications.)
9. **Fixed S&A expenses.** This includes all cash S&A expenses that don't vary with unit volume.
10. **Manufacturing fixed assets.** This is the end-of-year book value (net of depreciation) of manufacturing fixed assets.
11. **S&A fixed assets.** This is the end-of-year book value of S&A fixed assets.
12. **Depreciation rate on ending fixed assets.** Note ending vs. beginning.
13. **Receivables turnover.** This is the number of times that customer receivables turn over each year, which is defined as sales divided by ending receivables.
14. **Materials turnover.** This is the number of times that raw materials turn over each year and is defined as total annual materials cost divided by the ending value of materials inventory.
15. **Work-in-process and finished goods turnover.** This is the number of times WIP and finished goods turn over each year and is defined as cost of goods sold divided by the ending value of this inventory.

After it does this, it not only can plan an activity but the funding of it as well. Again, see Table 2.

Finally, the business has combined CVP elements and turnovers into an ROA model, which allows it to understand the constructs that truly define Level 3 knowledge:

- It can fundamentally assess its profitability drivers (profitability represented by ROA). It now has a knowledge-driven platform for evaluating profit-improvement opportunities, capital-spending opportunities, and tradeoffs among drivers. It can track drivers on a continuing basis.
- It can make very definitive policy statements about the limits of spending money to make money. These initiatives could be R&D, promotion, hiring, training, etc.
- It can apply its business modeling at more granular levels such as product-line profitability or customer profitability, although Level 4 knowledge can be a much more definitive achievement level for true product-line profitability.

Only 10 to 15 years ago, a business that consistently operated at a Level 3 state of knowledge had a distinct competitive advantage. Today, we must raise our sights.

Level 4 Financial Knowledge

There's a very distinct increment in knowledge when moving to Level 4. This increment recognizes that the business isn't just an output system but a highly interdependent input/throughput/output system. And this ITO system is defined much more effectively by the discipline of process engineering than by the discipline of accounting. Nevertheless, the Level 4 business has married the engineering equations with the accounting equations.

An ITO system possesses known physical recipes (or what older accountants call bills of material) that are defined by their interdependencies as well as their dependencies. If, say, a manufacturing firm is at least partially self-sufficient in its use of energy, it converts fuel and water into steam and then steam into electricity and electricity into machine hours. That's the dependency. But electricity is used to run the steam plant, and manufacturing by-products may be used as fuel to convert water to steam. The Level 4 business can fundamentally specify and track these interdependencies. It can deploy them to create a credible operating plan and also a reporting and control system tied to the financial reporting and control system.

Level 4 knowledge also introduces profound understanding of the multiple and interdependent constraints that often define the ITO system capabilities. The business recognizes that its system is composed of interconnected resources on which processes are performed. It knows the capacities of those resources and the recipes for performing the processes and the process speeds. The business knows and has documented how costs actually vary as processes are performed on those resources. (It knows how they vary per input and output unit, as well as resource unit, and how they are impacted by process yields.) And, yes, it knows where the defining constraints lie.

While Level 3 introduces profitability drivers as a key construct, Level 4 dimensionalizes how those drivers really operate. At Level 4, the business knows that only three relations are required to understand and account for all operating dependencies:

Relation 1. There is stuff in, stuff out, and process yield.

Relation 2. A factor cost per output unit is completely defined by resource units per output unit, factor consumption per resource unit, and cost per factor unit.

Relation 3. It isn't contribution margin per output unit that drives the system—it's contribution margin per key resource unit. (Thus, Level 4 is a better platform for understanding product-line profitability than Level 3.)

That's it. That's all there needs to be. At this point some of you may be asking, "Isn't this activity-based costing (ABC)?" Well, Level 4 is what ABC wanted to be when it grew up and before most businesses turned it into an elaborate overhead-allocation exercise.

Level 4's vocabulary greatly depends on applying contemporary

technology. This knowledge must reside on an information-and decision-support platform that possesses the following characteristics:

1. An integrated model of the business that can withstand engineering and scientific scrutiny.

2. The ability to credibly reproduce the firm's Level 1 financial reporting through the model (i.e., it can withstand accounting scrutiny).

3. The ability to deploy the model to react rapidly to tactical and environmental changes—not just produce a plan.

4. The capacity to fundamentally deploy the model for strategic analysis and decision making.

Many businesses possess enough integrated Level 4 knowledge to create a very credible annual operating plan, but only a few have truly reached this level on a continuing basis.

Level 5 Financial Knowledge

The transition into Level 5 financial knowledge is accomplished only with very contemporary supporting systems, structures, and processes. You'll know it when you see it, but there are three primary ingredients for getting there.

1. Substantive cost/volume/profit knowledge and supporting information-handling structures (i.e., Level 4).

2. Very contemporary business process modeling that fundamentally maps the input/throughput/output interrelationships and constraints across the entire business.

3. A contemporary optimization platform that accommodates the business model and allows the business to simultaneously optimize its ITO system in terms of all flows through the system (product mix, sourcing, resource utilization, etc.).

Thus, the essence of Level 5 financial knowledge initially is captured by the capability to fundamentally optimize the business—at least in a planning mode.

Although business-level financial optimization is only just getting into the knowledge-management capability of more sophisticated firms, it will come on quickly. In high-volume process industries it will soon be required to continue participating in the industry. Other industry categories may move more slowly, but the following new best practice is now observable. To enter Level 5, a company has already taken the following steps:

1. The business has mastered Level 4.

2. The whole business, not just part of it, has been fundamentally mapped and modeled at a substance level where modern optimization solvers are imbedded in the model.

3. The business has thoroughly validated the model. It has selected real historical time periods and recreated actual flow volumes and financial reports throughout.

4. The business has "deconstrained" the validated model and begun to fundamentally learn the optimization relationships across its systems. A validated optimization model always creates significant new knowledge.

5. The business has acted on the more tactical-level profit-enhancing opportunities the model offers. The outcomes of these tactical actions are further reinforced and refined in the model, which is a principal tool for all continuous-improvement project selection and justification.

6. The business has internalized the model's use as a condition for all capital justification and strategic analyses.

Again, you'll know it when you see it.

The Level 5 vocabulary of optimality includes two other constructs that greatly facilitate knowledge building. The first is opportunity cost. In an interdependent, multiconstraint ITO system, the opportunity cost of another resource unit, another labor hour, another source of materials, another unit of saleable product—and so on—greases the whole decision-making process. To return to our steam, electricity, and operating machine example, if each is constrained, which has the highest opportunity cost? Which one should receive the infusion of capital first? On which can we go outside for added capacity (OK, outsource), and which must be internally upgraded?

Knowledge of opportunity cost greatly enhances pricing decisions and negotiations, and it provides the platform to vastly improve priority setting and to allocate scarce resources. Since the marketplace is often a highly binding constraint in an optimized system, opportunity cost constitutes an ultimate measure of customer profitability (e.g., the next customer).

A by-product of opportunity cost is Level 5's second key construct—decision making at the margin. Although marginal analysis is done at any level of financial knowledge, at Level 5 it almost defines the way the system works. For example, unless a business has reached this level, a decision to outsource a key process lacks sufficient knowledge for dealing effectively with all the inter-dependencies. Or, for instance, a decision to bring in semifinished units and avoid the capital necessary for expanding a constrained resource has a huge number of impacts across the system. It can radically impact the optimal product mix, the energy balance, and optimal sourcing. And it can literally change the whole face of the business when, at the margin, you move from one optimum to another optimum. Even a Level 4 business has trouble coping with these inter-

dependencies because it lacks the capacity to specify what is best in an absolute sense.

You can't overestimate the importance of enterprise-wide enhancements available to a Level 5 business. Whether it concerns resource allocation to competing remote sites, decisions to open/close, intrasystem transfers, inventory swings, etc., the enterprise has more profound knowledge. And this knowledge allows it to move faster and more intelligently with the best interests of the entire system in mind.

I once worked for a CEO who excelled at what he termed back-of-the-envelope economics. Of course, you can't put Level 5 knowledge on an envelope. It takes contemporary technologies supporting the company's desire to get there. Yet the prize is worth the chase.

Level 6 Financial Knowledge

At Level 6, a business not only exhibits Level 5 knowledge, but it can apply it across multiple time periods. Is reaching this level really that big of a jump from the previous level? The contention here is that the capacity to optimize across time is a huge increment in at least the application of knowledge—and most probably knowledge itself.

There are several driving constructs behind the financial advantages of optimizing across time. The first driving force is simply the ability to plan through seasonality in a profit-optimizing fashion. Whether this seasonality is in demand, factor prices, or resource productivity, the capability to deal optimally with the seasonality is Level 6's principal defining characteristic.

A second driver, which is highly interdependent with seasonality, manages periodically slack or constrained resources. As a highly interdependent ITO system faces seasonality, it may use its knowledge to optimally deploy periodic slack resources to buffer the flows through the system via buildups and drawdowns in various inventories. For instance, suppose we have a highly seasonal business, we possess several similar machines with different run speeds/yields across product lines, we can deploy some work-in-process and finished inventory, and we must take down each machine for preventive maintenance at least twice each year. A Level 6 firm would know exactly how to simultaneously optimize production (and\mix), inventory buildups/drawdowns, and machine takedowns each time period across the planning cycle. Businesses have always had to do this, of course, but at Level 6 they do so with profound enterprise-wide knowledge rather than within subsystems. Multivendor, multisite, multigeography, logistically complicated businesses will be hugely impacted when they can approach Level 6 capability across multiple time periods.

Another driving concept is the capability to manage the uptime/downtime sequencing of key resources across multiple time periods with the optimality of the enterprise governing the decision-making process. The interdependent complexities across a business that has a tricky need for preemptive maintenance can single-handedly justify the pain of moving to this knowledge level. I'll even go so far as to say that to avoid capital spending by more profoundly managing uptime and downtime across time periods will in itself pay back the investment in gaining Level 6 knowledge.

A further driving concept behind moving to this level is the more fundamental ability to manage the complexity of multiresource, multiproduct/service setup times, run lengths, and run speeds across time periods—especially in just-in-time (JIT) environments.

A final driver is that it doesn't take a business leader long to tune in to an absolutely basic principle of financial knowledge: Profit flows don't equal cash flows. Yet this basic principle needs Level 6 business-wide modeling to receive optimal treatment. Inventory buildups and drawdowns and the behavior of receivables in a seasonal environment highly impact the profit flow vs. cash flow principle. It takes very sophisticated business models that optimize the enterprise to truly deal with these complexities.

The Level 6 fraternity contains very few members. Those who have moved past Level 5 into an optimality model with many time periods have done so primarily within a planning framework. But Level 6 comes with dramatic, enterprise-level payoffs to those willing to take the journey.

Collective Mastery

Management accounting can provide a business with the decision-support environment in which it can evaluate its financial knowledge level and establish a target-setting vehicle for continuous improvement. Knowledge, though, is only the beginning. At each level, we seek to achieve a greater sense of mastery, which implies that we not only possess knowledge but have the understanding and confidence to act on that knowledge in a way that leads to superior financial outcomes. Knowledge is an absolute prerequisite, but collective mastery is the ultimate objective. By "collective mastery" I imply that knowledge is broadly and deeply shared within the business and that individuals possess the knowledge, resources, and skills to master the operating requirements of the interconnected processes. Moving up the levels of knowledge is well worth it.❑

Performance Management Systems–Building the Competitive Advantage

Krishna Chaitanya .D*
Jayendran. G.S*

"Know the enemy and know yourself; in a hundred battles you will never peril" This quote was made by the legendary Chinese general Sun Tzu in the context of warfare in 6th century B.C but is equally relevant to how businesses operate today. The key driver in any corporate strategy is the knowledge of the business, its market and its competitors.

What is Performance Management?

Performance management includes the processes of planning, measuring performance against plans and actioning to ensure the predetermined goals are achieved.

Business Executives strive to transform strategies into measurable metrics and to obtain greater insight into the various cause-effect relationships that influence their business.

This is achieved by using a combination of people, processes and technology to collect relevant data from various functions and sources, analyze the same, collate the results to identify course of action and view performance of the actions. This combination of people, process and technology is known as the **Performance Management System**.

The decision of what business processes to choose for deployment of a Performance Management System would depend on several factors such as complexity, variability, controllability and relative importance of the process. For example, a manufacturing enterprise would typically target the following areas for early wins:

- Procurement and Spending
- Production
- Inventory
- Quality control

The Technology behind Performance Management

Enterprises that have effectively deployed Enterprise Resource Planning (ERP) systems as well as those that use alternative architectures are now being faced with the problem of 'data explosion'. This has resulted in the advent of technologies to effectively manage and leverage on these masses of data.

Performance Management Systems typically ride on the back of Business Intelligence technologies to provide the right persons in the organization, with the information required to effectively manage performance.

Typically, they include one or more of the below IT systems:

- Data warehouse – consolidate and reconcile information from across disparate business units and IT systems into a common repository which can be used for enterprise-wide analysis.
- Business Intelligence Systems– utilize the organization's data (often from a data warehouse) to create meaningful analysis and reports to stakeholders thereby enabling decision-making.
- Scorecards and Dashboards – are reports which are displayed in an ergonomic and easy-to-read format. They are often customized to the requirements of the reader and provide the necessary information the reader requires.
- Decision Support Systems – are specific systems designed to support decision making. They consist of one or more IT applications that enable structured problem solving.
- Management Information System - refers to the people, process and technology elements which collectively enable processing of data into information for management decisions.
- OLAP - expanded as Online Analytical Processing is a technical tool that enables users to process data (usually from a data warehouse) and provides multi-dimensional analysis.

Benefits of having a Performance Management System

An effective Performance Management System results in simplifying the management activity in an organization. The benefits include the following:

- **Alignment of organizational performance to strategy** to enable maximization of output in achieving common goals.
- **Objectivity and comparability** in performance evaluation is made possible by creation of measurable metrics.
- **Greater agility in responding to market changes** through collection, analysis and presentation of information in a timely and actionable manner.
- **Improved compliance management** by creation of monitors and triggers which would aid in early detection of deviations.

Contd. on Page 137

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IFRS 5 Non-current Assets Held for Sale and Discontinued Operations-A Closer Look

K.S.Muthupandian*

The International Financial Reporting Standard 5 (IFRS 5) was issued as one of the outputs of a short-term project being undertaken by the International Accounting Standards Board (IASB) and the United States Financial Accounting Standards Board (FASB). In September 2002, the project was added to the IASB agenda. On 24 July 2003, the IASB issued the Exposure Draft ED 4 *Disposal of Non-current Assets and Presentation of Discontinued Operations*. Then on 31 March 2004 the IASB published IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

IFRS 5 arises from the IASB's consideration of the FASB's Statement of Financial Accounting Standards No. 144 (SFAS 144) *Accounting for the Impairment or Disposal of Long-Lived Assets* with the objective of reducing differences between IFRS and US Generally Accepted Accounting Principles (GAAP) that are capable of resolution in a relatively short time. IFRS 5 achieves substantial convergence with the requirements of SFAS 144 with respect to the timing of the classification of operations as discontinued operations and the presentation of such operations. With respect to long-lived assets that are not being disposed of, the impairment recognition and measurement standards in SFAS 144 are significantly different from those in IAS 36 *Impairment of Assets*. However those differences have not been addressed in the short-term convergence project.

Objective

The objective of IFRS 5 is to specify the accounting requirements for non-current assets that are held for sale, and the presentation and disclosure of discontinued operations. IFRS 5 supersedes IAS 35 *Discontinuing Operations.*

In particular, the objectives of IFRS 5 are to specify that:

(a) assets that meet the criteria to be classified as held for sale to be measured at the lower of carrying amount and fair value less costs to sell, and depreciation on such assets to cease; and

(b) assets that meet the criteria to be classified as held for sale, and the assets and liabilities included within a disposal group classified as held for sale to be presented separately as a single amount either on the face of the income statement or in the notes, and the results of discontinued operations to be presented separately in the income statement.

Scope

(a) establishes a classification for non-current assets 'held for sale' using the defined terms set out in Appendix A to the IFRS 5 and the same criteria as those contained in SFAS 144.

(b) introduces the concept of a 'disposal group', being a group of assets, which an entity intends to be disposed of, by sale or otherwise, together as a group in a single transaction, and some liabilities directly associated with those assets that will be transferred in the transaction.

(c) classifies an operation as discontinued at the date the operation meets the criteria to be classified as held for sale or when the entity has disposed of the operation

d) requires assets or disposal groups that are classified as held for sale to be measured at the lower of carrying amount and the fair value less costs of sale;

e) specifies that assets classified as held for sale, or included within disposal groups classified as held for sale, should not be depreciated;

f) specifies that assets classified as held for sale, and the assets and liabilities included within disposal groups classified as held for sale, should be presented separately on the face of the balance sheet;

g) requires the results of discontinued operations to be presented separately on the face of the income statement; and

h) prohibits the retrospective classification of an operation as discontinued, when the classification criteria are not met until after the balance sheet date.

The measurement provisions of IFRS 5 apply to all non-current assets and disposal groups, except for:

*deferred tax assets (IAS 12 *Income Taxes*);

*assets arising from employee benefits (IAS 19 *Employee Benefits*);

*financial assets within the scope of IAS 39 *Financial Instruments: Recognition and Measurement*;

*non-current assets that are accounted for in accordance with the fair value model in IAS 40 *Investment Property*;

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*non-current assets that are measured at fair value less estimated point-of-sale costs in accordance with IAS 41 *Agriculture*; and

*contractual rights under insurance contracts as defined in IFRS 4 *Insurance Contracts.*

Assets held for sale

An entity classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered mainly through a sale transaction rather than through continuing usage. That is, the asset (or disposal group) is available for immediate sale in its present condition and its sale is highly probable. Sale should be expected within one year. The classification also applies to disposal groups, which are a group of assets and possibly some liabilities which an entity intends to dispose of in a single transaction.

For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset (or disposal group), and an active programme to locate a buyer and complete the plan must have been initiated. Further, the asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification, except as permitted by paragraph 9, and actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. In other words, a component of an entity will have been a cash-generating unit or a group of cash-generating units while being held for use.

An entity shall not classify as held for sale a non-current asset (or disposal group) that is to be abandoned. This is because its carrying amount will be recovered principally through continuing use.

Held for sale classification

The conditions for a non-current asset or disposal group to be classified as held for sale are as follows:

- the management must be committed to a plan to selling the assets
- an active programme to locate a buyer must be initiated
- the assets must be available for immediate sale in their present condition and its sale must be highly probable
- the asset must be currently marketed actively at a sale price that is reasonable in relation to its current fair value
- the sale should be completed, or expected to be so, within a year from the date of the classification as held for sale (subject to limited exceptions), and
- the actions required to complete the planned sale will have been made, and it is unlikely that the plan will be significantly changed or withdrawn.

The assets need to be disposed of through sale. Therefore, operations that are expected to be wound down or abandoned would not meet the definition (but may be classified as discontinued once abandoned). It is possible that the sale may not be completed within one year, but the delay effectively must be caused by events beyond the entity's control and the entity must still be committed to selling the asset.

A non-current asset (or disposal group) should be re-measured in accordance with the applicable IFRS immediately before it is reclassified as held for sale. Gains and losses on re-measurement are recognised in accordance with the relevant standard.

Non-current assets or disposal groups that are classified as held for sale should not be depreciated.

Subsidiaries Held for Disposal

IFRS 5 applies to accounting for an investment in a subsidiary for which control is intended to be temporary because the subsidiary was acquired and is held exclusively with a view to its subsequent disposal in the near future. For such a subsidiary, if it is highly probable that the sale will be completed within 12 months then the parent should account for its investment in the subsidiary under IFRS 5 as an asset held for sale, rather than consolidate it under IAS 27 *Consolidated and Separate Financial Statements*.

However, IAS 27 still requires that if a subsidiary that had previously been consolidated is now being held for sale, the parent must continue to consolidate such a subsidiary until it is actually disposed of. It is not excluded from consolidation and reported as an asset held for sale under IFRS 5.

Measurement of non-current assets which are held for sale

The following principles apply:

At the time of classification as held for sale. Immediately before the initial classification of a non-current asset (disposal group) as held for sale, the carrying amount of the asset will be measured in accordance with applicable IFRSs. Resulting adjustments are also recognised in accordance with applicable IFRSs.

After classification as held for sale. When a non-current asset (or disposal group) are classified as held for sale, they are measured at the lower of the carrying amount and fair value less cost to sell. If the sale is expected to occur in over a year's time, the entity should measure the cost to sell at its present value, and any increase due to the unwinding of the discount is charged to profit or loss.

Impairment. Impairment must be

considered both at the time of classification as held for sale and subsequently:

At the time of classification as held for sale. Immediately prior to classifying an asset (or disposal group) as held for sale, measure and recognise impairment in accordance with the applicable IFRSs (generally IAS 16 *Property, Plant and Equipment*, IAS 36, IAS 38 *Intangible Assets*, and IAS 39). Any impairment loss on write-down of the asset (or disposal group) to fair value less costs to sell is recognised in profit or loss unless the asset had been measured at revalued amount under IAS 16 or IAS 38, in which case the impairment is treated as a revaluation decrease. Any gain on subsequent increase in fair value less costs to sell is also recognised in profit or loss, but not in excess of the cumulative impairment loss already recognised on the asset either in accordance with IFRS 5 or IAS 36.

After classification as held for sale. Calculate any impairment loss based on the difference between the adjusted carrying amounts of the asset/ disposal group and fair value less costs to sell. Any impairment loss that arises by using the measurement principles in IFRS 5 must be recognised in profit or loss, even for assets previously carried at revalued amounts.

Assets carried at fair value prior to initial classification. For such assets, the requirement to deduct costs to sell from fair value will result in an immediate charge to profit or loss.

Subsequent increases in fair value. A gain for any subsequent increase in fair value less costs to sell of an asset can be recognised in the profit or loss to the extent that it is not in excess of the cumulative impairment loss that has been recognised in accordance with IFRS 5 or previously in accordance with IAS 36.

Disclosure – non-current assets held for sale

The key disclosure requirements include:

Non-current assets classified as held for sale and the assets of a disposal group classified as held for sale must be disclosed separately from other assets in the balance sheet.

The liabilities of a disposal group classified as held for sale must also be disclosed separately from other liabilities in the balance sheet.

Analysis of the major classes of assets and liabilities that is classified as held for sale must be disclosed on the face of the balance sheet or in the notes.

Gain or loss arising on reclassification or subsequent measurement of a non-current asset classified as held for sale.

There are also several other additional discloses required, including a description of the non-current assets of a disposal group classified as held for sale and the reason for reclassification, a description of the facts and circumstances surrounding the sale, and the expected manner and timing of that disposal.

Definition of a Discontinued Operation

The definition of a discontinued operation is very much the same as the definition of a discontinuing operation in IAS 35. IFRS 5 states that a discontinued operation is considered as a component of an entity that either has been disposed of or is classified as held for sale, and

*represents a separate major line of business or geographical area of operations,

*is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations, or

*is a subsidiary acquired exclusively with a view to resale.

It may be a subsidiary, or a major line of business or geographical area. It will have been a cash-generating unit (or group of cash-generating units) as defined in IAS 36.

An operation should be classified as discontinued at the earlier of the date that the operation has been disposed of and the date that it meets the criteria to be classified as held for sale.

Disclosures - Discontinued Operation

In addition to the income statement and cash flow statement presentations noted above, the following disclosures are required:

*Adjustments made in the current period to amounts disclosed as a discontinued operation in prior periods must be separately disclosed.

*If an entity ceases to classify a component as held for sale, the results of that component previously presented in discontinued operations must be reclassified and included in income from continuing operations for all periods presented.

The additional disclosure requirements of discontinued operations include:

*analysis of the post-tax profit or loss into revenue, expenses, pre-tax profit or loss, and the related income tax expense;

*the gain or loss recognised on re-measurement to fair value less costs to sell or on disposal, and the related income tax expense;

*net cash flows attributable to operating, investing and financing activities;

*assets held for sale separately from all other assets; and

*liabilities of a disposal group held for sale separately from all other liabilities.

Presentation - Discontinued Operation

Income statement presentation. The total of the post-tax profit or loss of the discontinued operation, and the post-tax gain or loss recognised on the

measurement to fair value less cost to sell or fair value adjustments on the disposal of the assets (or disposal group) should be presented as a single amount on the face of the income statement. Detailed disclosure of revenue, expenses, pre-tax profit or loss, and the related income tax expense is required either in the notes or on the face of the income statement. If this information is presented on the face of the income statement, then the information should be separately disclosed from that of continuing operations.Such detailed disclosures must cover both the current and all prior periods presented in the financial statements.

Cash flow statement presentation. As regards the presentation in the cash flow statement, the net cash flows attributable to the operating, investing and financing activities of the discontinued operation should be separately shown on the face of the cash flow statement or disclosed in the notes.

No retroactive classification. Retroactive classification as a discontinued operation where the discontinued criteria are met after the balance sheet date is prohibited by IFRS 5.

Key Changes from IAS 35

While IFRS 5 supersedes IAS 35, the actual amendments are limited to:

* The introduction of the term "a component of an entity", which is defined as a cash generating unit or a group of cash generating units;

*A change in the timing of the classification of an operation as discontinued. IAS 35 classified an operation as discontinuing at the earlier of (i) the entity entering into a binding sales agreement and (ii) the board of directors approving and announcing a formal disposal plan. Under the new standard, an operation shall be classified as discontinued at the date the operation meets the criteria to be classified as held for sale or when the entity has actually disposed of the operation;

*A requirement to show the results of discontinued operations separately on the face of the income statement, which is optional under IAS 35;

*A prohibition of retroactive classification of an operation as discontinued when the criteria for that classification are not met until after the balance sheet date but before the financial statements are authorised for issuance.

Effective Date and Transition

IFRS 5 is applicable prospectively for annual periods beginning on or after 1 January 2005, with earlier application encouraged provided the valuations and other information needed to apply the standard were obtained at the time that the IFRS 5 criteria were originally met. In terms of IFRS 1, a first time adopter shall apply IFRS 5 retrospectively unless transition date is prior to 1 January 2005 in which case the transitional provisions apply.

Comparison with UK GAAP

Under both FRS 3 *Reporting Financial Performance* and IFRS 5, the activities that are ending must be significant to be classed as discontinued operations. FRS 3 requires that they must have a material effect on the nature and focus of the reporting entity's operations and a material reduction in its operating facilities, whereas IFRS 5 states that the activities must represent a separate, major line of business or geographical area of operations.

The classification criteria for a discontinued operation under IFRS 5 precludes recognising an operation as discontinued where those criteria were not met at the balance sheet date. The criteria, which are the same as those for recognising any other asset as held for sale, include:

a) the asset or disposal group is available for immediate sale;

b) an active plan, supported by management, should be in place, and active steps being taken to find a buyer and conclude the sale;

c) the asset (or disposal group) should be marketed for sale at a price that is reasonable relative to its fair value, and the sale is expected to be concluded within one year at that price, although a period of more than one year does not preclude carrying the asset as available for sale provided that the events that cause the extension are outside the entity's control; and

d) if changes in circumstances mean that the classification criteria are no longer met, the entity should immediately cease to classify the asset (or disposal group) as available for sale.

Under FRS 3 operations could be recognised as discontinued if the sale or termination had been completed after the balance sheet date, but no later than three months of the balance sheet date or the date on which the financial statements were approved, whichever was the earlier. This need not be the case under IFRS 5, where the sale needs to be completed normally within one year of the asset or disposal group becoming available for resale.

FRS 3 requires full information to be given about discontinued operations (for example, turnover, costs of sales and net operating expenses) in the profit and loss account. IFRS 5 requires only the profit from discontinued operations to be shown on the face of the income statement (after profit from continuing operations), with appropriate analysis given in the notes.

There are no specific requirements in UK GAAP (FRS 15 *Tangible fixed assets*, for example) to disclose separately on the balance sheet assets held for sale, although some argue that they should be disclosed as a separate category within fixed assets. Others consider that assets no longer held for use should be reclassified as current assets or as current asset investments. If the former, the asset will be carried

at the lower of cost or net realisable and if the latter, can be carried at valuation. IFRS 5 requires the assets and liabilities to be disclosed separately: as additional lines after sub-totals of other current assets and current liabilities. Additionally, if any amounts relating to the assets have been taken direct to equity, then a separate line needs to be shown in the equity section of the balance sheet disclosing that amount.

Other key points

Entities often acquire non-current assets exclusively with a view to disposal. Such a non-current asset will be classified as held for sale at the date of the acquisition only if it is anticipated that it will be sold within the one-year period, and it is highly probable that the held for sale criteria will be met within a short period (normally three months) of the acquisition date. If the criteria for classifying a non-current asset as held for sale occur after the balance sheet date, then the non-current asset should not be shown as held for sale but disclosure of the fact should be made.

If an entity is winding up operations or 'abandoning' assets, then these assets do not meet the definition of held for sale. However, a disposal group that is to be abandoned may meet the definition of a discontinued activity. Abandonment means that the non-current asset has been used to the end of its economic life or the disposal group will be closed rather than sold. If the asset is temporarily not being used, it is not deemed to be abandoned.

Change of plans

If criteria for an asset to be classified as held for sale are no longer met, then the asset or disposal group ceases to be held for sale. In this case, it should be valued at the lower of the carrying amount before the asset or disposal group was classified as held for sale (as adjusted for any subsequent depreciation, amortisation or re-valuation), and its recoverable amount at the date of the decision not to sell. Any adjustment to the value should be shown in income from continuing operations for the period.

Conclusion

This IASB/FASB convergence initiative leads to high quality accounting solutions in accounting for assets held for sale, the timing of the recognition of discontinued operations and the presentation of those operations.❑

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- **Competitive advantage** created by gaining insight into the key drivers that affect performance, both at an organizational as well as a process level.

Challenges

Organizations have to overcome certain challenges before realizing the benefits of an effective Performance Management System. Some of the key challenges are listed below.

- **Lack of Top Management support:** The key to any system deployment activity is the 'Tone-at-the-top'. Initiatives that lack the support and involvement of the Top Management typically end up in generating little or no impact to the organization as a whole.
- **Change Management:** Deploying a Performance Management System could involve significant changes from the existing philosophies and methods of management. Procedures to effectively manage the change and create acceptance for the new system are vital.
- **Complexity:** Since enterprises are composed of several distinct entities in the form of business units, functions, processes and groups, an effective Performance Management System needs to remain relevant at the level of these entities and yet integrate into a unified system for the enterprise. Further, as Performance Management Systems need to be aligned to the specific goals of each organization, there is no 'Off-the-shelf' solution that can be easily purchased and deployed.
- **Selection of the right-fit IT tools:** IT tools that support Performance Management are available in a variety of capabilities and costs. Organizations need make careful decisions to ensure that the new tools are compatible with existing IT systems and derive the required return on investment.
- **Obsolescence:** As the business environment is rapidly evolving, the systems face the risk of obsolescence if they cannot keep pace with the changes and stay relevant.

The Bottom Line

Organizations are becoming increasingly dependant on IT systems and system-based sources of information. Management teams often find it difficult to rely on the traditional methods of reviewing reports to run the business. The success of an organization is increasingly becoming dependant on its ability to adapt and make decisions with speed. In this regard, Performance Management Systems harness the power of data and help build competitive advantage for the organization.

Projects to deploy Performance Management Systems require focused initiatives along multiple fronts. They may involve considerable investments in terms of time, effort and money. Further, careful planning and consideration of risks is absolutely vital to the success of these projects.

Nevertheless, these initiatives have the potential to yield significant long-term returns by building competitive advantage. Soon this competitive advantage may cease to be a differentiator and even evolve into a baseline requirement.❑

IFRS 6 Exploration for and Evaluation of Mineral Resources-A Closer Look

K.S.Muthupandian*

In the absence of a global accounting standard dealing specifically with extractive activities (mining and oil and gas), the International Accounting Standards Committee (IASC) published the Issues Paper *Extractive Industries* in November 2000. The International Accounting Standards Board (IASB) carried over the Project on extractive industries from its predecessor organization IASC on 1 April 2001. The IASB, on 16 January 2004, issued Exposure Draft ED 6 *Exploration for and Evaluation of Mineral Resources*. Following comments received on ED 6, IASB on 9 December 2004, issued International Financial Reporting Standard (IFRS) 6 *Exploration for and Evaluation of Mineral Resources*. IFRS 6 is shorter than many recent standards running to a mere 27 paragraphs excluding appendices.

Introducing IFRS 6, Sir David Tweedie, IASB Chairman, said: Developing a widely respected accounting standard that addresses the many complex practical and conceptual problems in the accounting for extractive activities is a concern for the IASB. However, the Board could not consider and reach an informed conclusion on all issues and viewpoints and complete its work by the 2005 deadline for the introduction of IFRSs in many jurisdictions. At the urging of some of our partner national standard-setters and other interested parties, the IASB has developed IFRS 6 to provide some initial guidance on accounting for some extractive activities without imposing significant costs on those industries in advance of completing the larger project. Although the requirements are not mandatory until 2006, entities wishing to adopt IFRS 6 early are encouraged to do so, and the standard contains special transitional provisions for that purpose."

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Objective

The publication of IFRS 6 provides, for the first time, guidance on accounting for exploration and evaluation expenditures, including the recognition of exploration and evaluation assets, and completes the first step in the IASB's project to achieve the convergence of widely varying accounting practices for extractive activities around the world. The objective of IFRS 6 is to specify the financial reporting for the exploration for and evaluation of mineral resources. The principal objective of IFRS 6 is to limit the need for entities to change their existing accounting policies for exploration and evaluation assets.

Scope

IFRS 6 applies to exploration and evaluation expenditures, i.e. to expenditures incurred by an entity in connection with the exploration for and evaluation of mineral resources (including minerals, oil, natural gas and similar non-regenerative resources) before the technical feasibility and commercial viability of extracting a mineral resource are demonstrable. Affected activities include the search for mineral resources, as well as the determination of the technical feasibility and commercial viability of extracting those resources.

The following are specifically excluded from the scope of IFRS 6:

- Expenditures incurred before the entity has obtained legal rights to explore in a specific area; and
- Expenditures incurred after the technical feasibility and commercial viability of extracting a mineral resource are demonstrable.

Definition of Exploration for and Evaluation of Mineral Resources

Exploration for and evaluation of mineral resources is the search for mineral resources, including minerals, oil, natural gas and similar non-regenerative resources after the entity has obtained legal rights to explore in a specific area, as well as the determination of the technical feasibility and commercial viability of extracting the mineral resource.

Requirements

The IFRS 6:

(a) Permits entities to develop an accounting policy for exploration and evaluation assets without specifically considering the requirements of paragraphs 11 and 12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Thus, entities adopting IFRS 6 may continue to use the accounting policies applied immediately before adopting the IFRS provided that such policies result in information that is relevant and reliable. This includes continuing to use recognition and measurement practices

that are part of those accounting policies.

(b) Requires entities recognising exploration and evaluation assets to perform an impairment test on those assets when facts and circumstances suggest that the carrying amount of the assets may exceed their recoverable amount.

(c) Varies the recognition of impairment in respect of such assets from that in IAS 36 *Impairment of Assets* but measures the impairment in accordance with IAS 36 once an impairment is identified.

(d) Requires disclosure of information that identifies and explains the amounts recognised in its financial statements arising from the exploration for and evaluation of mineral resources, including

(i) its accounting policies for exploration and evaluation expenditures including the recognition of exploration and evaluation assets.

(ii) the amounts of assets, liabilities, income and expense and operating and investing cash flows arising from the exploration for and evaluation of mineral resources.

Accounting policies

IFRS 6 is an interim standard, and is a short-term solution to the problem of accounting for the exploration and evaluation of mineral resource assets. There was a lack of guidance prior to IFRS 6, and where national standards did exist, the accounting practices were diverse, and a number were used throughout the world to account for the costs involved in exploration and extraction. These included capitalising the costs, or writing them off in the same way as research expenses.

Most of the major entities in this sector use the 'successful efforts' method, where the costs incurred in finding, acquiring, and developing reserves are capitalised on a 'field by field' basis. On discovery of a commercially-viable mineral reserve, the capitalised costs are allocated to the discovery. If a discovery is not made, the expenditure is charged as an expense. However, some companies have used the 'full cost' approach, where all costs are capitalised. Without IFRS 6, many entities would have had to change their practice of accounting for these costs. It would have forced them to fall back to the IASB Framework, or to standards issued by their respective national standard setters.

IFRS 6 makes limited changes to existing practice. This means that the fundamental principal of capitalisation of exploration costs, used by the majority of mining entities, still remains. A principal purpose of the IFRS is to specify the circumstances in which entities should test exploration and evaluation costs for impairment, and when to require disclosure of information about such assets.

The costs capitalised under the IFRS might not meet the IASB Framework definition of an asset because, for example, the capitalisation criteria followed might not require the demonstration of probable future economic benefits. IFRS 6 therefore deems these costs to be assets. Exploration and evaluation expenditure might therefore be capitalised earlier than would otherwise be the case under the IASB Framework.

Selection of Accounting Policies

IFRS 6 allows entities using quite different accounting policies to all claim adherences to the standard, effectively exempting them from applying the IASB Framework. This is similar to IFRS 4, *Insurance Contracts*. It was argued that some entities are created just to carry out exploration, and once this is complete, they sell the rights to the minerals found. If the IASB Framework or IAS 36 was applied to these entities, then no assets would ever be recognised. The IASB accepted these arguments and therefore issued IFRS 6.

A wide variety of accounting policies are followed by entities engaged in the exploration for and evaluation of mineral resources – ranging from deferring on the balance sheet nearly all exploration and evaluation expenditures, to recognising all such expenditures in profit or loss as incurred. IFRS 6 does not require or prohibit any specific accounting policies for the recognition and measurement of exploration and evaluation assets. Rather, IFRS 6 permits entities to continue to use their existing accounting policies, provided that they comply with the requirements of paragraph 10 of IAS 8 – i.e. that they result in information that is relevant to the economic decision-making needs of users, and that is reliable. An entity accounts for its exploration and evaluation expenditure either in accordance with the IASB Framework or with the exemption permitted by IFRS 6. This allows an entity to apply an accounting policy for exploration and evaluation assets which is relevant and reliable, even though the policy may not be in full compliance with the IASB Framework.

The criteria to be used to determine if a policy is relevant and reliable are set out in paragraph 10 of IAS 8. A policy must:

*be relevant to the decision-making needs of users

*provide a faithful representation

*reflect the economic substance

*be neutral (free from bias), prudent, and complete.

Paragraphs 11 and 12 of IAS 8 specify the various sources of authoritative requirements and guidance that should generally be considered in developing an accounting policy for an item if no IFRS specifically applies. There had been concern that requiring entities to apply those paragraphs when assessing their existing accounting policies for exploration and evaluation assets would highlight areas of uncertainty. To avoid the potential costs and disruption that

such uncertainties could cause, IFRS 6 grants a temporary exemption from applying paragraphs 11 and 12 of IAS 8 until the Board addresses these issues as part of a comprehensive project.

Changes in accounting policies

Entities may change their accounting policies for exploration and evaluation expenditures if the change makes the financial statements more relevant to the economic decision-making needs of users and no less reliable, or more reliable and no less relevant to those needs, judged using the criteria in IAS 8. Changes made to an entity's accounting policy for exploration and extraction assets can only be made if the result is closer to the principles of the IASB Framework.

The adoption of IFRS 6 will not generally result in changes in accounting policies for the recognition and measurement of exploration and evaluation assets. Where an entity voluntarily changes its accounting policies to improve the relevance or reliability of the financial information provided in respect of such assets, then the general principles of IAS 8 apply. Therefore, such changes in accounting policies should be applied retrospectively, unless it is impracticable to do so.

Costs which may be treated as exploration and evaluation costs

Entities must develop a policy for the capitalisation of exploration and evaluation costs and apply it consistently. IFRS 6 lists the following as examples of expenditures that might be included in the initial measurement of exploration and evaluation assets (the list is not exhaustive):

*acquisition of rights to explore; topographical, geological, geochemical and geophysical studies;

*exploratory drilling; trenching; sampling; and activities in relation to evaluating the technical feasibility and commercial viability of extracting a mineral resource.

Assets to be measured at cost at recognition

When they are first recognised in the balance sheet, exploration and evaluation assets are required to be measured at cost. The expenditures to be included in the cost of such assets are determined by the entity as a matter of accounting policy, which should be applied consistently. In making this determination, the entity should consider the degree to which the expenditures can be associated with finding specific mineral resources.

Where an entity incurs obligations for removal and restoration as a consequence of having undertaken the exploration for and evaluation of mineral resources, those obligations are recognised in accordance with the requirements of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

Subsequent measurement

Unlike the exposure draft, the IFRS 6 does not specifically exclude administration or other general costs where these costs relate directly to the exploration and evaluation activity. When first recognised in the balance sheet, exploration and evaluation assets are measured using the cost model. After original recognition, entities can apply either the cost model or the revaluation model to exploration and evaluation assets. Where the revaluation model is selected, the rules of IAS 16 *Property, Plant and Equipment* are applied to exploration and evaluation assets classified as tangible assets, and the rules of IAS 38 *Intangible Assets* are applied to those classified as intangible assets.

Both these require valuations to be based on fair value by reference to the market and thus reliable valuations may be difficult to determine. In practice, this means it will be rare for assets to be recognised at anything other than cost. There are some restrictions on the capitalisation of costs to the extent that entities can only apply IFRS 6 once they have obtained the legal right to explore a specific area and must stop applying it once technical feasibility and commercial viability have been established. Thus costs incurred before an exploration licence, or similar, has been obtained should be written off to the profit and loss account as incurred. Depreciation and amortisation is not calculated for the assets because the economic benefits that the assets represent are not consumed until the production phase.

Impairment

Where the facts and circumstances indicate that exploration and evaluation costs exceed their recoverable amount they should be tested for impairment. Indications of impairment include the period for which the entity has the right to carry out exploration activities coming to an end, costs going over budget without the additional expenditure being planned, the discontinuance of activities in an area or an indication that the capitalised costs exceed the estimated recoverable amount.

Because of the difficulty in obtaining the information necessary to estimate future cash flows from exploration and evaluation assets, IFRS 6 modifies the rules of IAS 36 as regards the circumstances in which such assets are required to be assessed for impairment. A detailed impairment test is required in two circumstances:

- when the technical feasibility and commercial viability of extracting a mineral resource become demonstrable, at which point the asset falls outside the scope of IFRS 6 and is reclassified in the financial statements; and
- when facts and circumstances suggest that the asset's carrying amount may exceed its recoverable amount.

As this type of asset does not generate cash inflows, it is tested for impairment as part of a larger group of assets. An entity should determine an

accounting policy for allocating these assets to groups of cash generating units (CGUs) and apply that policy consistently. When such circumstances, or similar circumstances, arise, the entity is required to assess the affected assets for impairment in accordance with IAS 36, subject to special requirements with respect to the level at which impairment is assessed. IFRS 6 allows a greater degree of flexibility as regards the level at which the impairment assessment should be performed. The allocation of exploration and evaluation assets to CGUs, or groups of units, for the purpose of assessing such assets for impairment can be determined as a matter of accounting policy by individual entities. The only limitation specified is that each CGU, or group of units, to which an exploration and evaluation asset is allocated for this purpose should not be larger than an operating segment determined in accordance with IFRS 8 *Operating Segments*.

IAS 36 specifies that a CGU is the smallest unit for which independent cash flows can be identified. Without this exemption, it could mean that each individual extraction unit (such as an oil rig) would be treated as a CGU. IFRS 6 therefore also gives some flexibility when defining a CGU.

Exploration and evaluation assets shall be assessed for impairment when facts and circumstances suggest that the carrying amount of an exploration and evaluation asset may exceed its recoverable amount. When facts and circumstances suggest that the carrying amount exceeds the recoverable amount, an entity shall measure, present and disclose any resulting impairment loss in accordance with IAS 36. In considering whether an asset has been impaired entities should group assets by reference to cash generating units and segmental reporting with no aggregated group of assets being larger than a segmental unit (as defined in other IAS). For example if an entity reports its assets by country it could assess impairment on a countrywide basis. However, the IFRS 6 does not preclude the use of a smaller identifiable group of assets.

IFRS 6 includes the following examples of "facts and circumstances" that may indicate that an entity should test exploration and evaluation assets for impairment (the list is not exhaustive):

- the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed;
- substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned;
- exploration for and evaluation of mineral resources in the specific area have not led to the discovery of commercially viable quantities of mineral resources, and the entity has decided to discontinue such activities in the specific area; and
- sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

Presentation

The nature of a cost should drive how an asset is classified. Recognised exploration and evaluation assets should be classified as either tangible or intangible assets under IFRS 6. Examples of assets to be classified as tangible assets are vehicles and drilling rigs. Intangible assets will include items such as drilling rights. The drilling costs would normally be treated as intangible whereas the cost of plant acquired to carry out the drilling would normally be a tangible asset.

Assets recognised in respect of licences and surveys should therefore be classified as intangible assets. Subsequent costs incurred during the exploration and evaluation phase should be capitalised in accordance with this same policy. Basically, the entity can retain the accumulated cost as an exploration asset until there is sufficient information to determine whether there will be commercial cash flows or not. However, where a tangible asset is used in carrying out exploration activities it should be depreciated with the depreciation capitalised as part of the intangible exploration cost asset (rather than merely not depreciating the asset).

Once the technical and commercial feasibility of extracting a mineral resource has been demonstrated, the assets fall outside IFRS 6 and are reclassified according to other IFRSs. Before reclassification, the assets should be tested for impairment.

Disclosure

Exploration and development costs that are capitalised are classified as non-current assets in the balance sheet, and should be separately disclosed on the face of the balance sheet and distinguished from production assets, where material. The classification as 'tangible' or 'intangible', established during the exploration phase, should be continued through to the development and production phases. Details of the amounts capitalised, and the amounts recognised as an expense from exploration, development, and production activities, should be disclosed.

Where relevant, entities are required to disclose information that identifies and explains the amounts recognised in their financial statements arising from the exploration for and evaluation of mineral resources. To comply with this requirement, the following should be disclosed:

- the entity's accounting policies for exploration and evaluation expenditures, including the recognition of exploration and evaluation assets; and

- the amounts of assets, liabilities, income and expenses and operating and investing cash flows arising from the exploration for and evaluation of mineral resources.

The amount of exploration and evaluation assets will be treated as a separate class of assets for disclosure purposes. The disclosures required by either IAS 16 or IAS 38 should be made, consistent with how the assets are classified.

The IFRS 6 notes that there has been a lack of authoritative international guidance in relation to mineral resource assets and that where national standards do exist accounting practices required by those standards are diverse.

Recognising this, the standard only makes limited changes to existing accounting practice. Consequently the requirements of the IFRS 6 do not change the fundamental principal of capitalisation of exploration costs that has been applied for many years by the majority of mining exploration companies.

Treatment of evaluation and exploration assets on acquisition

The IFRS doesn't give any further guidance on the treatment of exploration and evaluation costs on acquisition other than cross referring to IFRS 3 *Business Combinations*. This requires a lower "standard of proof" than existing UK standards for the allocation of fair values to intangible assets and suggests that, in future, the amount of goodwill on the acquisition of mineral acquisition costs will reduce.

Effective Date and Transition

IFRS 6 is effective for annual periods beginning on or after 1 January 2006, with earlier application encouraged. If an entity applies IFRS 6 for a period beginning before 1 January 2006, transitional relief is available for some comparative disclosures and that fact should be disclosed. For entities that chose to wait until 1 January 2006 to adopt the Standard, IAS 8 requires the entity to disclose that fact and, if estimable, the expected impact in the period of initial application.

First time adoption

IFRS 1 *First-time Adoption of International Financial Reporting Standards* has been amended for entities adopting IFRSs for the first time before 1 January 2006 and choosing to adopt IFRS 6 before 1 January 2006. Such entities need not present the disclosures required by IFRS 6 for comparative periods in their first IFRS financial statements. This exemption is not available for entities adopting IFRSs for the first time on or after 1 January 2006.

Otherwise, the requirements of IFRS 6 should be applied retrospectively by first-time adopters. Note that the exemption as regards recognition of impairment for comparative periods beginning before 1 January 2006 outlined in the previous section does not apply to first-time adopters. Therefore, for example, entities adopting IFRSs for the first time from 1 January 2005, and electing to adopt IFRS 6 before its effective date, should apply the impairment requirements of IFRS 6 retrospectively at the date of transition.

Post-issue Developments in IFRS 6

Amendments to the standards for first-time adopters of IFRSs and for exploration and evaluation expenditures

At its April 2005 meeting, the IASB discussed a proposed technical correction to IFRS 1 to give effect to the intent of the Board to provide relief from restating comparative information (rather than just producing comparative disclosures). After some discussion, the Board concluded that IFRS 1 did not correctly reflect the intention of the Board and that the correction should be made.

IFRS 1 provided an exemption from the requirement to provide comparative disclosures for IFRS 6 to an entity that both (a) adopts IFRSs for the first time before 1 January 2006 and (b) applies IFRS 6 before that date.

Some constituents raised a concern that the wording of the exemption did not properly convey the IASB's intention, which was to exempt such entities from the requirement to provide comparative information for IFRS 6 in the first year of application.

Given the concern, the IASB decided to amend IFRS 1 and the Basis for Conclusions on IFRS 6 to clarify that such entities are not only exempt from providing comparative disclosures, but also exempt from the recognition and measurement requirements of IFRS 6 for the comparative period.

On 2 May 2005, the IASB invited comments on a proposed small amendment to IFRS 6 and, as a consequence, an amendment to IFRS 1.

On 30 June 2005 the IASB issued amendments to IFRS 1 and the Basis for Conclusions on IFRS 6 to clarify that an entity that both (a) adopts IFRSs for the first time before 1 January 2006 and (b) applies IFRS 6 before that date is exempted not only from providing comparative prior-period disclosures but also from applying the recognition and measurement requirements of IFRS 6 in the prior comparative period.

The amendments clarify the IASB's intentions with respect to an exemption provided to first-time adopters of IFRSs who choose to adopt IFRS 6 before 1 January 2006.

Conclusion

The impact of IFRS has been felt extensively in the exploration industry. IFRS 6 is shifting the boundaries of CGUs down to the level of the petrol station or smallest group of retailing assets under IAS 36. IFRS 6 completes only the initial phase of the IASB's project on extractive activities. It seeks to increase transparency by requiring improved disclosures for exploration and evaluation assets.❑

Analysis of Onsite/ Offshore Cost Control Model for Indian IT Majors

One of the main reasons considered to be behind the immense success of Indian IT Sector companies is onsite/offshore model, which has enabled these players to provide the world class services at highly competitive prices. This paper seeks to analyze the cost structure of Indian IT majors TCS, Wipro Technologies, and Infosys to capture significant trends in quarterly analysis for financial year 2005-06 to analyse onsite/offshore cost control model for Indian IT majors. The paper also attempts to quantify the benefits of much talked about Onsite/Offshore Model. The offshore cost per person hour is found to be approximately four to five times less than that incurred at onsite.

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Introduction

Global competition in today's so called "Global Village", where companies have no boundaries to expand and operate, is forcing companies to continuously improve their operations. Worldwide competition is forcing managers to produce high-quality products and services, to provide excellent customer service, and to do so at the lowest possible cost. This new competitive environment has increased the demand of not only cost information but also of more accurate cost information. Cost information plays a vital role in reducing costs and improving efficiency.

In today's age, the importance of service sector in economic development is undisputable. The impact of service sector on the economy has increased by leaps and bounds in recent years. All over the world, the share of service sector in total economy has increased, e.g. service sector comprises approximately 54.1% of the India's GDP[1]. Also, deregulation of many services has increased competition in the service industry. Due to the intense competition in this sector, managers now need more accurate cost information for planning, controlling, continuous improvement, and decision making. Continuously growing and evolving service sector demands for relevant and innovative cost management information for CC.

Significance of Cost Analysis in Indian IT Industry

It is well recognized that service sector is growing rapidly and India has shown promising growth in this sector. Service sector, especially IT industry has played a role of growth engine in Indian economic boom. Currently, Indian IT industry (including ITES and hardware) stands at USD 28.4 billion and is expected to grow at 28 % to exceed USD 36 billion in FY 2005-06[2]. According to Strategic Review 2006 of Nasscom, IT-ITES sector is expected to contribute to 4.8 per cent of GDP in FY06. Indian IT industry has grown in an unmatched fashion, but now it is facing competition from many Asian countries, China, Singapore, Philippines to name a few.

The sharp growth of Indian IT industry is driven by Onsite/Offshore (Hybrid) Delivery Model. In this Model, the outsourcing work is distributed between the service provider's onsite center and the offshore development center. It is one of the most successful and popular outsourcing models employed today by many companies. The distribution of work depends on the type of project. Usually 20-30% of the work is done by the onsite center and the rest is done by the offshore development center.

Success of this model has attracted IT companies in other countries to adopt the model. Many multinationals arrived in India and other South Asian countries to take the advantage of low labour cost. Multinationals like Accenture, IBM too have setup offshore centers and are currently aggressively pursuing expansion in India. Now, since almost all the IT companies are trying to adopt this model, though in varying extent, to cut their costs, the competition for Indian IT companies is rising.

Facing stiff competition, Indian IT companies are also striving to cut costs. But to decide what to eliminate due to financial reasons, we need to know how much it costs. Accurate information about current costs is crucial to take business decisions related to cost control. It is important to know the costs incurred under different function to judge whether the particular function or department is being efficiently managed. Cost information about different functions enable mangers to

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make good business trade-offs. IT companies, making their best attempts to control costs, required to observe in which function a particular company is spending more than its competitors. These companies need to pay attention to strategically important function(s) having higher cost and seek how the other competitors are controlling the cost of the same function(s) efficiently.

Objectives of the Study

The study is focused on following aspects.

1) To categorize various cost components of IT majors into broad cost heads which we from now on will call as strategic cost heads.
2) To allocate and apportion individual cost heads into their respective onsite and offshore components.
3) To compute cost per person hour, overall as well as with respect to strategic cost heads along with the breakup into onsite and offshore components for cc purpose.
4) Capture the trends, if any, for last one year into above mentioned cost heads.

It is important to note that our analysis does not include BPO operations of above mentioned companies. The reason behind it is that the cost structure of IT and ITeS operations are generally quite different and moreover focus of this analysis is IT operations.

Methodology

A company mentions several cost components in its financial statements. Many times the number of these components runs into hundreds. Within a particular industry, IT being no exception, the types of costs incurred are more or less the same across companies. For top level management, it may be tedious and most of the time infeasible to keep track of such a large number of cost components. That is why the need of broad categorization of costs, specific to IT industries, was felt. Another big advantage of such categorization may be that it can facilitate the comparison across companies in a relatively easier manner. So we segregated the cost in the following broad strategic heads as mentioned in Table 1:

Quoting billing rates in terms of cost per person hour (e.g. INR per person hour) is the standard practice. It makes therefore person hour as obvious choice for cost unit. Adding margins on cost per person hour computed would give billing rate.

The basis on which onsite/offshore allocation and apportionment of various cost heads has been done is explained in table 2. For Infosys the onsite and the offshore compensation cost (for software development alone i.e., excluding Selling and General & Administrative expenses) as percentage of revenue is published. To distribute the total compensation cost into onsite and offshore components onsite/ offshore personnel cost ratio has been assumed to remain the same. In absence of any such data for TCS and Wipro Technologies, the onsite/offshore compensation cost ratio has been normalized with respect to effort (Refer to Appendix-1). It simply means that ratio of onsite compensation cost per person time to offshore compensation cost per person time has been assumed to be the same for all three companies.

The allocation of travel & conveyance cost into onsite and offshore component is rather easy. The airfare and the visa charges have been clubbed towards onsite expenses, while other travel related expenses mainly related to Selling, General & Administrative expenses have been classified into offshore component.

The allocation of vendor, IT services, occupancy and other cost towards onsite and offshore components is done on the basis of effort, i.e., the person-month data. Vendor cost is incurred due to outsourced work and therefore its allocation into onsite and offshore components is merely a symbolic exercise. The allocation of IT services costs and occupancy warrant into onsite and offshore components warrant data at the facility level. That is not available publicly. Therefore, effort, the next best basis of allocation has been adopted.

Analysis

The costs of TCS, Infosys, and Wipro under different strategic cost

Table 1: Components of Strategic cost heads

Strategic cost head	Cost components
Compensation	Salaries, health insurance, provident fund, staff welfare
Travel & conveyance	Overseas travel, visa charges, depreciation on vehicles
Vendor	Technical sub-contractors (subsidiaries or others)
IT Services	Software packages, communication, telephone, computer maintenance, depreciation on computer equipments
Occupancy	Rent, office maintenance, repairs, depreciation on plant & machinery
Others	Consumables, donations, postages etc.

[1]Ministry of Finance, http://indiabudget.nic.in/es2005-06/chapt2006/chap68.pdf

[2]Indian IT Industry Fact Sheet, http://www.nasscom.in

heads have been shown in Appendix-2. Compensation cost is the major cost of any service industry, especially knowledge based industry and IT is no exception. For all the top three Indian IT organizations, compensation cost is more than 60% of total cost. Travel cost, vendor cost, and IT services cost are some other costs which vary from 6 to 8% of total cost.

Compensation cost was found to have taken up the largest pie of total cost for all the three companies. This was expected as IT services business is human resource centered. The compensation cost, being largest, becomes the most important cost head as far as cost control is concerned. Figure 1 compares compensation cost as percentage of the total costs for the three companies. It can be observed that the compensation cost as percentage of total cost is showing decreasing trend for TCS and Wipro Technolgies. One of the reasons for this trend could be the sustained increase in offshore effort. Out of the three companies TCS has always had significantly higher onsite/offshore employee ratio. TCS seems to have focus on bringing this ratio at par with its peers (refer to Appendix-3).

A substantial decrease in the contribution of compensation cost towards total cost might be outcome of this.

As shown in Table 3, compensation cost per person hour at offshore for TCS is minimum. This is in spite of the fact that TCS has more number of experienced professionals[3]. With the lowest attrition rate among its peers, TCS has been successful in retaining employees and thus saving on the cost of hiring new employees with higher compensation. Significantly lower utilization might be contributing towards highest cost at offshore for Wipro Tech (Refer Appendix-4).

Offshore: How much beneficial?

As figures in table 4 boast of cost efficiency of Onsite/Offshore Model, the huge difference of costs between onsite and offshore justify the attempts of Indian organizations as well as multinationals to offshore as much work as possible.

Among the three companies, TCS has the lowest cost per person at onsite but at the same time, the effort at onsite is high. It means TCS has more employees at onsite but at lower cost per person. However, onsite cost per person hour of TCS went up by 15.7 % from Rs.1639 in Q1FY06 to Rs. 1896 in Q4FY06. In contrast, onsite cost per person hour for Infosys and Wipro Tech went up by just 4.3% and 2.1 % respectively.

TCS offshore cost per person hour rose by a huge 19.5 % from first to fourth quarter of FY06 in comparison to 5.5% for Wipro Tech. On the other hand, Infosys managed to contain its offshore cost very well.

As depicted in figure 2, travel cost for TCS towards onsite is quite low as compared to that for Infosys and Wipro Tech. The possible reason for this could be that in TCS average duration of employee stay at onsite is longer. Reduced turnover time would drop the airfare and visa costs substantially.

Travel cost for TCS towards onsite dipped substantially in second quarter of FY06 due to change in its policy. Effective July 1, 2005 the payments to employees deputed to the onsite were revised to include overseas allowances. As a result, employee compensation costs increased and overseas business expenditure decreased in the quarter ended September 31, 2005. Travel cost for Infosys reflected a declining trend while for Wipro and TCS, an upward trend.

IT services costs comprises of software & hardware expenses, communication expenses, depreciation on computer expenses. We have not differentiated between IT services costs for offshore and onsite as first IT services cost at onsite are generally borne by clients. Secondly costs like communication

Table 2: Bases behind cost head allocation into onsite/offshore components

Cost head	Basis of allocation & apportionment		
	Infosys	TCS	Wipro
Compensation cost	Given compensation cost onsite/offshore as %age of revenues for software development alone. Total compensation cost (incl. G&A) divided in the same ratio.	Onsite/offshore compensation cost ratio given for Infosys normalized (Appendix-1) with respect to the effort and then applied the ratio in the same way as done for Infosys.	Onsite/offshore compensation cost ratio given for Infosys normalized (Appendix- 1) with respect to the effort and then applied the ratio in the same way as done for Infosys.
Travel & conveyance	Onsite cost overseas	Onsite cost overseas	Onsite cost overseas
	travel exp + visa charges Offshore cost total	travel expenses Offshore cost total	travel expenses Offshore cost total
	travel cost - onsite cost	travel cost - onsite cost	travel cost - onsite cost
Vendor	Proportion of effort*	Proportion of effort	Proportion of effort
IT Services, Occupancy and Others	Proportion of effort	Proportion of effort	Proportion of effort

* published in operating metrics in quarterly financial results. This is usually person-month data.

expenses are for both onsite and offshore and so it can not be allocated to either side.

IT services costs per person hour (as in Table 5) reflect a typical declining trend. Again, one of the reasons for this trend might be the sustained increase in offshore effort. TCS has shown a deviation from the trend in the second quarter. This is because the software and hardware expenses for TCS have risen from Rs. 71.92 crores in Ql to extraordinarily high Rs. 168.10 crores in Q2. However, in Q3 these expenses have come back at the level of Rs. 72 crores. Since Wipro group has its own hardware business, Wipro technology seems to be in a better position to control its cost for hardware expenses. Thus, IT services costs are significantly lower for Wipro.

Vendor costs per person hour are presented in Table 6. Vendor costs per person hour for TCS and Wipro Tech. have increased significantly Q3 onwards. TCS' total vendor cost increased from Rs. 122.7 crores in Q2 to Rs. 189.51 crores in Q3. The same for Wipro Tech. increased from Rs. 90.74 crores in Q2 to Rs. 141.27 crores in Q3. Vendor costs for the three majors are expected to increase as these giants move up in value chain and outsource less value added services on a larger scale.

It is evident from figures presented in Table 7 that occupancy cost per person hour is higher for Infosys than the other two. Infosys has gone for building larger IT parks and owns furniture and fixtures etc. while other two giants depend more on rentals. This might be the reason for high depreciation on Building and Furniture & Fixtures for Infosys and hence for

[3] 51% - No of employees with more than three years of experience. Source - TCS Investors presentation January 2006.

Figure 1: Compensation Cost as percentage of total cost

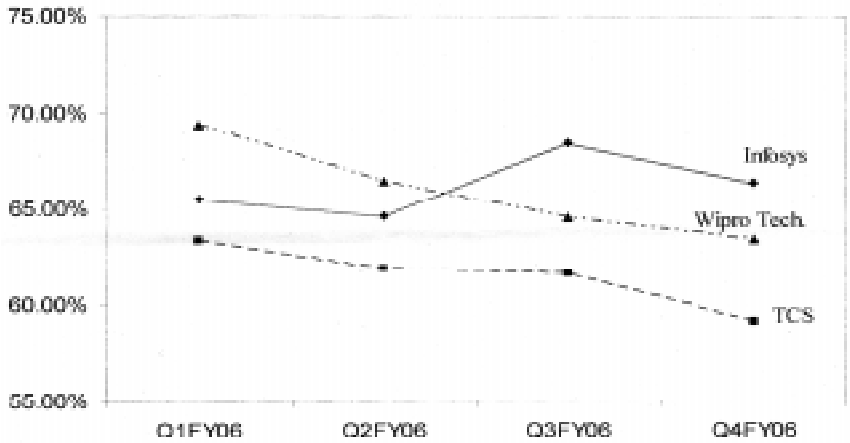


Table 3: Compensation Cost incurred per person hour-Offshore

Organization	Amount (INR)			
	Q1FY06	Q2FY06	Q3FY06	Q4FY06
TCS	158.33	165.96	164.14	168.23
Infosys	223.48	219.70	222.30	224.25
Wipro Tech.	253.84	245.37	231.95	231.57

Table 4: Total Cost incurred per person hour (INR)

Organization	Location	Q1FY06	Q2FY06	Q3FY06	Q4FY06
TCS	Onsite	1639.05	1724.82	1816.67	1896.31
	Offshore	450.73	489.31	496.05	538.68
Infosys	Onsite	2278.09	2280.68	2335.72	2376.55
	Offshore	481.01	482.37	456.63	487.42
Wipro Tech.	Onsite	2541.56	2524.04	2551.92	2595.01
	Offshore	508.60	527.59	528.43	536.21

Table 5: IT Services Cost per person hour (INR)

Organization	Q1FY06	Q2FY06	Q3FY06	Q4FY06
TCS	61.14	99.08	58.43	56.83
Infosys	67.57	63.78	59.24	62.93
Wipro Tech.	54.70	46.22	45.73	40.63

Table 6: Vendor Cost per person hour (INR)

Organization	Q1FY06	- -• — Q2FY06	Q3FY06	Q4FY06
TCS	43.84	50.62	72.32	72.54
Infosys	68.88	66.19	61.27	69.17
Wipro Tech.	56.43	67.99	92.58	92.46

higher occupancy cost. However, due to the same reason, Infosys saves a lot in rental cost.

Conclusion

Major cost in IT organizations is compensation cost (contributing more than 60% in total cost). Also, the cost incurred per person hour at onsite is almost four to five times of the cost at offshore for all the three leading Indian IT companies. For an industry with such high level of compensation cost as a percentage of total cost, low cost skilled labour force in India has been a major point of attraction for multinationals like Accenture, IBM to expand their business. With the increasing cost at offshore, the huge difference in cost at offshore and onsite (and that is the major advantage of Onsite/Offshore Model) is narrowing down but it is still lucrative enough to invest in India. The rising compensation cost at offshore and increasing competition by multinationals are some major challenges that Indian IT giants have to face in coming years.

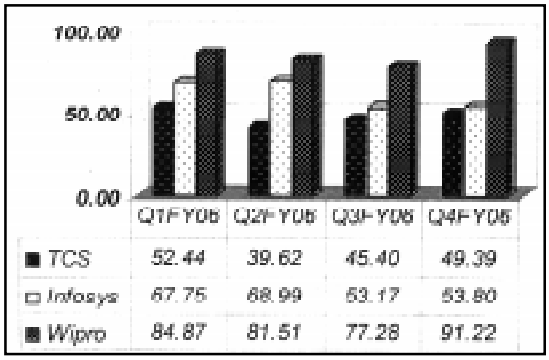
Limitations of the study

The main sources of data for the study are published financial results and investor documents available at the official websites of the companies under study. The other secondary sources of information are equity research reports. The study also involves some assumptions due to lack of data. Utilization' at onsite has been assumed to be constant 95%, same as for Wipro Technologies, across the quarters for TCS and Infosys. Onsite and offshore compensation costs as percentage of revenue (32.9% onsite and 14.9% offshore in FY06) are available for Infosys. These figures have been assumed to be valid for individual quarters as well. The ratio of onsite personnel cost to offshore personnel cost for Infosys, normalized

Table 7: Occupancy Cost per person hour (INR)

Organization	Q1FY06	Q2FY06	Q3FY06	Q4FY06
TCS	41.30	41.59	44.30	51.78
Infosys	52.08	55.66	55.19	67.25
Wipro Tech.	42.56	43.30	39.04	42.63

Figure 2: Travel Cost per person hour (INR)



Appendix 1: Onsite compensation cost for TCS

$$OnCC_{TCS} = (TCC_{TCS})\left(\frac{(OnCCR_{Infosys})\left(\frac{OnE_{TCS}}{OnE_{Infosys}}\right)}{(OnCCR_{Infosys})\left(\frac{OnE_{TCS}}{OnE_{Infosys}}\right)+(OffCCR_{Infosys})\left(\frac{OffE_{TCS}}{OffE_{Infosys}}\right)}\right)$$

Here,

OnCC	Onsite Compensation Cost
TCC	Total Compensation Cost
OnCCR	Onsite Compensation Cost as %age of Revenues
OffCCR	Offshore Compensation Cost %age of Revenues
OnE	Onsite Effort (as %age of total effort)
OffE	Offshore Effort (as %age of total effort)

Appendix 2:

a) Cost of TCS under strategic cost heads

Cost head	Amount (Rs crores)			
	Q1FY06	Q2FY06	Q3FY06	Q4FY06
Compensation cost	1214.28	1312.75	1454.66	1613.75
Travel & conveyance cost	98.82	70.96	85.63	103.76
Vendor cost	98.91	122.70	189.51	209.40
IT services cost	137.94	240.15+	153.12	164.04
Occupancy cost	93.16	100.81	116.09	149.45
Other costs*	273.16	274.46	362.55	488.29
Total	1916.27	2121.84	2361.56	2728.68

with respect to effort, is applied for TCS and Wipro Technologies. These data normalized with respect to effort are used for TCS and Wipro Technologies. This assumption can be justified on the basis that if for some company onsite cost is higher, offshore costs too should be higher. The management of any company can be expected to adopt uniform compensation policy across onsite and offshore locations. Headcount data wherever not found are calculated by linear extrapolation or interpolation.

The scope of the study is limited to quantifying some significant differences in the cost structure of companies under discussion. We do not go into finding reasons behind these differences. Based on our results, further research can be conducted to explore these reasons.

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+ Due to jump in software and hardware expenses from Rs. 71.92 crores to Rs. 1681 crores

* Include product expenses

b) Cost of Infosys under strategic cost heads

	Amount (Rs crores)			
Cost head	Q1FY06	Q2FY06	Q3FY06	QFY06
Compensation cost	913.64	1004	1140	1212
Travel & conveyance cost	108.31	123	105	112
Vendor cost	110.12	118	121	144
IT services cost	108.03	113.7	117	131
Occupancy cost	83.26	99.22	109	140
Other costs	71.22	94	73	85
Total	1394.58	1551.92	1665	1824

c) Cost of Wipro Tech. under strategic cost heads

	Amount (Rs crores)			
Cost head	Q1FY06	Q2FY06	Q3FY06	QFY06
Compensation cost	830.63	884.22	962.19	1027.22
Travel & conveyance cost	101.09	108.79	117.93	148.94
Vendor cost	67.22	90.74	141.27	150.97
IT services cost	65.16	61.68	69.78	66.34
Occupancy cost	50.69	57.79	59.57	69.60
Other costs	82.60	126.31	139.01	156.52
Total	1197.38	1329.53	1489.75	1619.59

Appendix 3: Effort distribution at offshore and onsite

Organization	Location	Q1FY06	Q2FY06	Q3FY06	Q4FY06
TCS	Onsite	33.55%	31.25%	30.68%	29.95%
	Offshore	66.45%	68.75%	69.32%	70.05%
Infosys	Onsite	21.77%	21.58%	20.56%	20.58%
	Offshore	78.23%	78.42%	79.44%	79.42%
Wipro	Onsite	24.43%	23.47%	22.13%	22.13%
	Offshore	75.57%	76.53%	77.87%	77.87%

Appendix 4: Utilization (including trainees) at offshore

Organization	**Q1FY06**	**Q2FY06**	**Q3FY06**	**Q4FY06**
TCS	**74.80%**	**L 74.97%**	**75.50%**	**75.80%**
Infosys	**74.10%**	**72.90%**	**70.00%**	**69.70%**
Wipro	**66.60%**	**65.00%**	**63.00%**	**64.80%**

Corporate Social Responsibility

Editors: Bhabatosh Banerjee, Kanika Chatterjee, Dhrubaranjan Dandapat

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Corporate Social Responsibility (CSR) is about how companies manage the business processes to produce an overall positive impact on Society. The review of this idea of CSR has been given ample exposure in the opening paper by R.P.Banerjee. However, the school of profit holds that corporate profit making in itself adds value to the resources of the society and spreads its benefit across the society. On the other hand the school of concern and empowerment (SCE) thinks that wanton pursuit of corporate profit making only looks after its own interest regardless of its harmful consequences caused to others. Then is there any conflict between CSR and business interests?

Interestingly, one opinion survey shows that majority of the respondents are either neutral or disagree that CSR will lead to lower corporate profit in the short run. Most of them agree that CSR will lead to higher corporate profit in the long run.

Today, profit, environment and social justice are the three bottom lines as envisaged by the United Nations. Harming environment and social justice ultimately harms the company.

That is why the global initiatives for introducing and standardizing CSR report by the Corporates. In this context, the author amply described various environmental issues involved and actions for implementation of the CSR.

The next paper by Tanima Roy and Amitava Sarkar seeks to establish a link between CSR and sustainable development. It also tries to show how CSR contributes to sustainable development. An economic model of social responsibility cost was also proposed that however appeared to be rather sketchy. Interesting illustrations of CSR implementation was also presented. For example, Lijjat papad, started in 1959 as an organization for poor and lower middle class women with all the workers as its shareholders increased sales to Rs. 2 crores by mid 1970. Gulson Kumar's success lay in making music cassettes affordable by all.

Kanika Chatterjee's paper on socially responsible investing (SRI) dwelt upon various aspects of SRI as an ethically driven approach. She held the opinion that SRI can impact favourably share prices by way of triggering improvement in the quality of corporate performance and its alignment with the issues of CSR – a hypothesis that needs further and regorous testing and reality check. A flow chart was given describing the relationship between corporate strategy, SRI and share prices. But can SRI serve as a reliable guiding light? There is conflict between rating organizations. For example, in 2003, Toyota was given AAA rating by Innovest Strategic Value Advisers whereas another respected rating agency Oekom gave Toyota a C rating. According to the author this may be due to different interpretations of the same phenomenon by different observers-what psychologists may call "Roshomon Effect" following Akira Kurosawa's classic film Roshomon.

While on the same subject Tanupa Chakraborty's paper traced the history of SRI that enable investors to shoulder broader social responsibility for a better future. The SRI strategies involve: screening (of including or excluding appropriate corporate securities based on ethical, social and environmental criteria), shareholders advocacy and community investing. Growth of SRI from country to country has also been mapped.

Swapan Chakraborty's paper on the logic and logistics of CSR traced the generic root of CSR and explored the conflict between economic responsibility and social responsibility. In this context, a critique of MNCs was presented, although in a very shady manner. The evils of monopoly capital and rule of MNCs is a much discussed topic. To add value to it one needs to substantiate with hard facts and figure the real impact of MNCs and alternatives available which was rather missing. However, an interesting issue was raised on the question of levying pigovian taxes vis-à-vis CSR.

In his paper on drivers and obstacle of CSR, D..Dandapat aimed at identifying the factors that motivate a company to take up CSR Programme. The drivers of such motivation include internal corporate culture and values whereas external drivers related to pressure groups from the outside society. The main obstacles are unclear boundary and communication gap, short term interest and competition from outside world etc. However, there are potential benefits like, improving financial performance, lower operating cost, enhanced brand image etc. The critical success factor lies in appropriate formulation of CSR based on relevant data and communication process and its integration in corporate strategy using sufficient flexible CSR instrument and processes. But all these may be derived from commonplace logic and we have miles to go for evolving and establishing their cause-effect relationships and their substantiation.

Malayendu Saha's paper on CSR in BRICS country (Brazil, Russia , India , China and South Africa) traced the development of CSR issues in those countries in the context of growing liberalization. In Brazil the forestry partners programmes enabled the MNCs to incorporate local stakeholders into the supply chain. Thus by providing capital

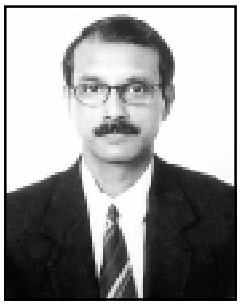
and resources farmers were enabled to raise crop and do small forestry operation at the same time. In Russia , the corporation developed their own corporate code that all suppliers must comply with. The code covered a wide range of aspects around environment. health, safety etc. In India , after liberalization a stake holder participation- based model of CSR evolved. A company is now accountable for its triple bottom line: social, environmental and financial performance rather than traditional financial performance alone. Of course, public sector units were fore- runner in discharging social responsibility. In China , due to its greater exposure to international market and increasing public expectation arising out of liberalization CSR issues are coming to the fore. The corporate governance in South Africa focuses sustainability although specifics are lacking in some aspects. A recent study shows that South African companies are global leaders in CSR reporting. Qi Chen and Mike Jones' paper on climate change and sustainability report of top 50 global energy companies is based on a checklist survey of CSR reports of those companies selected from the Platts Top 250 global energy company ranking 2006. According to their research findings bigger companies are significantly more likely to produce sustainabililty report while companies in the exploration and production industry were least likely. There was great inter company variation in the standard of quality report. A rich database appended to the paper enhances the value of this publication. However, we have to wait for justifying these empirical findings with a reliable cause-effect relationship model.

Melkote K. Shivaswamy & Bhabatosh Banerjee's paper compares CSR reporting in USA with India . The US sample consists of: Coca Cola, General Electric (GE) and UPS (United Parcel Services) while Indian sample consists of 10 companies including Gujarat Ambuja, Hindalco, Infosys, L&T, Nestles, Ranbaxy, Reliance Industries, Reliance Petroleum, Satyam and Tata Chemicals. In the US sample Coca-cola has a formalized and structured reporting system committed to fair treatment of its associates throughout the world. UPS report gives detailed focus on economic, social and environmental impact using its key performance indicators. GE's report uses G3 reporting principles of balance, comparatabililty, accuracy and reliability, materiality. It also constituted a stakeholders' review panel for comments and review before publication of the report. The CSR reports of Indian companies have been compared with reference to various aspects like healthcare, environment, safety, education and other initiatives.

The last paper by Ashish Kumar Sana makes an assessment of NTPC in the context of CSR policy. NTPC's CSR focuses on four important areas: environmental protection, ash utilization, community development and energy conservation. It pursues environment management system, ISO 14001 and occupational health and safety system (OHSAS) 18001. All NTPC units are certified for ISO 14001 and OHSAS 18001. Detailed description and fund allocation were provided for environmental protection and ash utilization, resettlement and rehabilitation, community development programme and energy conservation.

CSR is still an evolving issue – a burning issue today and many of its core areas belong to the domain of Cost & Management Accountants. The present publication provides rich knowledge resource and background information on the subject. Although the treatment is mainly descriptive and leaves many grey areas and domains of fuzziness, in times to come, it is hoped that greater standardization in CSR reporting will evolve with distinct models and guidelines for churning social meaning out of the torrents of numbers and words presented in the voluminous CSR Reports.

AT THE HELM



Mr. T. K. Gupta M.Com, FICWA, became Director Accounts in Damodar Valley Corporation, on 25.9.06. Mr. Gupta has become Chairman, Bokaro Power Supply Corporation Limited (BPSCL), a JV of DVC and SAIL w.e.f. 5th February 2008.

Mr. T. K. Gupta is a very Sr. fellow member of the Institute of Cost & Works Accountants of India. He has graduated from St. Xavier's College in Kolkata. He has done his masters from Kolkata University. All through he had a bright academic career.

He has got a very rich experience in his professional carrier spreadover 30 years as he has served in various sectors and in the Companies of national and international repute. In the early part of his carrier he had served in General Electric. Latter on he had moved on to Companies like TELCO, SAIL, Coal India and Hindusthan Cables.

While serving at TELCO, he was also a Professor of repute at the XLRI, Jamshedpur. Prior to joining in DVC, his present organization, he was Dy. General Manager in Hindusthan Cables, Kolkata. He was attached to the Rupnarayanpur chapter of ICWAI where he served as faculty.

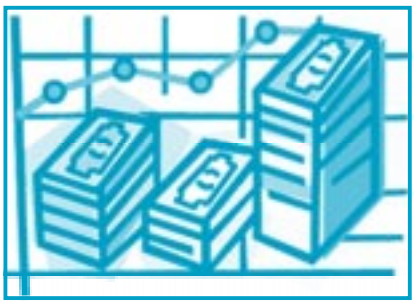
On joining DVC, Mr. Gupta like a true professional and role model is leaving his mark in the areas of Strategic Management decisions which is helping DVC to gain new heights and to face the challenges of competition.

TAX PROPOSALS

- Tax to GDP ratio that was 9.2 per cent in 2003-04, set to rise to 12.5 per cent at the end of 2007-08.
- Set to achieve the Budget Estimates of indirect taxes and exceed the Budget Estimates of direct taxes.

Indirect Taxes

Customs duties



- No change in the peak rate of customs duty.
- Customs duty on Project Imports to reduce from 7.5 per cent to 5 per cent; 4 per cent special CVD to be imposed on a few specified projects in the power sector.
- Customs duty being reduced on steel melting scrap and aluminium scrap from 5 per cent to nil.
- Customs duty to be reduced from 10 per cent to 5 per cent on certain specified life saving drugs and on the bulk drugs used for the manufacture of such drugs. They are also being exempted from excise duty or countervailing duty.
- Customs duty is being reduced on vitamin premixes and mineral mixtures from 30 per cent to 20 per cent and on phosphoric acid from 7.5 per cent to 5 per cent to reduce cost of manufacture of dairy and poultry feeds
- Customs duty being reduced on bactofuges from 7.5 per cent to nil for the benefit of dairy industry and to increase shelf life of milk
- Specified parts of set top boxes and specified raw materials for use in the IT/electronic hardware industry to be exempted from customs duty.
- Customs duty on convergence products to be reduced from 10 per cent to 5 per cent to establish parity between devices used in the information/ communication sector and the entertainment sector
- Customs duty being reduced on specified machinery from 7.5 per cent to 5 per cent to provide fillip to the manufacture of sports goods; duty also being exempted on specified raw materials for sports goods.
- Customs duty to be exempted on rough cubic zirconia and being reduced on polished cubic zirconia from 10 per cent to 5 per cent, in order to encourage value addition and exports by gem and jewellery industry; Customs duty on rough coral being reduced from 10 per cent to 5 per cent.
- Customs duty removed on helicopter simulators to facilitate training of helicopter pilots
- Customs duty reduced on crude and unrefined sulphur from 5 per cent to 2 per cent, in order to support domestic fertiliser production
- Customs duty exemption is proposed to be withdrawn on naphtha for use in the manufacture of polymers in order to correct price distortions and revenue losses. Naphtha for use in the manufacture of polymers will be subjected to normal rate of 5 per cent. Naphtha imported for the production of fertilisers will continue to be exempt from import duty.
- Export duty on chrome being increased from Rs.2,000 per metric tonne to Rs.3,000 per metric tonne in order to conserve and make it available for value added manufacture in India.

Excise duty

- General CENVAT rate on all goods reduced from 16 per cent to 14 per cent to give a stimulus to the manufacturing sector.
- Excise duty on all goods produced in the pharmaceutical sector reduced from 16 per cent to 8 per cent.
- Excise duty reduced on buses and their chassis from 16 per cent to 12 per cent.
- Excise duty reduced on small cars from 16 per cent to 12 per cent and on hybrid cars from 24 per cent to the general revised rate of 14 per cent.
- Excise duty reduced on two wheelers and three wheelers from 16 per cent to 12 per cent.

- Excise duty to be reduced on paper, paper board and articles made therefrom manufactured out of non-conventional raw materials by units not having an attached bamboo/ wood pulp making plant from 12 per cent to 8 per cent with a further reduction on clearances up to 3,500 MT from 8 per cent to nil. Excise duty on certain varieties of writing, printing and packing paper is to be reduced from 12 per cent to 8 per cent.
- Excise duty is to be reduced from

16 per cent to nil on a few mass consumption items including composting machines, wireless data cards, packaged coconut water, tea and coffee mixes, and puffed rice.

- Excise duty reduction from 16 per cent to 8 per cent on a few more items including water purification devices, veneers and flush doors, sterile dressing pads etc,. specified packaging material and breakfast cereals.
- Anti AIDS drug, Atazanavir, as well as bulk drugs for its manufacture are to be exempted from excise duty.
- Excise duty being exempted on end-use basis, on refrigeration equipment (consisting of compressor, condenser units, evaporator, etc) above 2 TR (tonne refrigeration) utilising power of 50 KW and above.
- Excise duty rates on bulk cement and packaged cement brought on par; bulk cement to attract excise duty of Rs.400 per Metric Tonne or 14 per cent ad valorem, whichever is higher; cement clinkers excise duty at Rs.450 per Metric Tonne.
- Excise duty being increased on packaged software from 8 per cent to 12 per cent, bringing at par with customised software attracting a service tax of 12 per cent.
- Excise duty on both filter and non-filter cigarettes brought on par by applying higher rates on non-filter cigarettes.
- Ad valorem part of the excise duty on unbranded petrol and unbranded diesel being abolished and replaced by an equivalent specific duty of Rs.1.35 per litre; there will be only a specific duty of Rs.14.35 per litre on unbranded petrol and Rs.4.60 per litre on unbranded diesel; there will be no impact on retail prices.
- NCCD of 1 per cent removed on polyester filament yarn and the levy shifted to cellular mobile phones.

Service tax

- Four services brought under service tax net namely, asset management service provided under ULIP, services provided by stock/ commodity exchanges and clearing houses; right to use goods, in cases where VAT is not payable; and customised software, to bring it on par with packaged software and other IT services.
- Threshold limit of exemption for small service providers increased from Rs.8 lakhs per year to Rs.10 lakh per year; about 65,000 small service providers go out of the tax net.

Direct Taxes

- Threshold limit of exemption from personal income tax in the case of all assesses increased to Rs.150,000. The slabs and rates of tax are :

Up to Rs.150,000	NIL
Rs.150,001 to Rs.300,000	10 per cent
Rs.300,001 to Rs.500,000	20 per cent
Rs.500,001 and above	30 per cent

- In case of a woman assessee, the threshold limit increased from Rs.145,000 to Rs.180,000; for a senior citizens, the threshold limit increased from Rs.195,000 to Rs.225,000.
- No change in the corporate income tax rates.
- No change in the rate of surcharge.
- Senior Citizen Saving Scheme 2004 and the Post Office Time Deposit Account added to the basket of saving instruments under Section 80C of the Income Tax Act.
- Additional deduction of Rs.15,000 allowed under Section 80D to an individual paying medical insurance premium for his/her parent or parents.
- Income Tax Act to be amended to provide that reverse mortgage would not amount to "transfer"; and the stream of revenue received by the senior citizen would not be "income".
- Tax income arising from saplings or seedlings grown in a nursery exempted.
- Business of production of seeds and manufacture of agricultural implements added to the list of companies allowed weighted deduction of 150 per cent on any expenditure on in-house scientific research.
- Benefit of amortisation of certain preliminary expenses under Section 35D allowed to assessees in the services sector.
- Corporate debt instruments issued in demat form and listed on recognised stock exchanges exempted from TDS.
- Crèche facilities, sponsorship of an employee-sportsperson, organising sports events for employees and guest houses excluded from the purview of FBT.
- Parent company allowed to set off the dividend received from its subsidiary company against dividend distributed by the parent company; provided that the dividend received has suffered DDT and the parent company is not a subsidiary of another company.
- Insert a new sub-section (11C) in Section 80-IB to grant a five year tax holiday to hospitals located in any place outside the urban agglomerations especially in tier-2 and tier-3 towns; this window will

be open for the period April 1, 2008 to March 31, 2013.

- Five year holiday from income tax being granted to two, three or four star hotels established in specified districts having UNESCO-declared 'World Heritage Sites'; the hotel should be constructed and start functioning during the period April 1, 2008 to March 31, 2013.
- Coir Board included in Section 10(29A) and exempted from income tax.
- Rate of tax on short term capital gains under Section 111A & Section 115AD increased to 15 per cent.
- STT paid to be treated like any other deductible expenditure against business income; Levy of STT, in the case of options to be only on premium, where the option is not exercised; liability to be on the seller; where the option is exercised, levy to be on the settlement price and the liability on the buyer; no change in the present rates.
- Commodities Transaction Tax (CTT) to be introduced on the same lines as STT on options and futures.
- Law being amended to exclude entities carrying on regular trade, commerce or business or providing services in relation to any trade, commerce or business and earning incomes from claiming that their purposes also fall under "charitable purpose"; Genuine charitable organisations not to be affected in any way.
- Banking Cash Transaction Tax (BCTT) being withdrawn with effect from April 1, 2009.

CST and a Roadmap towards GST

- Central Sales Tax rate being reduced from 3 per cent to 2 per cent from April 1, 2008.
- Roadmap for Goods and Service Tax being prepared for introduction of GST from April 1, 2010.

(In Crore of Rupees)

	2006-2007 Actuals	2007-2008 Budget Estimates	2007-2008 Revised Estimates	2008-2009 Budget Estimates
1. Revenue Receipts	434387	486422	525098	602935
2. Tax Revenue (net to Centre)	351182	403872	431773	507150
3. Non-tax Revenue	83205	82550	93325	95785
4. Capital Receipts (5+6+7)$	149000	194099	184275	147949
5. Recoveries of Loans	5893	1500	4497	4497
6. Other Receipts	534	41651	36125	10165
7. Borrowings and other Liabilities$	142573	150948	143653	133287
8. Total Receipts (1+4)$	583387	680521	709373	750884
9. Non-plan Expenditure	413527	475421	501849	507498
10. On Revenue Account of which,	372191	383546	412975	448352
11. Interest Payments	150272	158995	171971	190807
12. On Capital Account	41336	91875	88874	59146
13. Plan Expenditure	169860	205100	207524	243386
14. On Revenue Account	142418	174354	175611	209767
15. On Capital Account	27442	30746	31913	33619
16. Total Expenditure (9+13)	583387	680521	709373	750884
17. Revenue Expenditure (10+14)	514609	557900	588586	658119
18. Capital Expenditure (12+15)	68778	122621	120787	92765
19. Revenue Deficit (17-1)	80222 (1.9)	71478 (1.5)	63488 (1.4)	55184 (1.0)
20. Fiscal Deficit {16-(1+5+6)}	142573 (3.5)	150948 (3.3)	143653 (3.1)	133287 (2.5
21. Primary Deficit (20-11)	-7699 - (0.2)	-8047 - (0.2)	-28318 - (0.6)	-57520 - (1.1)

* GDP for BE 2008-2009 has been projected at Rs.5303770 crore assuming 13% growth over the advance estimate of 2007-2008 (Rs.4693602 crore) released by CSO.

$ Does not include receipts in respect of Market Stabilization Scheme, which will remain in the cash balance of the Central Government and will not be used for expenditure.

Extracts from the Highlights of Central Plan 2008-2009

Rural Development

National Rural Employment Guarantee Scheme

- 16000 for providing 100 days of wage employment to each rural household opting for it.

Swaranjayanti Gram Swarozgar Yojana

- 2150 for establishing a large number of micro-enterprises in rural areas. Activity clusters and group approach are the two key components of the programme. At least 50% of the Swarozgaris will be SCs/STs, 40% women and 3% disabled.

Pradhan Mantri Gram Sadak Yojana

- 7530 for providing connectivity to eligible unconnected rural habitations through good all-weather roads. The systematic upgradation of existing rural roads is also an essential component of the scheme.

Rural Housing

- 5400 for providing assistance to rural BPL households for construction of houses and upgradation of kutcha houses. As per Indira Awaas Yojana guidelines, the house should be allotted in the name of the female member of household or in the name of husband and wife; 60% of the total allocation is to be utilized for construction of houses for BPL families of SCs/STs.

Drinking Water Supply

Accelerated Rural Water Supply Programme

-7300 for supplementing the States in their effort to provide safe drinking water to all rural habitations.

Rural Sanitation

- 1200 for Total Sanitation Programme.

Land Resources

Integrated Watershed Management Programme

- 1825 for Centrally sponsored scheme of Integrated Watershed Management Programme.

National Land Records Modernization Programme

Agricultural and Cooperation

- 1100 for National Horticulture Mission.
- 1100 for National Food Security Mission
- 500 for Micro Irrigation.
- 644 for National Agriculture Insurance Scheme (NAIS).
- 299 for Technology Mission on Horticulture in NE Region, Jammu & Kashmir and Uttarkhand.
- 320 for Integrated Oilseeds, Oil Palm, Pulses & Maize Development Scheme.

Animal Husbandry, Dairying and Fisheries

- 130 for Livestock Census.
- 160 for Special package for farming population in 31 suicide prone districts in the country.
- 75 for National Fisheries Development Board.

Agricultural Research and Education

- 315 for research issues in Crop Sciences.
- 350 for Agricultural Education to Improve the quality of human resource, upgrade infrastructure and educational reforms.
- 281 for Agricultural Extension Programmes to disseminate frontline technologies.
- 257 for National Agricultural Innovation Project.
- 45 for Fisheries research and quality fish seed.

Environment and Forests

- 599 for Ecology & Environment.
- 751 for Forestry and Wild life.

School Education and Literacy

- 13100 for Sarva Shiksha Abhiyan.
- 8000 for National Programme of Mid-Day Meals in schools.

Higher Education

- 3440 for University Grants Commission-includes an allocation of Rs. 875 crore for implementation of the recommendations of Oversight Committee.
- 3205 for Technical Education, including Rs. 1647 crore for implementation of the recommendations of Oversight Committee.
- 502 for National Mission on Information and Communication

Women & Child Development

- 6330 for Integrated Child Development Services (ICDS).
- 200 for Integrated Child Protection Scheme (ICPS)
- 200 for Swayamsidha-Women's empowerment Programme.

Information Technology

- 400 for National Informatics Centre.
- 800 for e-Governance programme.
- 100 for establishing the National Knowledge Network.
- 45 for Manpower Development initiatives.
- 33 for Cyber Security.

Telecommunications

- 170 for OFC based Network for Defence Services.
- 158 for C-DoT (including Telecom testing and security certification Centre).

Health

- 11930 for National Rural Health Mission
- 3650 for Health Sector

Science and Technology

- 415 for Multi Disciplinary Research in frontier areas.
- 145 for National Mission on Nano-Science and Nano Technology.
- 100 for Drugs and Pharmaceuticals Research.
- 85 for Scholarships for Science in Higher Education.

Biotechnology

- 235 for Autonomous R&D institutions.
- 315 for Research and Development
- 45 for Grand Challenge Programmes.

Space

- 435 for PSLV & GSLV operational projects.
- 350 for INSAT System
- 350 for Special Indigenisation/ Advance ordering.
- 270 for Navigational Satellite System.
- 270 for Geo-synchronous Satellite Launch Vehicle (GSLV) Mark-III Development.
- 125 for Manned Mission Initiatives/ Human Space Flight.
- 78 for Indian Lunar Mission Chandrayaan-1 & 2.

Earth Science

- 364 for improving weather and monsoon forecast.
- 36 for strengthening Polar Science activities.
- 20 for development of Technology to harness ocean resources.

Chemicals and Petro-Chemicals

- 100 for establishment of a Petrochemical Gas Cracker Complex at Lapetkata, Dibrugarh (Assam).
- 35 for establishment of 6 new NIPERs.

Heavy Industry

- 125 for setting up a world-class automotive testing and homologation facilities in India.
- 78 to UP Paper Mill Project, a subsidiary of Hindustan Paper Corporation Ltd., for manufacture of paper.

Fertilizers

- 119.02 lakh tonnes of Nitrogenous fertilizer production targetted.
- 41.68 lakh tonnes of phosphatic fertilizer production targetted.

Coal and Lignites

- 496.84 million tonnes of domestic viability of coal has been assessed .
- 21.5 million tonnes of lignite production targetted.

Steel

- 15.73 million tonnes of saleable steel production by SAIL and RINL targetted.
- 28 million tonnes of Iron Ore production by National Mineral Development Corporation targetted.

Railways

- 20900 Rolling stock wagons, 3928 coaches; 490 locos to be added.
- 3750 kilometers of track renewal; 700 route kilometers of electrification; 2150 route kilometers of gauge conversion.
- 350 kilometers new lines to be added; 1000 Kilometers doubling of lines targeted.

Annual Economic Suvery 2007-08

Per capita income and consumption

1.2 Growth is of interest not for its own sake but for the improvement in public welfare that it brings about. Economic growth, and in particular the growth in per capita income, is a broad quantitative indicator of the progress made in improving public welfare. Per capita consumption is another quantitative indicator that is useful for judging welfare improvement. It is therefore appropriate to start by looking at the changes in real (i.e. at constant prices) per capita income and consumption.

1.3 The pace of economic improvement has moved up considerably during the last five years (including 2007-08). The rate of growth of per capita income as measured by per capita GDP at market prices (constant 1999-2000 prices) grew by an annual average rate of 3.1 per cent during the 12-year period, 1980-81 to 1991-92. It accelerated marginally to 3.7 per cent per annum during the next 11 years, 1992-93 to 2002-03. Since then there has been a sharp acceleration in the growth of per capita income, almost doubling to an average of 7.2 per cent per annum (2003-04 to 2007-08). This means that average income would now

double in a decade, well within one generation, instead of after a generation (two decades). The growth rate of per capita income in 2007-08 is projected to be 7.2 per cent, the same as the average of the five years to the current year.

1.4 Per capita private final consumption expenditure has increased in line with per capita income. The growth of per capita consumption accelerated from an average of 2.2 per cent per year during the 12 years from 1980-81 to 1991-92 to 2.6 per cent per year during the next 11 years following the reforms of the 1990s. The growth rate has almost doubled to 5.1 per cent per year during the subsequent five years from 2003-04 to 2007-08, with the current year's growth expected to be 5.3 per cent, marginally higher than the five-year average. The average growth of consumption is slower than the average growth of income, primarily because of rising saving rates, though rising tax collection rates can also widen the gap (during some periods). Year to year changes in consumption also suggest that the rise in consumption is a more gradual and steady process, as any sharp changes in income tend to get adjusted in the saving rate.

Economic growth

1.5 GDP at current market prices is projected at Rs. 46,93,602 crore in 2007-08 by the Central Statistical Organisation (CSO) in its advance estimates (AE) of Gross Domestic Product. Thus, in the current fiscal year, the size of the Indian economy at market exchange rate will cross US$ 1 trillion. At the nominal exchange rate (average of April-December 2007) GDP is projected to be US$ 1.16 trillion in 2007-08. Per capita income at nominal exchange rate is estimated at US$ 1,021. According to the World Bank system of classification of countries as low income, middle income and high income, India is still in the category of low income countries.

Table 1.2

Per capita income and consumption (in 1999-2000 prices)

	Income		Consumption	
	Rs.	Growth(%)	Rs.	Growth(%)
IX plan avg.	19245	3.4	12392	3.0
X plan avg.	24156	6.2	14677	4.3
2002-03	20996	2.2	13352	1.1
2003-04	22413	6.8	13918	4.2
2004-05	23890	6.6	14413	3.6
2005-06	25696	7.6	15422	7.0
2006-07	27784	8.1	16279	5.6
2007-08	29786	7.2	17145	5.3

Income is taken as GDP at market prices.
Consumption is PFCE.
Per capita is obtained by dividing these by population

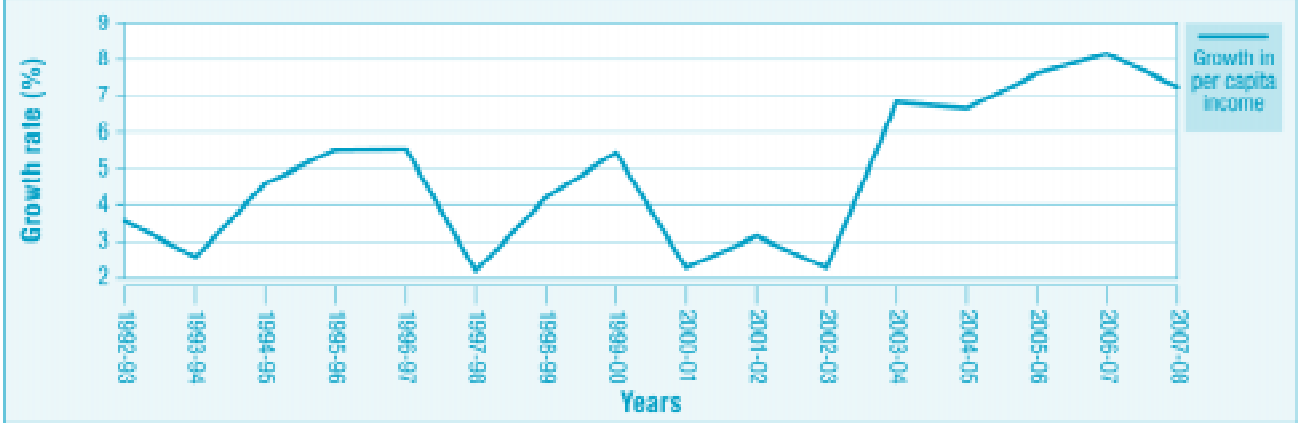
1.6 The (per capita) GDP at purchasing power parity is conceptually a better indicator of the relative size of the economy than the (per capita) GDP at market exchange rates. There are, however, practical difficulties in deriving GDP at PPP, and we now have two different estimates of the PPP conversion factor for 2005. India's GDP at PPP is estimated at US$ 5.16 trillion or US$ 3.19 trillion depending on whether the old or new conversion factor is used. In the former case, India is the third largest economy in the world after the United States and China, while in the latter it is the fifth largest (behind Japan and Germany).

1.7 GDP at factor cost at constant 1999-2000 prices is projected by the CSO to grow at 8.7 per cent in 2007-08. This represents a deceleration from the unexpectedly high growth of 9.4 per cent and 9.6 per cent, respectively, in the previous two years. With the economy modernizing, globalizing and growing rapidly, some degree of cyclical fluctuation is to be expected. This was taken into account while setting the Eleventh Five Year Plan (2007-08 to 2011-12) growth target of 9 per cent (both in the approach paper and in the NDC approved plan). Given the over 9 per cent growth in the last two years of the Tenth Five Year Plan it was argued that the Eleventh Five Year Plan target could be set at 10 to 11 per cent as 9 per cent had already been achieved. Maintaining growth rate at 9 per cent will be a challenge and raising it to two digits will be an even greater one.

Sectoral Contribution

1.8 The deceleration of growth in 2007-08 is generally spread across most of the sectors except electricity, community services and the composite

Figure 1.2 Growth in per capita income



category "trade, hotels, transport & communications". The deceleration in the growth of the agriculture sector is attributed to the slackening in the growth of *rabi* crops. Manufacturing and construction, which grew at 12 per cent in 2006-07, decelerated by about 2.5 percentage points in 2007-08. The slower growth of consumer durables (as reflected in the IIP) was the most important factor in the slowdown of manufacturing. Cement and steel, the key inputs into construction, grew by 7.4 per cent and 6.5 per cent respectively, during April-November 2007-08, down from 10.8 per cent and 11.2 per cent in the previous year.dampening the growth in the construction sector. There was also a deceleration in the growth of revenue earning freight traffic by railways, passengers handled at airports, and bank credit in April-November 2007-08, which formed the basis for the full year assessment.

1.9 Growth in 2006-07 initially estimated at 9.2 per cent in February 2007 was revised upwards to 9.4 per cent in May 2007 and further to 9.6 per cent in the Quick Estimates released by the CSO on January 31, 2008. This suggests that upward adjustments in the 2007-08 projections are possible.

1.10 The observed growth of 7.8 per cent in the Tenth Five Year Plan (2002-07), the highest so far for any plan period, is only marginally short of the target of 8 per cent. The dismal growth rate of 3.8 per cent during the first year of the plan was made up by an upsurge in growth in the next four years to an average of 8.8 per cent. A notable feature of growth during the Tenth Five Year Plan was the resurgence of manufacturing. There was a sharp acceleration in the growth of manufacturing from 3.3 per cent during the Ninth Five Year Plan to 8.6 per cent during the Tenth Five Year Plan. The average growth of manufacturing during the five years ending 2007-08 is expected to be about 9.1 per cent. The contribution of manufacturing to overall growth increased from about 9.6 per cent during the Ninth Five Year Plan to about 17.7 per cent during the Tenth Five Year Plan.

1.11 The growth in the services sector continued to be broad based. Among the subsectors of services, "transport and communication" has been the fastest growing with growth averaging 15.3 per cent per annum during the Tenth Five Year Plan period followed by "construction". The impressive progress in the telecommunication sector and higher growth in rail, road and port traffic played an important role in the growth of this sector. Besides manufacturing the two other sectors whose contribution to growth has increased over the two plans are construction and communications. The contribution of the construction sector increased to 10.8 per cent during the Tenth Five Year Plan from 7.5 per cent during the Ninth Five Year Plan, while that of telecom increased to 11.4 per cent from 6 per cent over the two plans. The growth of "financial services" comprising banking, insurance and business services, after declining to 5.6 per cent in 2003-04 bounced back to 8.7 per cent in 2004-05, 11.4 per cent in 2005-06 and 13.9 per cent in 2006-07. Manufacturing, construction and communication were the leading sectors in the acceleration of growth during the Tenth Five Year Plan, judged by their increased contribution to growth.

1.12 Agricultural growth, dependent as it is on the rnonsoon, continued to fluctuate, though the five-year period ending 2007-08 had the second lowest coefficient of variation (CV) since the five years ending 1956-57. The CV for the Tenth Five Year Plan was, however, higher than the 60- year average. The overall growth during the Tenth Five Year Plan was 2.5 per cent, the same as in the Ninth Five Year Plan. Weather induced fluctuations considerably influenced the GDP growth for agriculture. In 2002-03, the cumulative rainfall of North-East and South-West monsoon was -33 per cent and -19 per cent, respectively, of the

Table 1.3 Rate of growth of GDP at factor cost at 1999-2000 prices (per cent)

	IX plan	2002-03	2003-04	2004-05	2005-06	2006-07	X plan	2007-08
Agriculture and Allied	2.5	-7.2	10.0	0.0	5.9	3.8	2.5	2.6
Mining	4.0	8.8	3.1	8.2	4.9	5.7	6.1	3.4
Manufacturing	3.3	6.9	6.6	8.7	9.0	12.0	8.6	9.4
Electricity	4.8	4.7	4.8	7.9	4.7	6.0	5.6	7.8
Construction	7.1	7.9	12.0	16.1	16.5	12.0	12.9	9.6
Trade and hotels	7.5	6.9	10.1	7.7	9.4	8.5	8.5	12.1
Transport & communican	8.9	14.1	15.3	15.6	14.6	16.6	15.3	
Financing, real est, hsng	8.0	8.0	5.6	8.7	11.4	13.9	9.5	11.7
Community Services	7.7	3.9	5.4	6.9	7.2	6.9	6.1	7.0
GDP	5.5	3.8	8.5	7.5	9.4	9.6	7.8	8.7

Note: Plan period is simple average.

long period averages (LPA). Similarly, in 2004-05, the cumulative rainfall was -13 per cent and -11 per cent from LPA for South-West and North-East monsoon, respectively. The secular decline in the share of agriculture sector in GDP continued, with a decline from 24 per cent in 2001-02 to 17.5 per cent in 2007-08

Aggregate Demand

1.13 The most important contribution to demand growth has come from investment, while the external trade made negligible or negative contribution. The growth of GDP at market prices accelerated from 3.8 per cent in 2002-03 to 9.7 per cent in 2006-07, giving an average annual growth of 7.9 per cent for the Tenth Five Year Plan. The average rate of growth of gross capital formation during the Tenth Five Year Plan has more than tripled to 17.3 per cent per year from an average growth of 5.3 per cent per annum in the Ninth Five Year Plan. Consequently, its contribution to overall demand, as measured by the increase in GDP at market prices, tripled from 19 per cent in the Ninth Five Year Plan to 65 per cent in the Tenth Five Year Plan. The most important component of investment, namely, gross fixed investment, grew by an average of 14.3 per cent per annum during the Tenth Five Year Plan period.

1.14 The relative share of private consumption in GDP was 60.9 per cent while gross fixed capital formation had a share of 27 per cent. Though the average growth of private consumption (PFCE) accelerated somewhat to 5.9 per cent per annum from 5 per cent, its contribution to growth of demand declined from 59 per cent to 46 per cent between the two plans. The contribution of net exports of goods and services to overall demand also declined between the two plans to a negative 5 per cent.

Thus the external trade has had a dampening effect on aggregate demand during the just completed plan. Export growth, because of its spillover effects on productivity and efficiency, can, however, still act as a driver of growth.

1.15 NAS projections for 2007-08 show a deceleration in the GDP growth at market prices in line with its growth at factor cost. They also show a deceleration in the growth of consumption, both public and private, and an acceleration in the rate of growth of gross fixed capital formation. The higher growth in the gross capital formation is projected to improve its share in GDP at market prices to 32.6 per cent in 2007-08 compared to a share of 23.6 per cent in 2002-03. GDCF is projected to grow by 20 per cent and PFCE at 6.8 per cent in 2007-08, both of them above the average of the just completed plan.

Table 1.4 Growth of GDP at 1999-2000 market prices (per cent) – annual and plan average

	IX plan	2002-03	2003-04	2004-05	2005-6	2006-07	X Plan	2007-08
GDP at market prices	5.4	3.8	8.4	8.3	9.2	9.7	7.9	8.7
Consumption (Private)	5.0	2.7	5.8	5.2	8.7	7.1	5.9	6.8
Consumption (Govt)	7.9	-0.4	2.6	2.6	5.4	6.2	3.3	5.5
Gross Capital Formation	5.3	17.0	19.9	19.5	19.4	10.9	17.3	na
Gross Fixed Capital Formation	6.4	6.6	13.7	18.9	17.4	15.1	14.3	15.7
Change in stocks[a]		—	-13.4	144.0	47.7	3.9		5.1
Exports	10.7	21.8	5.8	28.1	14.8	18.9	17.9	6.4
Imports	9.6	10.4	16.8	16.0	45.6	24.5	22.7	6.4
Contribution to growth (per cent)								
Consumption (Private)	59.2	45.5	44.2	39.0	56.6	43.9	45.8	45.8
Consumption (Govt)	16.7	-1.1	3.6	3.5	6.2	6.5	3.7	6.2
Gross Capital Formation	19.4	—	59.5	65.4	64.3	37.5	65.4	na
Gross Fixed Capital Formation	25.0	40.5	38.5	56.3	51.2	45.5	46.4	55.2
Net Exports	-0.1	40.5	-17.5	22.3	-51.7	-18.2	-4.9	-3.2
Relative share (per cent)								
Consumption (Private)	64.4	63.6	62.1	60.3	60.0	58.6	60.9	57.6
Consumption (Govt)	12.3	11.7	11.1	10.5	10.2	9.8	10.7	9.5
Gross Capital Formation	24.0	25.0	27.7	30.6	33.4	33.8	30.1	na
Gross Fixed Capital Formation	22.7	23.6	24.7	27.1	29.2	30.6	27.0	32.6

[a] Change in stocks was negative during 2001-02 hence growth rate has not been calculated.

Repositioning The Management Accountant

Enterprise Governance and Cost Audit

Moving beyond Corporate Governance and reporting of resource utilization

Dhananjay V Joshi*

A. Corporate Governance (Cg) : Matter of domestic policy for many decades. Rarely described and in circulation prior to 1990s.

CG arose out of :

Incompleteness and deficiencies of traditional financial disclosures.

Non transparency of Corporate goings Leading to Corporate failures – Enron, WorldCom etc. Disaster to investors and stakeholders.

CG emerged for:

Balancing of interests of all stake holders giving rise to ideas of Audit Committees, Independent Directors, Risk Management etc.

Definition :

Narrowest sense - a formal system of accountability of corporates, Primarily to shareholders and secondarily to stake holders.

Cadbury Committee - Corporate Governance is the system by which companies are directed and controlled.

Crux of CG :

Companies to be assessed on their ability of "wealth creation", "wealth management" and "wealth sharing".

CG should get reflected in the performance of the company in terms of profits, profitability, growth, diversification, welfare, cordial industrial and other relationship at all levels.

Companies to be judged not only on "form" part of CG but also on "substance" part of CG.

CG should create credible, competent, creative, committed and caring corporate citizen.

Corporate governance is the means and corporate excellence is the end.

B. Paradigm Shift from Corporate Governance to Enterprise Governance

CG Over the time degenerated into a mere compliance procedure. Need felt for looking beyond the procedures and numbers.

CG By itself cannot make a company successful. Companies need to balance conformance with performance.

C. Enterprise Governance : (Eg)

PAIB of IFAC – IFAC Board asked PAIB to explore the emerging concept of EG.

PAIB to Focus why CG fails and what must be done.

Definition :

IFAC in collaboration with CIMA defined

"EG is 'the set of responsibilities and practices exercised by the board and executive management with the goal of providing strategic decisions, ensuring that objectives are achieved, ascertaining that risks are managed appropriately and verifying that organization's resources are used responsibly'.

Objectives.

a. providing the perenniality of the organization – includes the aspirations of all stake holders.

b. maximizing its performance – in terms of efficiency, value creation, the repartition of the richness created.

Crux of EG :

EG focuses on strategy and value creation. Heart of EG is the philosophy that CG on its own cannot make a company successful.

D Supremacy of Law

In a society governed by the Rule of Law - Law is an Instrument of Social Change.

Law, is the regulating and enhancing force that harmonizes diverse social interests, resolves conflicts and puts in place a meaningful framework for effecting social changes.

It guides us to move towards an egalitarian society and allows us to extend the benefits of socio-economic justice to all sections of society.

E. The Great Constitution of India :

Constitution is the supreme organic law which gives direction to the organs of State for Societal transformation and progress.

Social engineering by way of pro-people legislations is the paramount social philosophy of our Constitution.

Preamble to the Constitution – to secure citizens of India justice – social, economic and political.

Constitution – Chapters on fundamental rights and directive principles on state policy, delineate a framework for securing the socio-economic uplift of our people.

The Directive Principles of State Policy,

State shall strive to ensure that:-

a) the stewardship and control of the **physical resources of the community** are to be administered, converted, distributed and made available to the community at large **at the most economic and competitive prices** to sub serve the common people.

b) The operation of the economic system does not result in the

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generation and concentration of wealth and means of production to the common detriment; and

c) **economic management of physical, human, financial and managerial resources must be aimed at** and achieved with the desired managerial competence to ensure **higher productivity of the resources.**

F. Corporate Social Responsibility (Csr) :

Enterprise Governance + Business ethics - flows the concept of Corporate Social Responsibility (CSR)

Business depends for its survival & long term prosperity on society providing the resources viz. people, raw materials, services & infrastructure. It is obligatory for business to use these resources optimally for benefit of all stake holders.

Jean Jacques Rousseau writing in 1762, said that "society & corporations must co-exist & contribute to the well being of each other".

Benjamin Franklin contended that "Doing goods is not a private act between a bountiful giver & grateful receiver, it is a prudent social act."

Mahatma Gandhi advocated the "Trusteeship Concept", saying that "one holds large wealth only as a trustee of the society."

The concept has also received a lot of impetus from religion & scriptures, which emphasises responsibilities associated with wealth & success.

The famous, *Kural* , the great book of *Tiru Valluvar's* verses aptly apply to corporate citizen which says "Good men put forth industry & produce wealth, not for themselves but for the use of society."

Indian *Vedas* say "man can live individually but can survive only collectively".

Wiston Churchill said "Responsibility is the price of greatness ."

Let our corporates work towards maximum welfare of the maximum people-*"samasta Janaanaam sukhino Bhavantu"*

G SOCIAL REPORTING

Social responsibility by business enterprises leads to social reporting.

Social reporting involves :

Communicating the social & environmental effects of organizations' economic actions on society at large.

Extending the accountability of organizations beyond number crunching to all stake holders.

H. Triple Bottom Line Approach of CSR

John Ellington, noted management consultant, coined the concept of TBL in 1997.

In addition to ***profits for owners***, two more bottom lines, i.e. ***environmental & social*** need to be added.

I. Enterprise Governance for Enterprise Excellence

Ultimately the object of EG is to bring and sustain Enterprise Excellence for which Cost Audit is a very powerful tool particularly in respect of Resource Management and Reporting.

J. Enterprise Governance and Cost Audit :

Shift from CG to EG - shift in emphasis from equity and disclosure to strategy, performance and responsible utilization of resources.

Resource utilization domain – India has unique invention – Statutory Cost Audit.

The Cost Audit has been in practice since 1965 in India, since 1984 in Pakistan and in Bangladesh since 1994.

Bangladesh – C&AG carries out the audit of "performance" or "value for money" (VFM) audit of all Public Accounts.

India - 1965 Companies Act amended – Sec 233B inserted for mandatory Cost Audit

Parliamentary debate - Mrs Sathe, MP, stated that what is Cost Audit? The Cost Audit is quite different from the financial audit. It is to see whether the labour is efficient or not, whether every material and every part of the machinery is used to the optimum, whether any material is wasted? Etc.

Concept and scope of Cost Audit is much wider as it lays emphasis on the evaluation of the efficiency of the operations and utilization of resources.

Indian experience on Cost Audit fits well with the IFAC framework and India can provide a blueprint for better enterprise governance.

K. Cost Audit for Resource Management

Cost Audit in India – provides authenticated information relating to propriety and efficiency in resource utilization, waste minimization and environment friendliness in resource utilization.

Parameters included in the Cost Audit Report are :

- Process of manufacture
- Quantitative details – installed capacity, utilized capacity etc.
- Input materials consumed
- Standard Vs actual consumption of input materials
- Power, Fuel and utilities consumed.
- Standard Vs actual consumption of utilities.
- Manpower utilization
- Research & Development
- Pollution Control expenses
- Value Addition and distribution of earnings etc.
- The Cost Auditor has to suggest measures for making further improvements in the performance of the company and also offer his observations and suggestions.

Strategic Factors revealed through Cost Audit :

- Dynamics of market change vis-à-vis globalization; Market share & sustenance;
- Linkage between material costs and product pricing;
- Technology drivers & IT orientation needs;
- Competition-national & global and competitive advantages;
- Customer satisfaction & customer demands;
- Quality & Delivery – efficiency and Cost Effectiveness

- And many other decisive, strategic parameters.

Index should be developed using such norms to judge how effectively resources are utilized by the enterprise. ICWAI should carry out a research exercise and firm up the concept of the Index.

Reporting of the index called ICWAI Resource Utilisation Index and it should be made obligatory for the companies to publish this index in the Annual Report of the Company.

Before concluding I would like to add some very vital points.

Cost Accounting Standards – The Institute has taken lead in developing standards and it is likely that these standards will also get statutory recognition. However, the role of the standards should be clearly understood which is basically to being uniformity in application of and treatment of cost and revenue items in the cost accounting records. Cost Accounting Standards are supplementary in nature like Accounting Standards and they can not replace Cost Accounting Record Rules and Cost Audit.

The Committee on Subordinate Legislation (14th Loksabha) has submitted its report **recommending number of manufacturing industries and service industries in which Cost Accounting Records Rules should be framed immediately**. Thus our parliamentarians are favouring Cost Audit mechanism.

I may recall that the Institute had organized a National Seminar on "Cost Audit – A way Ahead" on 2nd February, 2007. The various stakeholders like Industry, Industry Associations. Regulatory Authorities, Govt. Departments, Banks and Financial Institutions, Consumer Associations, Investor Associations and the government representatives participated in this national seminar. It is noteworthy that **all stakeholders supported the Cost Audit which is required for better monitoring of economy, better reporting and for social cause.**

L. Resource Utilisation Index

Material	Labour	Plant facilities	Capital-Fixed	Capital – Working
Input-Output ratio	Effective hours of work	Utilisation Hours	Asset turn over ratio	NWC turnover ratio
Rejection %	Idle time	Production in terms of standard units of output	Cost of Capital	Cost of capital
	Efficiency	Idle time		
	Absenteeism	Break down time		

Mr. Krishmoorthy, member of Electricity Regulatory Authority expressed usefulness of cost audit just yesterday.

Industrialist **Mr. Ruia** expressed that "**what we are looking for is not only Cost Audit but Management Audit**" and even suggested that Management Audit should be made mandatory.

Mr. S. K. Singhal, Chairman, CBEC expressed very clearly that **Cost Audit is very much useful for Govt. Departments** and it must be continued and enlarged.

CMA Australia has also supported Cost Audit.

I appeal that the Institute should come out with an appropriate research and white paper on Cost Audit. Let us take Cost Audit to outside world. We need an approach which is "Inside Out" rather than "Outside In" approach. We should bring out How Cost Audit process has helped to regulate, to monitor for the betterment of the Industry and how it has helped India and is used in India. The message should be given to outside world about the strength of Cost Audit rather than checking what is there outside India. When Cost Audit itself is not there in operation what kind of information or research you are going to carry out outside India.

Today we are discussing "Repositioning of Management Accountant". My friends, I only make you one appeal that the Institute has already passed a resolution that you can prefix the word CMA before your name. So you are the ambassador of your own profession. When you want to reposition the Management Accountant, the first step for our 40000 members is that they should start using "CMA" to create the brand image. That itself will reposition the profession and you will be recognized as management accountants and due course of time the name change and all those things will come. This summit was an opportunity that we should have also made it clear vocally that "Yes..! The name change is very much required and it should be done." But even before the name change we must start adopting whatever is available to us in the form of prefix because in the words of great philosopher Shri. Vamanrao Pai " You are the sculpturist of your own" i.e. " Tuch Tuzya Jeevanacha Shilpkar". **Start using CMA is my humble appeal to each one of you.**

M. Concluding

Preserving, protecting and defending the resources has been part of our age old culture. Concept of 'panchbhootas" – land, water, fire, sky and air constitutes divine forces – resources.

We should attempt to find the best use of all our resources - at home and at office and in Industry and everywhere.

Mahatma Gandhi -'The earth has enough for everybody's need but not for everybody's greed.'

Last but not the least we must also keep in mind the moral right of future generations on resources and we must answer what can we leave our progeny?❑

The Micro, Small and Medium Enterprises Development Act, (MSMEDA) 2006 and Amendment to Schedule VI of the Companies Act

An exposure on Micro, Small and Medium Enterprises Development Act 2006 and the corresponding change in Sch VI of the Companies Act

L. Venkatesan*

Introduction :

The Government of India in order to encourage development of industries gave special protection to Small Scale Industry by issuing a notification under Sec 11B of the Industries (Development and Regulation) Act, 1951. Section 29B of the Act provides for notifying reservation of items for exclusive manufacture in the small scale industry sector. The Schedule VI of the Companies Act had a special provision for disclosure of amount outstanding to small scale industries. Further interest on delayed payment through small scale and ancillary industrial undertaking Act 1993 provided for timely payment and payment of interest to such undertakings. All these thing have been drastically amended with the passage of Micro, Small and Medium Enterprises Development Act 2006. This Act has been notified from 2-10-2006 (Gandhi Jayanthi day). However there has been delay in implementation by the companies as there was no corresponding amendment in Schedule VI. However Schedule VI has been amended in line with above said act with effect from 29th November 2007 (vide Notification No. G.S.R. 719(E) dated 17th Nov'07). With this amendment a lot of responsibility has been given to industry with regard to payment of Micro and Small Scale Industries within time and also payment of interest. These requirements have been made very stringent with the introduction of the above said Act and corresponding amendment in Schedule VI.

Implications of the Amendements:

MSMED ACT 2006

The definition of Small Enterprise where the investment in Plant and Machinery is more than 25 Lakhs but does not exceed Rs. 5 crores, As against the earlier limit of Rs. 1 crore. By this higher limit more and more suppliers will get included under the definition of Small Scale Industry.

In the case of enterprises engaged in providing or rendering of services, as a small enterprise, where the investment in equipment is more than ten Lakhs rupees but does no exceed two crore rupees, as against the previous limit of Rs. 10 lakhs in fixed assets, excluding land and buildings.

The increase in limits as mentioned above is an important matter for arriving at the definition of Small Scale Industry. This should be taken care of suitably while deciding the status of the supplier as per MSMED ACT 2006.

The term medium enterprise as been defined in the new Act. This does not have any implication as nowhere in the said Act such a sector gets any kind of benefits.

Provisions of sec 8 of MSMED act 2006:

As per the provisions of the above said Act, Micro, Small and Medium enterprises shall file the memorandum of micro, small or, as the case may be, of medium enterprise with such authority as may be specified by the State Government under sub-section (4) or the Central Government under sub-section (3). The form of the memorandum, the procedure of its filing and other matters incidental thereto shall be such as may be notified by the Central Government after obtaining the recommendation of the Advisory Committee in this behalf. The authority with which the memorandum shall be filed by a medium enterprise shall be such as may be specified by notification, by the Central Government. The State Government shall, by notification, specify the authority with which a micro or small enterprise may file the memorandum. A Small Scale Industry who, before the commencement of the MSMED ACT 2006 established shall file the memorandum, in accordance with the provisions of the this Act within one hundred and eighty (180) days from the commencement of this Act.

Amendement to Schedule VI:

The amendment to Schedule VI has got for reaching implications. The Micro and Small Enterprises have to fail a memorandum with the authority as may be specified by the state government or by the central government. However small scale industries that obtained Registration Certificate have time 180 days to file such memorandum.

Now one has to identify the supplier who qualifies for the definition of Micro and Small Enterprises. Companies who are holding small scale industry registration certificate earlier continue to enjoy the benefits under the New Act also subject to failing necessary memorandum within 10 days.

For all the people who come under the definition Micro Enterprises and Small Enterprises, the payment has to be effected within 15 days of acceptance or as per the credit terms, which cannot exceed 45 days. If the payment is not made as per the agreement interest has to be paid three times of the Bank rate announced by the Reserve Bank of India.

*Cost Accountant

DETAILS OF AMENDMENT:

PRIOR OT 2-10-2006	AFTER 2-10-2006
Definition as per Industrial Development Regulation Act: Small scale industrial units are those engaged in the manufacture, processing or preservation of goods and whose investment in plant and machinery (original cost) does not exceed Rs. 1 crore. These would, *inter alia*, include units engaged in mining or quarrying, servicing and repairing of machinery. In the case of ancillary units, the investment in plant and machinery (original cost) should also not exceed Rs. 1 crore to be classified under small-scale industry. The investment limit of Rs.1 crore for classification as SSI has been enhanced to Rs.5 crore in respect of certain specified items under hosiery and hand tools by the Government of India ***Definition of 'Small Scale Service & Business Enterprises' (SSSBE's)*** Industry related service and business enterprises with investment upto Rs. 10 lakhs in fixed assets, excluding land and building will be given benefits of small scale sector. For computation of value of fixed assets, the original price paid by the original owner will be considered irrespective of the price paid by subsequent owners ***SCHEDULE VI*** (i) The name(s) of small scale industrial undertaking(s) to whom the company owe any sum together with interest outstanding for more than thirty days, or to be disclosed. (ii) Total outstanding dues of small scale undertaking; and (iii) Total outstanding dues of creditors other than small scale industrial undertaking.	Definition as per MSMEDA: (a) In the case of the enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951(65 of 1951), as ➢ A micro enterprise, where the investment in plant and machinery does not exceed twenty-five lakh rupees; ➢ A small enterprise, where the investment in plant and machinery is more than twenty-five lakh rupees but does not exceed five crore rupees; or ➢ A medium enterprise, where the investment in plant and machinery is more than five crore rupees but does not exceed ten crore rupees; (b) ***In the case of enterprises engaged in providing or rendering of services, as*** ➢ A micro enterprise, where the investment in equipment does not exceed ten lakh rupees; ➢ A small enterprise, where the investment in equipment is more than ten lakh rupees but does no exceed two crore rupees; or ➢ A medium enterprise, where the investment in equipment is more than two crore rupees but does not exceed five crore rupees. ***SCHEDULE VI*** (i) Total outstanding dues of micro enterprises; and (ii) Total outstanding dues of creditors other than micro enterprises. Notes to Accounts: (a) The principal amount and the interest due thereon (to be shown separately) remaining unpaid to any supplier as at the end of the accounting year. (b) The amount of interest paid by the buyer in terms of section 16 of the Micro, Small and Medium Enterprises Development Act, 2006, (MSMEDA) along with the amount of the payment made to the supplier beyond the appointed day during each accounting year; (c) The amount of interest due and payable for the period of delay in making payment (which have been paid but beyond the appointed day during the year) but without adding the interest specified under the Micro, Small and medium Enterprises Development Act, 2006;

	(d) The amount of interest accrued and remaining unpaid at the end of each accounting year; and (e) The amount of further interest remaining due and payable even in the succeeding years, until such date when the interest dues as above are actually paid to the small enterprise, for the purpose of disallowance as a deductible expenditure under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.
Interest for delayed payments to Small Scale and Ancillary Industrial undertaking act, 1993: Interest on delayed payments to Small Scale and Ancillary Industrial Undertaking Act, 1993, it is mandatory for large companies to repay their dues to SSIs within 120 days, failing which the companies will have to pay on their outstanding a penal interest @ 1.5 times of PLR charged by State Bank of India. Section 8 of the said Act also requires a buyer of SSI products to specify the outstanding dues in its annual accounts.	**Interest for delayed payments as per msmed act, 2006:** Where any buyer fails to make payment of the amount to the supplier, as required under Section 15, the buyer shall, not with standing anything contained in any agreement between the buyer and the supplier or in any law for the time being in force, be liable to pay compound interest with monthly rests to the supplier on that amount from the appointed day or, as the case may be, from the date immediately following the date agreed upon, at three times of the bank rate notified by the Reserve Bank. Not withstanding anything contained in the Income-tax Act, 1961 (43 of 1961), the amount of interest payable or paid by any buyer, under or in accordance with the provisions of the Act, shall not, for the purposes of computation of income under the Income-tax Act, 191, be allowed as deduction.

Such interest will not qualify for Income-Tax deduction.

Some of the companies are giving in the Notes to Accounts stating they are in the process of compiling the data. Since the concept of Small Scale Industries were there earlier this kind of statement may not be correct atlest for the suppliers who are covered by the earlier definition of the Small Scale Industry the company should comply with the provisions of the Micro, Small and Medium Enterprises Development Act (MSMED), 2006.

The master data of the suppliers should contain a provision for those suppliers who are covered by this act. All the existing small scale suppliers will get qualified under the above said act. For all such suppliers a program should be run to check the following items.

1) Whether payments have been made within 45 days from the date of supply
2) If not what is the interest payable
3) Whether interest has been paid
4) What is the unpaid interest
5) Whether it has been provided in the accounts
6) If not to provide in the accounts
7) Total amount of outstanding due to Micro Enterprises and Small Enterprises.

The requirement of giving the name(s) of small scale industrial undertaking(s) to whom the company owe any sum together with interest outstanding for more than thirty days, has been dispensed with. The companies have to develop a special program to comply with this requirement. As the requirement of Micro, Small and Medium Enterprises Development Act, 2006, has now been embedded in Schedule VI, non-compliance thereof will now be required to be dealt with within the meaning of Section 211 of the Companies Act, 1956 and accordingly, dealt with in auditors report, so far as it relates to non-availability of information and presentation of accounts in the manner prescribed.

Conclusion:

With the introduction of MSMED ACT 2006 and corresponding amendment of SHEDULE VI imposes lot of responsibility on the industry to pay the micro and small enterprises (both production and service industry included) within 45 days of appointed date. If not interest as to be paid at the rate of three times the bank rate notified by the RBI with compounding such interest with montly rest. Such interest is not allowable for Income Tax purpose. Suitable additional disclosures have to be given in terms of Schedule VI

The Industrie Has Lost its Indepence Of Negotating Power of Credit Terms as Regard Micro and Small Enterprises.

Reference:

- The Micro, Small and Medium Enterprises Development Act 2006 (27 of 2006)
- Vide Notification No. G.S.R. 719(E) dated 17th Nov'07

(These are the personal views of the author who can be contacted through email at 1.venkatesan @ hotmail.com)❑

Corporate Law Updates March 2008

SEBI

CIRCULAR/PRESS RELEASE

Amendment to Securities Contracts (Regulation) Rules proposed

PRESS RELEASE, DATED 1-2-2008

Based on a review, Government has proposed to amend the Securities Contracts (Regulation) Rules, 1957 (SCRR) for both initial and continuous listing requirements of companies in stock exchanges. The amendments proposed by the Ministry of Finance are:

(a) The standards for initial listing and continued listing may be prescribed in the SCR Rules.

(b) The standards for initial and continuous listing may be uniform, as the objective is same.

(c) The public offer envisaged at initial listing is of no consequence unless the public are actually allotted shares. The SCRR may speak in terms of allotment to public, not just public offer.

(d) As of now, the word 'public' is not defined. If 'public' means 'non-promoters' and includes Fls, FIIs, MFs, employees, NRls/OCBs, private corporate bodies, etc., the floating stock would be insignificant. A view needs to be taken on this.

(e) For a company to be listed and continue to be listed, it must have a public stake of 25 per cent.

(f) If for any reason, the public holding reduces below 25 per cent, the promoters, management and company may be jointly and severally be liable to bring the public holding to 25 per cent within 3 months, in the manner prescribed by SEBI, failing which appropriate enforcement action, including delisting, may be taken.

(g) There should not be any discrimination between a Government company and non-Government company. The powers of the stock exchange to relax any of the conditions of listing with the prior approval of SEBI in respect of a Government company needs to be withdrawn. Similarly, the powers of SEBI to relax listing requirements may be withdrawn.

A large number of shares distributed among a large number of shareholders is essential for the sustenance of a continuous market for listed securities to provide liquidity to the investors and to discover fair prices. The larger the number of shares and the number of shareholders, ie., the larger the public float, the less is the scope for price manipulation. In order to ensure this, the securities laws prescribe initial and continuous listing requirements.

SEBI

CIRCULAR/PRESS NOTE

SEBI (Issue and Listing of Debt Securities) Regulations, 2008/ SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008/ SEBI (Intermediaries) Regulations, 2008/ Amendment to SEBI (Mutual Fund) Regulations, 1996

PRESS RELEASE NO. 24/2008. DATED 30-1-2008. ISSUED BY SEBI

The SEBI Board at its meeting held in Mumbai today, approved the following:

- SEBI (Issue and Listing of Debt Securities) Regulations, 2008
- SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008
- SEBI (Intermediaries) Regulations, 2008
- Amendment to SEBI (Mutual Fund) Regulations, 1996

1. SEBI (Issue and Listing of Debt Securities) Regulations, 2008

The regulations pertain to issue and listing of debt securities which are not convertible, either in whole or in part into equity instruments. They provide for a rationalized disclosure requirements and a reduction of certain onerous obligations erstwhile attached to an issue of debt securities. Regulations have been aimed at reducing time and unnecessary burden of issuance of these securities and according flexibility to issuers to structure their instruments, without diluting areas of regulatory concern. Key features of the Regulations are:

- Due diligence, proper disclosures and credit rating, the key elements of corporate debt issuances will be ensured by SEBI mainly through due diligence exercise by the merchant bankers.
- Where the equity of a company is listed, and such company wishes to issue debt instruments (whether by way of public offering or private placement), as large amount of company-related information is already in public domain and material developments are available as per the equity listing agreement on a nearly continuous basis minimal incremental disclosures are sufficient.
- Where the equity of the issuer is not listed, and such a company raises debt capital (whether by way of public offering or private placement) detailed disclosures are required.
- Offer to fifty or more persons shall require mandatory listing and specific disclosures in terms of the Regulations and a simplified listing agreement where the equity securities of such entity are listed.

2. SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008

The SCRA was amended in 2007 enabling SEBI to provide

for disclosure based regulation for public issue of or listing of securitized debt instruments on the recognized stock exchanges. Accordingly, SEBI has made regulations in this regard.

The regulations are principle based and have been made taking into account the market needs, cost of the transactions, competition policy, the professional expertise of credit-rating agencies, disclosures and obligations of the parties involved in the transaction.

Salient features of the regulations are as follows:

(a) The special purpose distinct entity (the issuer) will be a trust and the trustees thereof will require registration from SEBI. The instrument issued by the issuer to the investor shall acknowledge the beneficial interest of such investor in underlying debt or receivables assigned to the issuer. The issuer can undertake only the activities permitted by the regulations.

(b) The regulations permit securitization of both existing as well as future receivables.

(c) The regulations provide flexibility in terms of pay through/pass through structures.

(d) In case of public issuances listing will be mandatory. The instruments issued on private placement basis may also be listed subject to the compliance of simplified provisions of the regulations.

(e) Regulations require strict segregation of assets of each scheme.

3. Securities and Exchange Board of India (Intermediaries) Regulations, 2008

In the present regime a dozen regulations govern different categories of intermediaries. The broad framework of such regulations is similar to one another. The new regulations seek to consolidate the common requirements and put in place a comprehensive framework which will apply to the intermediaries and prescribe the obligations, procedure, limitations etc. insofar as the common requirements are concerned. The new regulations seek to simplify procedures to make the registration/regulation process of intermediaries less burdensome and cost effective without diluting the regulatory oversight. The regulation is primarily principle based and some significant changes in the framework are given below:

Permanent Registration

1. Subject to compliance with the SEBI Act, regulations, updation of relevant disclosures and payment of fees registration shall be permanent.

Registration for multiple activities

2. The process for registration for undertaking multiple activities by the same intermediary has been simplified.

Registration Form-information divided into two parts

3. Part I of the form will be disclosed and available to the public and Part II will contain such information which will be retained with the Board as regulatory filing.

Fit and Proper person requirements

4. The criteria to determine whether the intermediary is a Fit and Proper person have been revised and are now principle based.

Suspension/Cancellation of certificate of registration

5. The manner of suspension/cancellation of any certificate granted to any person has been provided in the regulations. Consequently the SEBI (Procedure for holding enquiry by enquiry officer and imposing penalty) Regulations, 2002 will be repealed. The procedure for suspension/ cancellation has been simplified and the time taken in this regard is sought to be reduced.

4. Amendment to SEBI (Mutual Fund) Regulations, 1996 for removal of initial issue expense in close-ended mutual fund schemes

The SEBI Board approved the proposal for removal of charging and amortization of initial issue expense in close-ended mutual fund schemes. Accordingly, henceforth, all mutual fund schemes shall meet the sales, marketing and other such expenses connected with sales and distribution of schemes from the entry load. Consequently, waiver of load for direct applicants will also be available in close-ended schemes.

This would bring in more transparency and better upfront disclosures to the investors in terms of the expenses charged in close-ended schemes.

Necessary amendments to the respective regulation are being issued.

INSURANCE MATTERS

RULES/REGULATIONS

Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) (Third Amendment) Regulations, 2008 - Amendment in regulation 3; insertion of Regulations 3B, 4A, 5, 6 and 7

NOTIFICATION F.NO. IRDA/REG/1/42/2008, DATED 3-1-2008, ISSUED BY

INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY

In exercise of the powers conferred by section 32C read with section 32B of the Insurance Act, 1938 (4 of 1938), the Authority, in consultation with the Insurance Advisory Committee, hereby makes the following Regulations to further amend the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) Regulations, 2002, notified on October 17, 2002 in the Gazette of India F.No. IRDA/ Reg./10/2002 and amended

on December 26, 2005 in the Gazette of India F. No. IRDA/ Reg./4/2005/37, namely:

Short title and commencement

1. (1) These regulations may be called the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) (Third Amendment) Regulations, 2008.

(2) They shall come into force on the date of their publication in the Official Gazette.

(3) In the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) Regulations, 2002,

(i) The third proviso to Regulation 3 shall stand deleted.

(ii) After Regulation 3A as inserted by the Insurance Regulatory and Development Authority (Obligation of Insurers to Rural or Social Sectors) (Amendment) Regulations, 2005, the following Regulation 3B shall be added:

"3B. Obligations after the Sixth Financial Year.-(l)(a) Rural Sector:

(i) in respect of a life insurer,

(I) eighteen per cent in the seventh financial year;

(II) nineteen per cent in the eighth and ninth financial years;

(Ill) twenty per cent in the tenth financial year, of the total policies written direct in that year;

(ii) in respect of a general insurer,

(I) five per cent in the seventh financial year;

(II) six per cent in the eighth financial year;

(Ill) seven per cent in the ninth and tenth financial years; of the total gross premium income written direct in that year.

(b) Social sector

(i) in respect of all insurers,

(I) twenty-five thousand lives in the seventh financial year;

(II) thirty-five thousand lives in the eighth financial year;

(Ill) forty-five thousand lives in the ninth financial year;

(IV) fifty-five thousand lives in the tenth financial year.

(2) The obligations of the insurers towards the rural and social sectors for the tenth financial year shall also be applicable in respect of the financial years thereafter."

(iii) After Regulation 4, the following Regulation 4A shall be added:

"4A. Obligations of the existing insurers for the financial years 2007-08 to 2009-10.-(1) The obligations of the existing insurers as on the date of the commencement of the Insurance Regulatory and Development Authority Act, 1999 towards the rural and social sectors from the financial year 2007-08 to the financial year 2009-10 are as under-

(a) Life Insurance Corporation of India,-

(i) Rural Sector,

(I) twenty-four per cent in the financial year 2007-08;

(II) twenty-five per cent in the financial years 2008-09 and 2009-10, of the total policies written direct in that year;

(ii) Social Sector,

(I) Twenty lakh lives in the financial years 2007-08,2008-09 and 2009-10.

(b) General insurers,

(i) Rural Sector,

(I) six per cent in the financial year 2007-08;

(II) seven per cent in the financial years 2008-09 and 2009-10, of the total gross premium income written direct in that year;

(i) Social Sector,

(I) for the financial year 2007-08 the average of the number of lives covered by the respective insurer in the social sector from the financial years 2002-03 to 2004-05 or 5.50 lakh lives, whichever is higher;

(II) for the financial year 2008-09, the obligations of the existing insurers shall increase by 10 per cent over the number of persons prescribed for the financial year 2007-08;

(Ill) for the financial year 2009-10, the obligations of the existing insurers shall increase by 10 per cent over the number of persons prescribed for the financial year 2008-09.

(2) The obligations of the insurers, towards the rural and the social sectors for the financial year 2009-10 shall also be applicable in the financial years thereafter:

(iv) After regulation 4A, the following regulations 5, 6 and 7 shall be added:

"5. Notes applicable to regulations 3, 3A, 3B, 4 and 4A.-(1) The term 'lives' referred to in regulations 3, 3A, 3B and 4A in respect of all insurers refers to human lives insured as at the end of each financial year.

(2) Re-insurance premium shall not be included while calculating the obligations of the insurers in respect of the rural and social sectors.

(3) The Authority may prescribe or revise the obligations as specified in these Regulations, from time to time.

6. Compliance.-{1) For the purpose of these Regulations, compliance with the obligations towards the rural sector in respect of both general and life companies shall be based on the sale of products conforming to the proviso that all such contracts meet the stipulation as to the minimum amount of cover as laid down in Schedules I and II of the Insurance Regulatory and Development Authority (Micro Insurance) Regulations, 2005.

(2) For the purpose of these Regulations, compliance with the obligations towards the social sector in respect of both

general and life companies shall be based on the sale of products conforming to the proviso that all such contracts meet the stipulations as to the cover laid down in Schedules I and II of Insurance Regulatory and Development Authority (Micro Insurance) Regulations, 2005.

7. Submission of returns.-Every insurer shall submit a return, as part of the financial returns to be submitted under the Insurance Regulatory and Development Authority (Preparation of Financial Statements and Auditors Report of Insurance Companies) Regulations, 2002, the rural and social sector obligations specified under these regulations and disclose the level of compliance achieved during the said year. Such reporting shall form part of the 'Notes to the Accounts."

SEBI

Circular/Press Note

'Art Funds' Covered by Collective Investment Scheme

PRESS RELEASE NO. 44/2008, DATED 13-2-2008, ISSUED BY SEBI

This message is issued by SEBI in the interest of investors with regard to their investments in Art Funds, funds / schemes launched by companies or any entity formed for the purpose. From the analysis of the characteristics of 'art funds' these are 'collective investment schemes' as defined under section 11AA(2) of the SEBI Act, 1992. The schemes/ funds have been launched/floated by these entities without obtaining a certificate of registration in accordance with the SEBI (Collective Investment Schemes) Regulations, 1999 (the Regulations).

In terms of section 12(IB) of the SEBI Act, 1992, no "person" shall sponsor or cause to be sponsored or cause to be carried on a collective investment scheme unless he obtains a certificate of registration from the Board in accordance with the regulations.

Regulation 3 of the Regulations permits only a 'Collective Investment Management Company' having certificate of registration from Board to launch collective investment scheme. Thus, only a company which has been granted certificate of registration by the Board in accordance with the Regulations can launch or sponsor a collective investment scheme. In .other words, for a collective investment scheme to raise money from the public it is pre-requisite that the entity must (a) be a company and (b) registered with SEBI as a Collective Investment Management Company.

Therefore, the launching/floating of the 'art funds' or schemes without obtaining a certificate of registration from the Board in terms of the provisions of the Regulations amounts to violation of the provisions of section 12 read with sections 11 and 11AA of the SEBI Act and the Regulations. For such violations, appropriate actions, civil and criminal, under the SEBI Act may be taken by SEBI against such funds/ companies.

INSURANCE MATTERS

RULES/REGULATIONS

Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) (Fourth Amendment) Regulations, 2008 - Amendment in Regulation 3

NOTIFICATION F. NO. IRDA/REG. 2/13/2008, DATED 25-1-2008, ISSUED BY

INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY

In exercise of the powers conferred by section 32C read with section 32B of the Insurance Act, 1938 (4 of 1938), the Authority, in consultation with the Insurance Advisory Committee, hereby makes the following Regulations to further amend the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) Regulations, 2002, notified on October 17, 2002 in the Gazette of India F. No. IRDA/ Reg./10/2002, amended on July 30, 2004 in the Gazette of India F. No. IRDA/Reg./3/ 2004, December 26, 2005 in the Gazette of India F. No. IRDA/Reg./4/2005/37; and January 3, 2008 in the Gazette of India F. No. IRDA/Reg./l/42/2008, namely:

Short title and commencement

1. (1) These regulations may be called the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) (Fourth Amendment) Regulations, 2008.

(2) They shall come into force on the date of their publication in the Official Gazette.

(3) In the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural or Social Sectors) Regulations, 2002.

The first proviso to Regulation 3 shall be deleted and replaced to read as under:

'Provided that in cases where an insurance company commences operations in the second half of the financial year and is in operations for less than six months as at 31st March of the relevant financial year, (i) no rural or social sector obligations shall be applicable for the said period, and (ii) the annual obligations as indicated in the Regulations shall be reckoned from the next financial year which shall be considered as the first year of operations for the purpose of compliance. In cases where an insurance company commences operations in the first half of the financial year, the applicable obligations for the first year shall be 50 per cent of the obligations as specified in these Regulations'.

Appraisal of Financial Performance of Urban Cooperative Banks - A Case Study

The main purpose of this study is to identify and analyze the trends, progress and problems of urban cooperative bank.

Dr. Uttam Kumar Dutta*
Amit Basak**

Backdrop :

Cooperative movement owes its origin to England, where a great philosopher. Robert Owen (1771-1858) gave the idea of" self help through mutual help[1] to mitigate the sufferings *of* the exploited class of the society. The first ever effort towards the formation of a cooperative organization has made by 28 flannel weavers, at Rochdale near Manchester in England in 1844.Urban cooperative movement of global horizon lasted the sweet of success following success of Urban Credit Institutions between 1855 and 1885, organized by Herman Schulze and Luigi Luzzatti of Germany and Italy respectively. Similarly, the origin of urban credit movement in India dates back to 5[ln]. Frbruary, 1889 when under guidance of Shri Vilhal Laxman Kavthekar, a Mutual Aid Society was formed by some middle class Maharastrian families in Baroda State. The cooperative movement in India gained momentum with the establishment of the Cooperative Credit Society Act. 1904 After the enactment of this act Primary Cooperative Credit Societies were set up in the urban areas called the I Than Cooperative Banks(UCBs) with the objective of promoting sustainable banking practices among the lower and middle income strata of the urban population

Urban cooperative banks are one of the vital segments oi the banking industry of the country. They essentially cater to the credit needs of person;, of smalt means. There were 1872 urban cooperative banks in the country at the end of March M, 2005. The figures were 1106 in 1966, the year in winch they were brought under the purview of Banking Regulation Act ,1949. Deposits and advances of UCBs increased sharply from Rs.153 crore and Rs.87 crore respectively in 1966 to Rs. 105017 crore and Rs.66905 crore. The Gross NPA of Urban Cooperative Banks at the end of March,2005 stood at Rs. 15409 crore. which is 23 % of total loans and advances. Statistical distribution of UCBs shows that around 80% of UCBs are concentrated in 5 stales viz.Maharastra, Gujrat, Karnataka, Andhra Pradesh and Tamil Nadu.

On the other hand, at the end of March,2005. there were 5 i UCBs in West Bengal with total deposits of Rs. I 741 crore and total loans and advances of Rs.987 crore. 29 and, 12 banks are considered as Grade \ and 11 categories while 10 banks are classified as Grade II! and IV banks(previousiy known as Weak & Sick). None of UCBs in West Bengal falls under the category of scheduled banks.

Though some UCBs have shown credible performance in die recent years, a large number of banks have shown discernible signs of weakness. The operational efficiency is unsatisfactory and characterized by low profitability, ever growing non performing assets (NPA) and relatively low capital base. Over a long period of time, the performance of UCBs has been deteriorating due to non recovery of interest and instalment of loan portfolio. Probably the biggest challenge facing the banking sector, especially the UCBs, is the availability of quality assets. In case banks arc unable to generate income due to NPAs, it will put the banks into liquidity crunch. Major concerns suffering this sector include high levels of loan delinquency . erosion of capital base, paucity of funds for fresh deployment, ineffective credit planning . lack of professionalism in conduct and management, deficiency in application of computerized system, lack of HRD policies, poor management information system etc. In this context, the paper makes an attempt to examine the working and financial performance of the urban cooperative banks To make our analysis lucid and representative we have considered workings of Nabapally Cooperative Bank Ltd. Barasat, West Bengal as a case study.

The paper is divided into six sections . In section 1 and II backdrop and objectives of the study have been chalked out. Section III contains the data and methodology; Section IV deals with the profile of the bank; The analysis and interpretations are presented in section V and in Section VI a few suggestions for improvement of the efficiencies and effectiveness in the operation of the bank are given.

II. Objectives of the Study :

The main purpose of this study is to identify and analyze the trends, progress and problems of urban cooperative bank. To achieve the main purpose and to give direction to the study the following objectives are set forth :

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** Lecturer , Deptt. of Commerce , Susil Kar College, W.B.

(i) To analyze the performance of the bank in mobilizing deposits.

(ii) To identify the tends in the volume and direction of credit advanced by the bank.

(iii) To identify the problem of swelling NPAs and to examine whether the bank has taken the initiative for keeping NPA under control and reduce NPA to She expected level so that the bank does not fall into lower category,

(iv) To evaluate the performance of the bank in terms of profit earned,

(v) To find out ways and means for improving the efficiency and effectiveness in the operation of the bank.

III. Data and Methodology :

The present study is based on secondary data and other information provided by the bank in its published annual reports. The relevant data have been colleted from the published annual report of the bank for the period from 1995-96 to 2004-05. The data collected tire analyzed with the help of the statistical tools like ratios, percentages, averages and trend analysis.

IV. The Nabapally Cooperative Bank Ltd. (NCB) - a profile.

The Nabapally Cooperative bank Ltd., Nabapally was registered on 17". April, 1962 (Regd.No. 1 16/24 Pgs) and started its function on and from 6th. May. 1962. The bank had come under the purview of the B.R. Act 1949 on 2002 , as it obtained permanent license for carrying on banking business from RBI on 25.1 1.2002. The bank has no branch.

It was established with a working capital of Rs.800 and in the first year it earned profit of Rs.186. The area of operation of the bank is confined to ward no. 1 to 5 and 19 to 30 of Barasat Municipality and Nilgunge and Khilkapur Gram Panchayet of Barasat Police Station of North 24-Parganas District of West Bengal state. The management of the bank is vested upon a Board of Directors consisting of 9 Directors elected from amongst 33 elected delegates and there is also one staff representative in the Board. . There are 15 employees at present working at the bank.

The membership of the bank has increased from 4772 from 1995-96 to 6678 in2004-05, which showed an increase of 39.94% during last 10 year period. At the same time the paid up share capital of the bank has increased from Rs.9.70 lakhs to 50.15 lakhs showing an increase of 417% during this period. The profit of the bank increased sharply from Rs.7.88 lakhs in 1995-96 to Rs.36.55 lakhs in 2004-05. This bank lias never suffered loss since its establishment.

V. Analysis and Interpretations

(a) Deposit Mobilization : The bank accepts deposits in the current accounts, saving bank accounts and fixed deposit accounts.. Total deposits of the bank increased from Rs.563.22 lakhs in 1995-96 to Rs.2056.77 lakhs in 2004-05. showing an increase of 265.18 % during this period. It registered a significant annual growth rate of 176.34 %. From table I, it is clear that the deposit mobilisation showed an increasing trend throughout the period and this is an indicator of good performance of the bank. Low cost deposit (Viz. Savings Account. Current Account etc.) of the bank were Rs.298.44 lakhs in 1995-96 and Rs.l 115.42 lakhs in 2004-05. These deposits ranged between 52.27%o and 54.23%) of total deposit of the bank during the period under study.

(b) **Loans and Advances** : Loans and advances play an important role in gross earnings and net profit of a bank and in promoting the economic development of a country. The NCB provides loans and advances for short term, medium term and long term to its members. In addition to it, net credit facilities are also provided against the cash credit limits of the cooperative societies. Further, the bank provides house building loan, transport loan, business loan, surety loan to the members.

Total outstanding loans and advances of the bank increased fromRs.125 lakhs in 1995-96 to Rs.369.10 lakhs in 2004-05, thus recorded an increase of 195.28 % during this period. The loans and advances registered annual growth rate of 23.67 % and it also showed an upward trend throughout this period. Percentage of loan and advances to the priority sector is 83.07%o and to the weaker section is 31.38%), both of which are higher than the optimum level (i.e. 60%> to priority sector, out of which 25% to weaker section). The Credit Deposit ratio of the bank ranged between 22.19%> and 17.94%) during the period under study. This ratio is very much unsatisfactory and so the bank should take initiative to improve this ratio through proper credit planning and fix up a time bound action to achieve the desired CD. ratio level of 60%) to 70%).

(c) Working Capital : The total working capital of the bank was Rs.682.13 Lakhs in 1995-96 which increased to Rs.2723.98 lakhs in 2004-05, thus recorded an increase of about 299.33 % till 2004-05 as compared to the year 1995-96. Table 1 depicts the increasing trend of working capital over the period and the growth of deposits was mainly responsible for this. The percentage of deposits to working capital remained above 64% throughout the period. The share capital, being another source of the working capital, was 9.70 lakhs in 1995-96 increased to Rs.50.15 lakhs in 2004-05, therefore, the share capital has gone by 4.17 times. Despite an increase in the share capital, its share in the working capital ranged between 1.42% to 1.84% . On the other hand, reserves ranged between 7.57% and 15.22% of the working capital

during the period. As the working capital is an indicator of the volume of the business of the bank, the NCB should strengthen its working capital base by increasing its deposits and owned funds.

(d) **Resource Management**: The resources mobilized in the form of share capital, deposits, borrowings must be utilized in a judicious and profitable manner, as it is an important aspect of resource management by a banking institution. The Cash Reserves Ratio(CRR) and Statutory Liquid Reserve (SLR) maintained by the bank (as a % of Net Demand and Time Liabilities or NDTL) during the last 10 years are given below:

From Table -III, it is clear that the bank did not default in maintenance of CRR/SLR during the last 10 years. But it maintained the cash reserve and liquid assets much above the statutory requirement! under the banking Regulation Act) which is fixed up 3% and 25% of NTDL respectively. So. proper care should be taken to avoid such surplus maintenance of both CRR/ SLR to utilize the idle fund for more productive purpose.

(e) NPA Management- Recovery of loans and Advances : The ability of a bank in serving as an active channel of credit is largely determined b\ its recover) of loans, otherwise there will be a stagnation in the credit How. The main reason for this is the mounting overdues which are clogging the process of credit recycling. Concept of

TABLE-III

Year	CRR	SIR
1995-96	4.49%	25.56%
1996-97	3.20%	25.70%
1997-98	3.20%	25.72%o
1 998-99	3.03%	25.60%
1999-00	3.13%	'0.12%
2000-01	3.43%	3 1.22%
2001-02	3.46%	28.45%
2002-03	5.75%	43.73%
2003-04	4.26%	43.52%
2004-05	3.24%	43.87%

TABLE -I
Financial position of the Nabapally Cooperative Bank Ltd.
For the period from 1995-96 to 2004-05 (Rs. in lakh)

Year	Share capital	Reserve & other Fund	Working capital	Deposits	Loan & advances	Net profit
1995-96	9.70	51.68	682.13	563.22	125.00	7.88
1996-97	11.12	66.18	856.43	703.49	153.00	8.50
1997-98	12.71	104.73	1018.31	890.13	1 74.00	43.61
1998-99	15.58	128.73	1230.22	1081.89	184.00	30.45
1999-00	18.92	191.36	1642.79	1311.30	198.68	39.38
2000-01	22.70	134.63	1958.23	1438.57	229.94	*M).},* 3
2001-02	29.25	224.80	2001.23	1716.25	262.67	47.12
2002-03	41.48	332.77	2220.25	1861.40	277.44	39.34
2003-04	46.58	363.71	2605.62	1955.98	285.29	29.30
2004-05	50.15	414.72	2723.98	2056.77	369.10	36.55

(Source : Annual Report of the Nabapally Cooperative Bank Ltd.)

TABLE-II
Table showing the trend value of different financial parameters
(Rs. in lakhs other than C/D ratio)

Year	Trend value of Deposits	Trend value of loan & Advances	Trend value of working capital	trend value of Net profit	C/D Ratio
1995-96	564.37	119.40	623.23	19.70	**ii j 9**
1996-97	740.71	143.07	861.16	22.26	.22.^{7}4
1997-98	917.05	166.74	1099.09	24.82	.19.55
1998-99	1093.39	190.41	1337.02	27.38	.17.01
1999-00	1269.73	214.08	1574.95	29.94	.15.00
2000-01	1446.07	237.75	1812.88	32.50	.16.00
2001-02	1622.41	261.42	2050.81	35.06	.15.30
2002-03	1798.75	285.09	2288.74	37.62	.14.90
2003-04	1975.09	308.76	2526.67	40.18	.14.58
2004-05	2151.43	332.43	2764.60	42.74	.17.94

(Source : compiled from the Annual Report of the Nabapally Cooperative Bank Ltd.)

Non-Performing Assets came into existence with the recommendations of Narsimham Committee implemented by RBI in 1992. The most dominant area of improvement in the profitability of banks continues to be reduction of NPAs. No other problem in the banking sector, especially UCBs, is as serious as the NPA problem. An asset becomes non-performing when it ceases to generate income for the bank.

Earlier an asset was considered NPA based on the concept of "Past Due" (i.e. due date + 30 days) but with effect from 31.03.2001. this concept of past due was dispensed with and NPA is advance which is overdue for more than 1 80 days. With a view to moving towards international best practices and to ensure greater transparency, it has been decided to adopt the 90 days overdue norm for identification of NPA from the year ending 31.03.2004.

In the light of this concept, the position of NPAs of NCB are analyzed..

(i) Trends of Cross NPAs : Table - IV shows a comparative stud) of NPAs of the NCB during the period from 2000-01 to 2004-05. The quantum of NPA has been mounting up during the period. The gross NPAs increased from Rs.30.06 lakhs in 2000-01 to Rs. 55.49 lakhs in 2004-05. showing an increase of 84.60% during this live year period.

The ratio of gross NPAs to total loans and advances gone up from 13.07% in 2000-01 to 15% in 2004-05. showing an decreasing trend in 2001-02. then increasing in 2002-03 by 87.39% and thereafter a slight decrease in 2003-04. So the ratio of gross NPAs of the bank shows a fluctuating trend

throughout the period. In 2001-02. the ratio of Cross NPA of the bank(i.e. 10.08%) was at the lowest point, in the next year it has reached its peak (i.e. 17.88%>).The percentage of gross NPAs to total loans and advances was 14.7%) on an average throughout the last five years. On the other hand, in case of net NPAs it depicts negative figure for each of the year under study. Thus the bank maintains adequate provision for NPAs. But it is pertinent to mention thai the Gross NPAs is the better indicator than the net NPA of the quality of loan portfolio, since it does not incorporate the endogenous provisioning response.

(ii) Analysis of Loan Assets : The Problem of swelling NPAs may be belter understood from the classification of loan assets . According to the Prudential Norms all performing loan assets are classified as " Standard Assets' but non-performing loan assets are classified as " Sub-Standard', "Doubtful' and " Loss Assets'. A sub-standard asset is an asset which has remained as a NPA for a period not exceeding 2 years. In case of Doubtful, it remains NPA for a period exceeding 2 years. On the other hand, a Loss Asset is one where the loss has been identified by the bank or internal or external auditor or under RBI inspection, but the amount has not been written off wholly or partly.

Table V represents that the quantum of standard assets in absolute term increased from Rs. 199.88 lakhs in 2000-01 to Rs.3 13.62 lakhs in 2004-05. But the share (or percentage) of standard assets to total loans and advances decreased from86.93% to 84.96%) during the period. This dwindle trend in percentage indicates the inefficiency of the bank in respect of NPA management. So far as the doubtful assets are concerned, it increased from26.67 lakhs in 2000-01 to Rs.29.88 lakhs in 2004-05.

Sub-standard assets increased from Rs. 1.98 lakhs in 2000-01 to Rs.23.59 lakhs in 2004-05, showing slight increase in 2001-02. then reached the peak point amounting to Rs.23.59 lakhs in 2004-05. Bus the serious concern is that the volume of loss assets has been mounting up. which have ultimately eaten up its profit. The loss assets increased from Rs.1.41 lakhs in 2000-01 toRs.2.02 in 2004-05.

TABLE-IV
Gross NPA and Net NPA of the NCB Period : 2000-01 to 2004-05
(Rs. in lakhs)

Item	2000-01	2001-02	2002-03	2003-04	2004-05 369.11
Gross advance(a)	229.94	262.67	277.44	285.84	
Gross NPAs (b)	30.06	26.48	49.62	50.05	55.49
Gross NPA as % of Gross Advances	13.07%	10.08%	i 7.88%	17.51%	15.03%
Total NPA provision held(including BDDR)©	50.77	68.33	77.02	83.68	89.1 8
Gross NPA as % of working capital	*nJ3%~*	1.32%	2.23%	1.92%	2.04%
Gross NPA as % of total Assets	1.50%	1. i 5%	1.95%	1.90%	2.02%
Net Advances(a-c)	179.17	1 94.34	*t~200A2T~*	202.16	279.93
Net NPAs(b-c)	(-)20.71	(-)41.85	(-)27.4	0)33.63 .	(-)33.69
Net NPA as % of Net Advances	(-) 11.56%	(-)2i.53%	(-) 13.67%o	(-) 16.63%	(-) 12.03%

From the analysis it is apparent that increasing trend of NPAs (major portion of which consist of doubtful and loss assets) indicates the inefficiency of the bank to collect loans and advances at the initial stage of NPA. The absolute amount of NPAs continues to be a major drag on the performance of banks. So it is urgently needed to arrest this situation through improved monitoring and follow up. Some drastic step need to be taken to reduce mounting doubtful assets at best, as well as to prevent the down gradation of existing NPAs which will ultimately result into less provision and consequently much higher profit. There is , therefore, a need to bring about improvements in credit administration and management of credit risk.

(f) Profitability : Although the prirnarv object of cooperative bank is service and the profit motive is incidental, the return on capital i.e. dividend is ceiled, so that the bulk of profit is used for strengthening the owned resource.,but in the present competitive environment unless a bank earn profit it can not be survived and ultimately it falls into lower gradation. From Table-1 it is clear thai the net profit of the bank increased from Rs. 7.88 lakhs in 1995-96 to 36.55 lakhs in 2004-05. registered an increase of 363.83% during this period. It evolves a significant annual growth rate of 2.56%>. Table -11 depicts the increasing trend in profit throughout the period, which represent the good performance of bank in this respect.

VI.Suggestion :

From the above analysis it is cropping up that the bank should take-certain steps for improving its efficiency and effectiveness. The lollovving initiatives may accelerate the process :

(i) In order to improve the recovery performance the management should keep in constant contact with the borrowers at a regular interval and motivate them to make timely payment by offering rebate on interest. The bank should take the initiative for preparing **"Defaulter's List"** and affix it on the notice board of the bank and also their name should be displayed in **"Local Cable Channel".** There is an urgent need to not only reduce the NPAs but also to arrest the fall of the lower graded NPAs to the next higher level, because, as the loan descends down to a lower category the percentage share of provisions to be made on them starts increasing which ultimately eats up the profit of the bank. So more effective measures should be taken for recovery

TABLE-V
Classification of Loan Assets of the NCB : 2000-01 to 2004-05
(Rs. in lakhs)

Classification of loan assets	2000-01	2001-02	2002-03	2003-04	2004-05 Averag
(A) Standard Assets	199.88 (86.93%)	236.19 (89.92%)	227.82 (82.11%)	235.79 (82.49%)	313.62 . ! 85.3%, (84.96%)
(B)NPAs (a) Substandard	1.98 (0.86%)	2.37 (0.90%)	22.58 (8.28%)	11.15 (3.90%)	23.59 i 4.06% (6.39%)
(b) Doubtful	26.67 (1 1.6%)	20.93 (7.97%)	23.94 (8.78%)	36.40 (12.73%,)	29.88 ! 9.84% (8.09%)
© Loss assets	1.41 ((0.61%)	3.18 (1.21%)	3.10 (1.39%)	2.50 (0.87%)	2.02 1 0.92%, (0.54%)
Gross NPAs(a+b+c)	30.06	26.48	49.62	50.05	55.49
Gross Loan & Advances(A+B)	229.94	262.67	277.44	285.84	369.81
%> of Gross NPAs to loan & advances	13.07%	10.08%	17.88%	17.51%	15% J 14.7%

(Note: Figures within parentheses represents percentage of Loans & Advances)

of sticky advances and lower clown of NPAs. The strongest measures should be taken to make credit appraisal, documentation, disbursement, monitoring etc.

(ii)The bank should adopt the system of computerized monitoring of loans. It should accept effective **"'Loan Recovery Policy"** and may organize recovery camps at the problem area at a regular interval. In this respect, it may take the help of local Municipality/ Panchayat to recover overdues. But if all these efforts will not give positive result, then the bank may file civil suit against defaulting borrower through ARCS for prompt action.

(iii)The bank should be very much effective to increase its credit deposit ratio and in this respect emphasfizeji should be given on house building loan specially. Because terms and conditions of HBL is much easier and EMI is implemented like any other commercial banks. So much attention is to be given on advertisement criteria where terms and conditions and EMI of HBL should be clearly displayed. Some innovative credit schemes like Self-help Group Finance Scheme may be tried.

(iv) Thc diversification ratio of the bank was 1.90% on an average throughout the lasi 10 years. So the income other than banking activities is not significant. Therefore, the bank can increase it's income by means of receiving electricity bill. Telephone bill, LIC Premium etc. on commission basis. At the same time, it will enhance the trust of the public more .in cooperative bank also. So the management need to prepare a comprehensive perspective plan for product diversification to maintain a competitive edge in the market.

(v) Cooperative banks, with their new formed emphasis on prudential norms, need a high degree of professionalism in management. The board of directors , in the era of competitive environments need professional and forward looking attitude in taking final decision on crucial aspects of risk management, credit policy. NPA management, investment strategies, marketing plan and asset- liability management (ALM).

(vi) Two or three days work shop on regular basis should be organized for updating the knowledge. because a perfect knowledge of current market leads to better productivity. In this perspective, the bank may seek cooperation from RCSs and Federation of West Bengal Urban Cooperative banks and Credit Societies. It must concentrate on scientific development of human resource and to fix up clear cut HRD policies.

(vii)Corporate governance has great relevance in the present environment.

Cooperative banks are supposed to run on ethical values to conduct their business and their success rest on the honesty and integrity of Board members. To exercise proper control on their operations in order to safeguard depositors and other stake-holders interest, good corporate governance is the only alternative. So. the bank have to adopt corporate governance principles to strengthen (lie accountability and transparency in their operation.

(viii)In the context of LPG and banking sector reforms, the bank needs development of a fully operational computer network system for smooth functioning of the business. It may take initiative for introduction of ATM Counter in near future.

(ix) For improving its position, the bank should open branches and extension counter in Noapara. Nilgunge and Khilkapur area, so that it can expand its credit facilities by finding avenues for investment.

(x) Last but not the least, customer's satisfaction is the perquisitive of the success of a bank. The primary objective of the bank is to provide service to the customers. Always it should keep in mind its customer friendliness out look.

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Cost Competitiveness by Productive and Profitable Maintenance

In the context of productive & profitable maintenance, Total Productive Maintenance (TPM) is referred to be maintenance program which involves a newly defined concept for maintaining plants and equipment. TPM brings maintenance into focus as a necessary and vitally important part of the business. Maintenance is no longer regarded as a non-profit activity. Down time for maintenance is scheduled as a part of the manufacturing day and, in some cases, as an integral part of the manufacturing process. The purpose/goal is to hold emergency and unscheduled maintenance to a minimum.

Ganesh Gomu*

Total Productive Maintenance has its origin traced to Japan which stresses upon curtailing losses continuously thereby to remain globally competitive in the overall Industry domain in terms of manufacturing cost.

As the utility of the plant comprising many equipments are stretching beyond its useful life by continual and timely maintenance schedules, it would be worthwhile to review and initiate actions on the deviations in equipment/plant maintenance cost/performance.

In the context of productive & profitablemaintenance,Total Productive Maintenance (TPM) is referred to be maintenance program which involves a newly defined concept for maintaining plants and equipment. TPM brings maintenance into focus as a necessary and vitally important part of the business. Maintenance is no longer regarded as a non-profit activity. Down time for maintenance is scheduled as a part of the manufacturing day and, in some cases, as an integral part of the manufacturing process. The purpose/ goal is to hold emergency and unscheduled maintenance to a minimum.

Objectives of Productive & Profitable Maintenance :

- Avoid wastage in a quickly changing business environment.
- Producing goods without reducing product quality.
- Reduce cost.
- Produce a desired batch quantity at the earliest possible time.
- Goods send to the customers must be non defective.
- Zero break downs
- Improving equipment efficiency rates
- Minimise costs associated with spareparts.

The process involved in TPM leads to looking at the six-big losses occurring in the plant or equipment which becomes the pre-dominant ingredient for measuring the overall equipment effectiveness.These areas have been dwelt briefly in the following paragraphs:

Six Big Losses :

In an ideal factory, equipment would operate 100 percent of the time at 100 percent capacity, with an output of 100 percent good quality.In reality , however, this is rare. The difference between the ideal and the actual situation is due to wastages and losses occurring in the plant. The losses are categorized into three major categories like down time,speed loss,defect loss. These losses have been elaborated briefly :

1) **Down Time Loss :** It is a time loss occurring due to machine remains standstill during its effective running time. Down time loss is categorized into two classes :

a. Equipment Failures - Equipment breakdown or failures causes loss as the machine will not be delivering any output during this period.

b. Set up and Adjustments - Substantial time spent on adjusting the machine to deliver the quality acceptable product .

2) **Speed Loss :** It is a loss occurring due to machine not operating at its maximum designed speed. Speed loss is categorized into two classes.

a. Idling and Minor Stoppage - When the machine is not running smoothly and at a stable speed,the frequent halt of the machine will reduce the effectiveness of the equipment.

b. Reduced Speed Operation - It refers to the difference between the actual operating speed and the equipment's designed speed .

3) Defect Loss : It means that the equipment is producing the product that do not fully meet the specified

Loss Category	Six Big Losses
Downtime (lost availability)	Equipment failures
	Setup and adjustments
Speed losses (lost performance)	Idling and minor stoppages
	Reduced speed operation
Defect losses (lost quality)	Scrap and rework
	Startup losses

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quality characteristics. Defect Loss is categorized into two classes:

a. Scrap and rework- This loss occurs when products do not meet quality specifications, even if they can be reworked to correct the problem.
b. Startup Losses - These are yield losses that occur when production is not immediately stable at equipment startup, so the first product do not meet specifications. It is a latent loss and inevitable.

Analysis of Six Big Losses :

Breakdowns

Eliminating unplanned Down Time is critical to improving OEE. It is not only important to know how much Down Time your process is experiencing (and when) but also to be able to attribute the lost time to the specific source or reason for the loss .Root Cause Analysis is applied starting with the most severe loss categories.

Setup and Adjustments

Setup and Adjustment time is generally measured as the time between the last good part produced before Setup to the first consistent good parts produced after Setup. This often includes substantial adjustment and/or warm-up time in order to consistently produce parts that meet quality standards. Tracking Setup Time is critical to reducing this loss, together with an active program to reduce this time.

Small Stops and Reduced Speed

Small Stops and Reduced Speed are the most difficult of the Six Big Losses to monitor and record. Cycle Time Analysis should be utilized to pinpoint these loss types. In most processes recording data for Cycle Time Analysis needs to be automated since cycles are quick and repetitive events that do not leave adequate time for manual datalogging.

Startup Rejects and Production Rejects

Startup Rejects and Production Rejects are differentiated, since often the root causes are different between startup and steady-state production. Parts that require rework of any kind should be considered rejects. Tracking when rejects occur during a shift and/or job run can help pinpoint potential causes, and in many cases patterns will be discovered.

Measuring Overall Equipment/Plant Effectiveness

OEE is a "best practices" way to monitor and improve the efficiency of your manufacturing processes (i.e. machines, manufacturing cells, assembly lines).

OEE is simple and practical. It takes the most common and important sources of manufacturing productivity loss, places them into three primary categories and distills them into metrics that provide an excellent gauge for measuring where you are - and how you can improve!

OEE is frequently used as a key metric in TPM (Total Productive Maintenance) and Lean Manufacturing programs and gives you a consistent way to measure the effectiveness of TPM and other initiatives by providing an overall

Defining Six Biq Loss :

Breakdowns	Down Time Loss	• Tooling Failures • Unplanned Maintenance • General Breakdowns • Equipment Failure	There is flexibility on where to the threshold between a Breakdown (Down Time Loss) and a Small Stop (Speed Loss).
Setup and Adjustments	Down Time Loss	• Setup/Changeover • Material Shortages • Operator Shortages • Major Adjustments • Warm-Up Time	This loss is often addressed through setup time reduction programs.
Small Stops	Speed Loss	• Obstructed Product Flow • Component Jams • Misfeeds • Sensor Blocked • Delivery Blocked • Cleaning/Checking	Typically only includes stops that are under five minutes and that do not require maintenance personnel.
Reduced Speed	Speed Loss	• Rough Running • Under Nameplate Capacity • Under Design Capacity • Equipment Wear • Operator Inefficiency	Anything that keeps the process from running at its theoretical maximum speed (a.k.a. Ideal Run Rate or Nameplate Capacity).

Startup Rejects	Quality Loss	• Scrap • Rework • In-Process Damage • In-Process Expiration • Incorrect Assembly	Rejects during warm-up, startup or other early production. May be due to improper setup, warm-up period, etc.
Production Rejects	Quality Loss	• Scrap • Rework • In-Process Damage • In-Process Expiration • Incorrect Assembly	Rejects during steady-state production

framework for measuring production efficiency.

In order to quantify the wastages and losses arising in a plant or piece of equipment ,it is essential to measure the effectiveness of the equipments/plant in an organisation.

The overall performance of a single piece of equipment or entire plant is governed by the cumulative impact of the three OEE factors: Availability Rate, Performance Rate and Quality Rate. As discussed earlier,the main ingredients for determining the overall equipment effectiveness are three main categories of equipment-related losses-downtime, speed loss, and defect loss. In short,the term is referred to as'OEE'or^OPE' OEE = Availability Rate X Performance Rate X Quality Rate

As a thumb rule,minimum of 85% - 90% OEE/OPE to be achieved in a factory/plant.

Components of OEE :

Availability Rate : This is the time the equipment is really running, versus the time it could have been running. A low availability rate reflects down time loss.

$$\text{Availability Rate} = \frac{\text{Oparatinq Titue - Dowrttimt}}{\text{Total Operating}}$$

Performance Rate : This is the quantity produced during the running time, versus the potential quantity, given the designed speed of the equipment. A low performance rate reflects speed loss.

$$\text{Performance Rate} = \frac{\text{Total Output:}}{\text{Potential Output at Rated Speed}}$$

Quality Rate : This is the amount of good products versus the total amount of products produced. A low quality rate reflects defect losses

$$\text{Quality Rate} = \frac{\text{Good Output:}}{\text{Total Output}}$$

Stair-step Diagram of Overall Equipment Effectiveness

The following table shows the Six Big Losses, the associated OEE Factors and how Visual OEE provides real-time metrics and a powerful set of analytical tools to help everyone see how efficiently, effectively and consistently a production line or work cell is operating.

How to calculate OEE ?

The table below contains hypothetical data used in a simulated plant OEE calculation. Note that the same units of measurement (in this case minutes and pieces) are consistently used throughout the calculations.

Total Operating Time			
A Net Operating Time			*No Scheduled Production
B Running Time		* Failures * Setup	
C Target Output			
D Actual Output		* Minor Stoppages * Reduced Speed	
E Actual Output		Lost Effectiveness	
F Good Output	* Scrap/rework * Startup Losses		
OEE = B/A	X *DIG* X F/E		

Benefits of measuring OEE

The benefit of measuring OEE is to improve the effectiveness of equipments. Since equipment effectiveness affects shopfloor employees more than any other group, it is appropriate for them to be involved in tracking OEE and in planning and implementing equipment improve-ments to reduce lost effectiveness.

Let's look at some of the benefits of OEE measurement for operators and shift leaders or line managers.

The operator who collects the data about the equipment for use in the OEE calculation on a daily basis and this process in turn will:

- ✓teach the operator about the equipment
- ✓ focus the operator's attention on the losses
- ✓ grow a feeling of ownership of the equipment

The shift leader or line manager is often the one who will receive the daily

Six Big Losses	OEE Factor	Visual OEE™
Breakdowns	*Availability*	• **Availability** • Down Time (cumulative and event) • Real-time production mode indication • Reason Code tracking and analysis • Statistics and metrics are real-time automated • Operators can focus on getting equipment running
Setup and adjustments	*Availability*	• Setup Time (cumulative and event) • Set goals for Setup Time reduction programs
Small Stops	*Performance*	• **Performance** • Average Cycle Time • Small Stops (occurrences and time) • Configurable Small Stop Threshold • Cycle Time Trace records every cycle • Identify when and how time is lost to Small Stops
Reduced Speed	*Performance*	• Reduced Speed (occurrences and time) • Configurable Reduced Speed Threshold • Cycle Time Trace records every cycle • Identify Reduced Speed patterns
Startup Rejects	*Quality*	• Reject Pieces (during Startup) • Percent Reject Pieces (during Startup)
Production Rejects	*Quality*	• **Quality** • Reject pieces (during Production) • Percent Reject Pieces (during Production)

operating data from the operator and process it to develop information about the OEE. Working hands on with the data will:

- ✓ give the leader/manager basic facts and figures on the equipment
- ✓ help the leader/manager give appropriate feedback to the operators and others involved in equipment improvement
- ✓ allow the leader to keep management informed about equipment status and improvement results

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Item	Data
Shift Duration	8 hours = 480 min.
Short Breaks	2 @ 15 min. = 30 min.
Lunch Breaks	1 @ 30 min. = 30 min.
Down Time	30 minutes
Ideal Production Rate	55 pieces per minute
Actual Total Production	21000 pieces
Rejected Production	500 pieces

Availability Rate	**= (Operating Time-Down Time)/Total Op. Time**
	= 390 minutes/420 minutes
	= 0.92857 (92.86%)
Performance Rate	**= Total Output/Potential Output at Rated Speed**
	= (21000 pieces/390 minutes)/55 pieces per minute
	= 0.9790 (97.90%)
Quality Rate	**= Good Output/Total Output**
	= 20500/21000 pieces
	= 0.9762 (97.62%)
OEE	**= Availability x Performance x Quality**
	= 0.92857 x 0.9790 x 0.9761
	= 0.8873 (88.73%)

The Impact of Foreign Institutional Investment on Stock Market Liquidity and Volatility in India

This paper is aimed at examining the investmet trends and patterns of FIIs and their impact on stock market liquidity and volatility. Liquidity with reference to capital market refers to easy conversio of capital market securities into cash. Whereas the stock market volatility implies the fluctuations in the stock market returs over a time period. Volatility is the inconsistency or variability in the returns of aggregate market portfolio.

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Introduction

Stock market liberalization is a decision by a country's Government to allow purchase of shares in that country's stock market (Henry, 2000). The process of economic reforms was initiated to liberalize the Indian economy and to integrate it with the global economy. One of the immediate effects of capital inflows from foreign countries on the stock market is the boom that causes in the stock price indices. In fact, in the nineties, the stock market boom in several emerging economies has coincided by the increase of capital inflows to these countries (Levine, 1996). The external sector reforms in India during the 1990s included a market based exchange rate system, introduction of convertibility of rupee for external transactions on the current account and compositional shift in cross-boarder capital inflows from debt creating to non-debt creating flows. The overall approach of prudence was integrated into the process of growing openness and financial liberalization which were basic elements of the package of structural reforms instituted in the wake of the balance of payments crisis of 1991. In order to strengthen the external sector reforms and to benefit from these measures, complementary reforms were introduced in other segments of the economy as well (Report on Currency and Finance, 2003-04).

As a part of the reform process, the Government of India opened up the Indian capital market to global competition and took measures to initiate structural reforms by putting in place the requisite regulatory and supervisory structure in the form of SEBI. In a move towards current account convertibility and to increase foreign exchange inflows, Foreign Institutional Investors (FIIs) were permitted to invest in the tradable Indian securities such as shares, debentures, bonds, mutual fund units etc. through primary and secondary markets as per guidelines issued by Government of India in September 1992. Financial liberalization improves stock market liquidity on one hand and volatility on the other. This paper examines the positive (liquidity) and negative (volatility) impact on the stock market by the investment of FIIs in the country.

Concepts of Stock Market Liquidity and Volatility:

Liquidity is an important feature of any financial market. Liquidity is the lubricating agent that facilitates a frictionless smooth functioning of the financial markets. Liquidity is an essential and efficient part of a stock market. While liquidity refers to the ease with which the buyers and sellers promptly transact with minimal impact on the price of a stock, efficiency refers to the speed with which the prices in the market move to reflect the information flows. In general, the term liquidity refers to the easy convertibility of assets into cash and when we talk about scrips i.e. shares, debentures, bonds etc. their liquidity is directly related to the technicalities, depth and speculative tendencies in the market. Liquidity of an asset is very precisely defined by Keynes that an asset is more liquid than another, Mf it is more certainly realizable at short notice without loss' (1930). The variations in the degree of liquidity affect the price discovery process and efficiency of the market. If the price difference is less, then it indicates more liquid or the reverse position is less liquid. The liquidity of the market is the situation in which large quantities of shares are traded without having any material impact on the price of such shares.

Furthermore, the term Volatility is the most basic statistical risk measure. It can be used to measure the market risk of a single instrument or an entire portfolio. While, volatility can be expressed in different ways,

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statistically, volatility of a random variable is its standard deviation. In day-today practice, volatility is calculated for all sorts of random financial variables such as stock returns, interest rates, the market value of a portfolio, etc. Stock return volatility measures the random variability of the stock returns. Simply put, stock return volatility is the variation of the stock returns in time. More specifically, it is the standard deviation of daily stock returns around the mean value and the stock market volatility is the return volatility of the aggregate market portfolio. The high volatility is the reflection of high risk, because the security values are not dependable and the capital markets are not regarded as efficient. When examining the issue of stock market volatility, it is relevant to measure percentage of volatility of stock return. This reflects the percentage change in the value of the amount invested in the stock market.

Review of Literature:

A. Some of the important studies on the stock market liquidity are presented below:

- **Gurucharan Singh (2004)** highlighted that the securities market in India has come a long way in terms of infrastructure, adoption of best international practices and introduction of competition. Today, there is a need to review stock exchanges and improve the liquidity position of various scrips listed on them.
- **Patro and Wald (2003)** examined the firm's level analysis on the impact of capital market liberalization in 18 emerging economies they find that the cost of raising equity capital for firms reduces considerably after stock market liberalization. Lowered cost of raising capital is one of the important indicators of stock market liquidity and therefore, it leads credence to the prediction of theory that stock market liberalization improves stock market liquidity.
- Chandra (2002) concluded that the stock market liberalization improves liquidity of stock markets.
- **Levine & Zervos (1998) Kim & Singhal (2000)** have opined . that the evidence for the liquidity enhancing effects of capital inflows.
- A **study conducted** by the World Bank (1997) reports that stock market liquidity improved in those emerging economies that received higher portfolio investments.

B. Various studies taken place on the concept of volatility of the stock markets throughout the globe. Some of the important contributions are as follows:

- **M.T. Raju and Anirban Ghosh (2004)** study concludes the mature markets continue to provide over a long period of time high return with low volatility. Amongst emerging markets except India and China, all other countries exhibited low returns. India with long history and China with short history, both provide as high a return as the US and UK market could provide but volatility in both the countries is higher.
- **Havinder Kaur** (2004) study describes the extent and pattern of stock return volatility of the Indian stock market during the yearl990 to 2000. He covers the two most prominent spot price indices viz. BSE Sensex and S&P CNX Nifty. It is found that the stock market volatility was the highest during 1992 followed by 1990 and 2000, in that order. It fell sharply after 1992 until 1995, after which it started increasing again.
- Gordon, *3.* **and** P. Gupta (2003) have made an observation that the volatility of portfolio flows into India was small in comparison to other emerging markets during 1998 to 2000. While the coefficient of variation for such flows in India was 1.58, the corresponding figures for the Philippines, Thailand, Korea, Chile and Brazil stood at 1.79, 25.07, 1.82, 1.94 and 2.14 respectively.
- **Jo, Gab-Je (2002) and Bae et al (2002)** studies had shown empirically tested instances where foreign investment induces greater volatility in markets compared to domestic investors and stocks mainly traded by such investors experience higher volatility than those in which such investors do not have much interest.
- **Kassimatis, et al., (1999) and Poshakwale, et al., (2001)** suggest that capital inflows have not caused stock markets to be volatile rather, In some cases volatility has declined after liberalization. This had found to be true in the case of Argentina, Pakistan, Philippines, and Taiwan as well as in the case of Poland and Hungary.
- **J.S. Pasricha and Umesh C. Singh (2001)** study found that FIIs have remained net investors in the country except during 1998-99 and their investment has been steadily growing since their entry in the Indian markets.
- **Calvo, et al., (1999)** suggest that foreign investors purse irrational trading strategies such as herding and quick changes in sentiments that make the emerging stock markets volatile. They argue that information disadvantage and diversified international portfolio investment create incentives for rational herd behavior causing stock markets in emerging economies to be volatile.
- **Fitz Gerald (1999)** observed that the large and sudden reversals of foreign equity investments make them extremely volatile in character. The securities markets in developing countries are typically narrow and shallow, and therefore, participation of foreign portfolio

investors may, a priori, induce considerable instability in these markets.

- **Levine, et al., (1998)** suggest that international portfolio investment can increase volatility of emerging stock markets, if fund managers or foreign investors make investment decisions based on short-term gains, flocking towards countries whose stock markets are booming and fleeing them at the hint of trouble.
- **Gregory, et al., (1996)** examined how volatility of S&P 500 Index Futures affects the S&P 500 Index volatility. Their study also examined the effect of good and bad news on the spot market volatility. They find that bad news increased volatility more than good news and the degree of asymmetry was higher for futures market.
- **Liu, et *al.*$_f$ (1996)** examined the transmission of daily stock price volatility among the US, Japan, Hong Kong, Singapore, Taiwan, Thailand and South Korea. Their study showed that international transmission of price volatility increased after the 1987 crash and that Japan and Singapore play a more important role in transmitting price volatility to other Pacific Basin markets.
- **Aitkin (1996) and Dornbusch, et al., (1995)** suggests that capital inflows cause volatility in the stock market is that of 'positive feedback trading'.

IV. Objectives and Research Design:

A. Objectives:

The present study based on the following main objectives:

- To explain the concepts of stock market liquidity and volatility.
- To study the impact of FII's investment on stock market liquidity and volatility.
- To present summary of findings based on the present study as well as offer suitable measures.

B. **Hypotheses:**

For the purpose of the study the following hypotheses are set:

- Stock market liberalization leads to high FII's investment inflow.
- FII's investment played a major role in improving stock market liquidity.
- FII's investment inflows affect the stock market volatility. FII's investment correlated with the market index of BSE Sensex and NSE S&P UNIX Nifty.

C. Sample:

The study based on the stock prices of two important stock exchanges in India i.e., BSE and NSE. For this purpose one market index is selected from each of these two stock exchanges such as BSE Sensex and S&P CNX Nifty respectively. NSE and BSE are the two major exchanges in terms of volumes traded, delivered and market capitalization. Between these two exchanges, NSE accounts for two-thirds of the turnover and the rest is claimed by BSE. The basic premises that the indices were constructed include all the listed and traded companies.

D. Data:

The stock price indices, FII transactions i.e. purchases, sales and investment data have been taken from PROWESS, the online database maintained by the Centre for Monitoring of Indian Economy (CMIE), Handbook of Statistics of the Reserve Bank of India (RBI), SEBI Handbook, SEBI Monthly Bulletin and SEBI Annual Report of 2004 and 2005. The relevant information is also taken from the business line, the economic times, NSE, BSE and SEBI Websites.

E. Study Period:

The study spans the period from January 2003 to March 2005. During this period SEBI/RBI initiated various policy initiatives, guidelines and enacted investment limits of FII's from the time to time in the Indian capital market.

V. Analysis of the Impact of FIIs Investment on Stock Market Liquidity in India:

The Indian stock markets entered into a new bull phase in November 2004. The BSE Sensex crossed the 7700 mark in July, 2005 and further gaining the strength. A major factor that has been driving the Sensex to new highs has been the increasing liquidity in the Indian stock market, with strong inflows from FIIs. In fact, in recent times as the number of FIIs registering with SEBI has gone up sharply, from 637 in 2004 to 733, as on July 14, 2005, it has resulted in a sharp rise in inflows. The net inflows from FIIs during the first seven months have already touched $ 5.42 billion, as on July 14, 2005 (during the 2004, last calendar year, FIIs invested $ 8.5 billion); experts believe that this could see the FII inflows surpassing the previous year's numbers. Their optimism Is based on the fact that the Indian economy has been growing at a faster rate and attracting more and more FIIs across the globe. The Japanese investors have also come to India in 2005 for the first time. According to the Economic Times, July 12, 2005 edition, Japan has emerged as one of the biggest investors in recent times. It estimates that Japanese investments in the Indian market have crossed the $ 1.5 billion mark. It further adds that Japanese investors with over $ 10 trillion in savings are looking at newer emerging markets. More so, with the terribly low interest rates in Japan, it adds.

The stock market rally was ignited by the FII inflows into the equity segment. This pattern examined by taking the proportion of FIIs investment in the market capitalization. "Market capitalization refers to the value of the stock multiplied by the total number of shares outstanding". The relationship between FIIs investment and market capitalization indicates the degree of liquidity in the capital market. The increased investment leads to the Increased capital employed and vice

versa in the short run (Table-1).

The following points are observed from the data of Table-1 and in general:

- There has been steady growth in investment by FIIs in India over the years. The highest amount (Rs. 9,483 crore) of FIIs net investment was recorded in the month of March 2003.
- The FIIs investment in Indian securities market as shown a fluctuating trend year after year starting from US $1.6 billion in the year 1994-95 and reached US $2.0 billion in the year 1995-96.
- The calendar year 2004 has received an historic net inflow from FIIs to the tune of US $ 9.187 billion which is around 28 percent of the total inflow has been received during the last six months of the year, July-December 2004.
- This explosive portfolio flows by FIIs brings with them great advantages as they are engines of growth lowering cost of capital in many emerging markets. They facilitate the flow of capital to firms and countries that offer the best investment opportunities breaking the geographical boundaries.
- The Indian economy has been one of the fastest growing economies in the world, next only to China. According to the strong growth rate of GDP, India now ranks 10th among the largest economies in the world (World Bank Report).
- The country's GDP has been growing at a faster rate in the recent years. In fact, in Financial Year 2004 it clocked a growth rate of 8.5 percent and is expected to grow well over 6 percent.
- FIIs have invested $4.7 billion in Indian equities in 2005 so far. Where as it were $8.4 billion in 2004 and $ 6.7 billion in 2003. Over the past six months, 100 new FIIs have registered with SEBI to take the total number to 733.

Tabie-1: Investment Behaviour of FIIs and Market Capitalisation

Months	Net **Investment (Rs. Crore)**	**Cumulative** Investment (Rs. **Crore) X**	**Market Capitalisation (Rs. Crore)**	
			NSE V	**BSE z**
2003				
January	1,163	58,831	572,277	611,472
February	482	59,313	581,985	619,873
March	877	60,190	537,133	572,197
April	1,012	61,202	530,630	572,526
may	3,102	64,304	612,030	660,982
June	3,438	67,742	678,550	734,389
July	2,243	69,985	719,145	775,996
August	2,163	72,148	836,651	905,193
September	4,293	76-,441	863,481	933,087
October	6,565	83,006	926,748	1,000,494
Noverber	3,773	86,779	979,541	1,065,853
December	6,407	93,186	1,167,029	1,273,361
2004				
January	3,161	_96,347	1,116,150	1,206,854
February	3,329	99,676	1,110,954	1,196,221
March	9,483	109,159	1,120,976	1,201,207
April	3,425	112,584	1,171,828	1,255,347
May	-3,507	109,077	950,494	1,023,131
June	-523	108,554	979,700	1,047,258
July	996	109,550	1,066,087	1,135,589
August	2,507	112,057	1,143,075	1,216,566
September	2,897	114,954	1,227,550	1,309,318
October	2,921	117,875	1,253,825	1,337,191
Noverber	8,139	126,014	1,446,292	1,539,594
December	8,988	135,002	1,579,161	1,685,989
2005				
January	564	135,566	1,557,444	1,661,533
February	8,827	144,393	1,614,597	1,730,941
March	7,686	152,079	1,585,585	1,698,428
Correlation (Rxy and Rxz)			**0.963**	**0.960**
Coefficent of Determination (%)			**93.00**	**92.00**
t- Test			**18.000**	**17.000**
to.oS (Table Value)			**2.074**	**2.074**

Source: CMIE: Capital Markets Special Issue June 2005, P.254, 278 and 300.

- The correlation between FIIs cumulative investment and market capitalization on NSE and BSE was recorded at 0.963 and 0.960 respectively.
- This highly correlated relation is also gives the higher percentage of determination i.e. 93% and 92% was observed on the NSE and BSE respectively.
- The higher percentage of determination explains any change has been taken place in capital employed was because of the FIIs investment.
- This is also proved by the t-test. The calculated value of t is greater than the table. Hence, it says that the capital employed was influenced by the FIIs investment in the NSE and BSE in particular and the Indian capital market in general.
- If we analyze the reasons for such enormous enthusiasm of FIIs in Indian capital market may be on account of the following:

✓ The Indian capital markets are well structured, regulated and matured market.

✓ The P/E ratios of Indian securities are lowest in the world.

✓ Relatively low risk associated with investment opportunities.

✓ Implementation of further capital market reforms along with liberalization of FIIs investment in India in different sectors.

✓ The overseas investment companies' mutual funds–USA,

UK, Japan and other European Countries find India is the safe heaven for investment.

- ✓ The optimistic growth rate in the GDP accompanies by low inflationary tendencies.
- ✓ Over pricing of securities in all other developed capital market in the world.
- ➢ Hence, we conclude that FIIs are active traders in the Indian stock market and their quantum of investment and active trading has possibly helped to increase the liquidity of the Indian stock market.

VI. The Impact of FIIs Investment on Stock Market Volatility in India:

The impact of global financial integration and the associated rise in capital inflows on stock market volatility is in general, investors' decision of buying/selling of shares depends on the price earning ratios of the companies. But FIIs influencing the stock market are very high even though their cumulative investment as a percentage of total market capitalization is relatively lower. They completely changed the pattern and psychology of the capital market and they have become the market movers. We examine the impact of FII's Investment on stock market volatility by comparing the market index movements of BSE Sensex and NSE Nifty.

Stock market volatility and FIIs investment is measured by using standard deviation. In simple terms, standard deviation measures the deviation of the returns of equity from its mean return. It is an absolute measure i.e. standard deviation of stock returns in one period can be compared with standard deviation of another period to understand which period has been more volatile. Volatility is calculated as the standard deviation of the rates of return. The rate of return is the change in price during the period, divided by the price of the investment at the beginning of the period. We compared the FIIs investment with the volatility of BSE SENSEX and NSE S&P CNX NIFTY indices by taking correlation and tests of hypothesis.

Following observations are made **on the basis of the above data:**

- ➢ We observed from the Table~2 that the cumulative investment by FIIs shows the increasing trend and some of the downwards are also witnessed. The BSE Sensex and NSE Nifty have been moving in cycle with investment behavior of FIIs over the period of two years (compared on month to month basis) from January 2003 to March 2005. The positive net investments by FIIs have resulted into appreciation in both BSE Sensex and NSE Nifty and negative net investment is followed by decline in both. This trend is recorded reverse in some of the months because of the other capital market reforms like online trading, dematerialized trading, etc. The high positive values of Coefficient of Correlation at 0.959 and 0.954 between cumulative investment and BSE Sensex and NSE Nifty indicate that the market indices are highly influenced by the FIIs flows. This is also supported by the t-test.
- ➢ However, it will also pertinent to note that the entire volatility in stock market is not due to investment behavior of FIIs. It is also evident from Table-3, the relative movement in BSE Sensex and NSE Nifty compared to FIIs investment is not of the same magnitude, rather somewhat greater both on upward and downward side. Thus, there are

Table-2: Investment Behaviour of FIIs and Market Index Movements

Months	Net investment **(Rs. Crore)**	Cumulative Investment (Rs. Crore) **X**	**BSE** SENSEX y	**NSE** S&P **CNX** NIFTY **z**
2003				
January	1,163	58,831	3,250	1,042
February	482	59,313	3,284	1,063
March	877	60,190	3,049	978
April	1,012	61,202	2,960	934
May	3,102	64,304	3,181	1,007
June	3,438	67,742	3,607	1,134
July	2,243	69,985	3,793	1,186
August	2,163	72,148	4,245	1,357
September	4,293	76,441	4,453	1,417
October	6,56s	83,006	4,907	1,5S6
Noverber	3,773	06,7/9	5,045	1,615
December	6,407	93,186	5.839	1,880
2004				
January	3,161	96,347	5,696	1,810
February	3,329	99,676	5,668	1,800
March	9,483	109,159	5,591	1,772
April	3,425	112,584	5,655	1,796
May	-3,507	109,077	4,760	1,484
June	-523	108,554	4,795	1,506
July	996	109,550	5,170	1,632
August	2,507	112,057	5,192	1,632
September	2,897	114,954	5,584	1,746
October	2,921	117,875	5,672	1,787
Noverber	8,139	126,014	6,234	1,959
December	8,988	135,002	6,603	2,080
2005				
January	564	135,566	6,556	2,058
February	8,827	144,393	6,714	2,103
March	7.686	152,079	6,493	2,036
Correlation (Rxy and Rxz)			**0.959**	0.954
Coefficent of Determination (%)			**91.97**	**91.10**
t- Test			**16.920**	**16.000**
to.o5 (Table Value)			**2.074**	**2.074**

Source: CMIE: Capital Markets Special Issue June 2004 and 2005, P.248, 270 and 296.

Table-3: Relative Movement of FII's Investment with Market Index

Months	Cumulative Investment	BSE SENSEX	NSE *S&P* CNX NIFTY
2003			
January	100.0	100.0	100.0
February	100.8	101.0	102.0
March	101.5	92.8	92.0
April	101.7	97.1	95.5
may	105.1	107.5	107.8
June	105.3	113.4	112.6
July	103.3	105.2	104.6
August	103.1	111.9	114.4
September	105.9	104.9	104.4
October	108.6	110.2	109.8
November	104.5	102.8	8.0
December	107.4	115.7	116.4
2004			
January	103.4	97.6	96.3
February	103.5	99.5	99.4
March	109.5	98.6	98.4
April	103.1	101.1	101.4
may	96.9	84.2	82.6
June	99.5	100.7	101.5
July	100.9	107.8	108.4
August	102.3	100.4	100.0
September	102.6	107.6	106.9
October	102.5	101.6	102.3
Noverber	106.9	109.9	109.6
December	107.1	105.9	106.2
2005			
January	100.4	99.3	98.9
February	106.5	102.4	102.2
March	105.3	96.7	96.8

Source: Compiled fromTable-2.

several other factors which also add to volatility in stock market. However, the effect of all of these together is quite lesser than that of the FIIs investment pattern. Hence, FIIs have emerged as the market movers.

VII. Conclusions:

The study of "The Impact of Foreign Institutional Investment on Stock Market Liquidity and Volatility in India" has revealed the following broad conclusions:

❖ The FIIs investment in Indian securities market has shown fluctuating trend year after year.

❖ The number of FIIs has also steeply increased from 158 in 1993-94 to 540 in 2003-04 registering an increase at 242 percent and it was further, steeply gone up to 733 as on July 14th, 2005.

❖ The reasons for enormous enthusiasm of FIIs in Indian capital market may be on account of well structured, regulated and matured capital market, low risk, and evidence of basic fundamental in the Indian capital market.

❖ According to the correlation and t-test analysis we conclude that the FIIs investment was influence the stock market liquidity and this evidence Is drawn by studying the relationship between FIIs investment and market capitalization.

❖ 'The high positive values of co-efficient of correlation at 0.968 between cumulative investment and BSE Sensex and NSE Nifty indicate that the market indices are highly influenced by the FIIs flows. However, it is also indicated that there are several other factors which also is relatively lower than the impact of FIIs. Hence, FIIs have emerged as the market movers in India.

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- www.epw.org.in❑

EASTERN REGION

CUTTACK BHUBANESWAR CHAPTER

Business Communication Training Programme for Intermediate (Stage-I) students

A training programme on "Business Communication and Soft skill" was organized for the students on 16th December, 2007. Emphasis was given on non-verbal and verbal communication and the students participated very actively in the training programme.

Talk on "Fringe Benefit Tax-It's Impact on Employers & Employees" by Dr. Vinod k Singhania

As a part of the continuing education programme, the Chapter organised an evening talk on **"Fringe Benefit Tax- It's Impact on Employers & Employees"** on 4th January, 2008 at its Conference hall. Dr. Vinod K Singhania, renowned author of many popular books was the chief speaker. Niranjan Swain moderated the technical session.

Workshop on "Winning Strategy" for Students

A Workshop was conducted on 13th January, 2008 (Sunday) for the final & Intermediate students on **"Winning Strategy"** Mr Ajaya Agarwal, Director, Rapid Learning System (Kolkata), an Associate member of our Institute and also a nationally acclaimed Corporate Trainer and Management Consultant conducted the workshop. Issues like effective Verbal and Non-Verbal communication, body language, self confidence, etiquettes, mannerism and time management etc. were dealt with in detail.

Faculty Meeting on Implementation of New Syllabus of ICWAI

A meeting was organised by the Chapter on 20th January, 2008 (Sunday) for its Managing Committee members, staffs and faculties to make open discussion for implementation of new syllabus.

Celebration on Republic Day

The Chapter observed Republic Day on 26th January, 2008 at its premises. G. B. Swain, Chairman of the Chapter hoisted the National Flag. Members, Students and Staffs participated in large numbers.

Career Awareness programme for ICWAI pursuing students.

A career awareness programme was organised by the Chapter at its conference hall on 18th January, 2008. Dr. Partha Sarathi Mohapatra, Asst. Professor, Morgaon State University, USA deliberated on the topic "Doctoral Education in Accounting in USA - Prospectus and opportunity". Students participated very actively and made lots of interaction with Dr. Mohapatra who enlightened the students with his excellent educational environmental analysis.

DHANBAD-SINDRI CHAPTER

Lecture Meet

Dhanbad-Sindri chapter of Cost Accountants organized a lecture meet on the topics "Survival of Underground Mines" at ICWAI Bhawan on 4.12.2007. The guest speaker of the evening was P. P. Gupta, Dy. CME, Bharat Coking Coal Limited, and a senior member of our profession. The lecture was followed by 'interaction session'. On this occasion, July-September-2007 edition of our quarterly 'newsletter' was also released by P G Nandi, General Manager (Finance), Bharat Coking Coal Limited. The meeting ended with vote of thanks by A. K. Nath, a member of our managing committee.

Career Awarness Programme

Dhanbad Sindri Chapter of Cost Accountants organised a **'Career Awarness Programme'** in the following colleges of Dhanbad on 16th January 2008.

1. Shree Shree Laxmi Narayan Trust Mahila College.
2. P. K. Roy Memorial College

K. N. Mukhopadhyay, Chairman of the Chapter along with members visited the colleges and impressed the students about the prospect of 'Cost and Management Accountancy' as a profession. Students took keen interest and raised numbers of queries about 'Cost Accountancy Course' which were duly dealt with.

RAJPUR CHAPTER

Members Meet and Annual Get Together

Rajpur Chapter of Cost Accountants organized a Members Meet & Annual Get Together function on 3rd February, 2008 at a farm house at Gobindopur, Baruipur, South 24 Pgs. A lively discussion took place on the prospects of the ICWAI profession in which members of the chapter including other AICWA guests Members present on the occasion participated.

SOUTH ORISSA CHAPTER

Eastern India Regional Cost Convention, 2007-08

The newly born South Orissa Chapter Of Cost Accountants (SOCOCA) organized three days Regional Cost Convention, 2007-08 from 8th February to 10th February, 2008 at Hotel Plaza Millennium, Gopalpur-On-Sea, Berhampur, Dist: Ganjam (Orissa) on the topic " Challenges of Reforms & Emerging Issues - Role of Management Accountants".

The Convention was inaugurated by Shri Chandra Sekhar Sahoo, Hon'ble Minister of State for Rural Development, Govt,. of India on 08.02.08 in presence of Dr. Trinath Behera, M.L.A, Gopalpur, Dr. Chau Pattnaik, M.L.A, Berhampur, Chandra Wadhwa, President, Kunal Banerjee, Vice-President, Pravakar Mohanty,

Former President, B B Goyal, I.C.A.S,Advisor (Cost) MCA, GOI, K K Sarkar, Chairman, EIRC, Central Council Members and Regional Council Members of EIRC and other dignitaries . The Hon'ble Minister appreciated the endeavour of the chapter to organize three days Convention at Gopalpur-On-Sea and was pleased to extend all types of support to the Chapter and utilize the services of the profession by his Ministry to ensure optimum utilization of the funds allocated for the development of the Country.

The Hon'ble Minister felicitated the President, Vice- President, B B Goyal, Advisor (Cost), B L Bagra, Director (Finance) NALCO, P.Mohanty , Former President of ICWA, Central Council & Regional Council Members present. N C Kar, Chairman, SOCOCA offered vote of thanks.

The plenary session on 09.02.08 was presided by Kunal Banerjee, Vice-President. Amal Kumar Das , Former President, ICWA, B. L .Bagra, Director (Finance) NALCO, S C Mohanty, Chairman, Corporate & Allied Laws Committee, G N Venkat Raman, Chairman, CEP Committee addressed the gathering. Smt Tanmaya S. Pradhan, Chairperson, MDPC of EIRC of ICWAI offered vote of thanks.

The First Technical Session on Valuation of Management & Pre-datory Price under Competition Commission was presided over by Chandra Wadhwa, President ICWA, B B Goyal, ICAS, Advisor (Cost), GOI & A. S. Durga Prasad, Chairman, WTO & International Affairs Committee presented paper on Valuation Management & Chandra Wadhwa, President spoke on pre-datory Price under Competition Commission. L D Upadhyay, Secretary, SOCOCA offered vote of thanks.

The Second Technical Session on "PSU Restructuring" was presided over by Pravakar Mohanty, Former President, ICWA. B. B. Goyal, ICAS, Advisor (Cost), GOI and professor Shreedhar Das, XIMB presented their papers. Saswat Dasgupta, Chairman, Research Committee of EIRC offered vote of thanks.

The Third Technical Session on "Power Sector Reforms" was presided over by B B Goyal, ICAS, Advisor (Cost), GDI. Professor D V Raman, XIMB, S K Mishra, Sr. General Manager (Finance) & Company Secretary, CESU, Shri B N .Mallick, DGM (Finance), Southco and B K Das, Manager (Finance), OHPC presented their papers. L D Upadhyaya, Secretary, SOCOCA offered vote of thanks.

The Fourth Technical Session on "Accelerating Industrialization & Related Issues" was chaired by Ajit Mohapatra, CMD, Kaling Engineers Ltd. Dr. Ranjan Bal, Professor, Dept. of Commerce, Utkal University & P K Bal, FCA presented their papers. A Acharya, Chief Manager (Finance) & Former Secretary Talcher- Angul Chapter was the rappoteur & offered vote of thanks.

The "Valedictory Session" was chaired by Ajit Mohapatra, President, Orissa State Productivity Council. B. Mohapatra, Director(Finance), Mahanadi Coal Fields Ltd , Dr. Jagannath Panda, Professor , Dept of Commerce , Berhampur University, Dr. Sudipti Banerjea, Professor, Dept. of Commerce , Calcutta University, Mr. Pravakar Mohanty, Former President ICWA & Mr. D C Sahu, General Manager (Finance) NALCO Ltd & Chairman,Talcher - Angul Chapter were the panelists. The Chief Guest released the Souvenir. B Mohapatra, Director (Finance), MCL was felicitated for his remarkable contribution in the Coal Industry and to the Chapter and the Profession. The Chapter also felicitated S C Mohanty, Chairman, Corporate & Allied Laws Committee , ICWAI, A. Acharya, Chief Manager(Finance), NALCO and B. K. Das, Manager (Finance), NALCO for their valuable guidance for the overall success of the Convention & remarkable contribution to the Profession. The dedicated services of volunteers were recognized and honored by the Chief Guest. N C kar, Chairman, SOCOCA offered vote of thanks.

B K Das, Manager (Finance) National Aluminium Company Ltd and Secretary, Talcher-Angul Chapter was the co-ordinated and conducted the proceedings of the Convention.

WESTERN REGION

KALYAN AMBERNATH CHAPTER

Inauguration of New Batch

The Chapter organised the inauguration function of its new batch of classes on 5th January, 2008. D. M. Bathija, Chairman welcomed the guests.

Jyotika Ozarkar, Vice Principal of C.H.M. College was the Chief Guest. She inaugurated the classes by lighting a lamp. She, in her inaugural address said that, human touch is necessary in every work which we do.

Study Circle Meeting

The Chapter's 8th Study Circle Meeting was held on 5th January, 2008 at 7.30 p.m. on the subject **"Reverse Mortgage".** A. K. Deshmukh spoke on the subject. He among other things, said that this scheme is beneficial for those Senior Citizens who are property rich but cash poor. Meeting was well attended by the members.

Republic Day Function

The Chapter organised Republic Day Function on 26th January, 2008 at 9.30 a.m. D. M. Bathija, Chairman hoisted the Flag.

PUNE CHAPTER

Republic Day Celebration

Pune Chapter of Cost Accountants

organised Flag Hoisting Ceremony on 26th January 2008 at the Chapter's premises at Laxminagar, Pune. A B Nawal, Vice-Chairman, WIRC hoisted the flag on this occasion.

Continuing Education Programme

Held on Tuesday, 29th January 2008

Pune Chapter of Cost Accountants conducted Continuing Education Programme on **'ERP Implementation'.** The program was inaugurated on 29th January 2008 at Ness Wadia College of Commerce, Pune. Milind Date, Cost Accountant and CFO– Endurance Technologies Ltd, Pune delivered the lecture on the subject. Pramod Dube, Practicing Cost Accountant and Chairman of Professional Development Committee of Pune Chapter felicitated Milind Date on this occasion.

The theme of the lecture was how CMAs can contribute in a great way to ensure smooth ERP Implementations. The purpose of the CEP is to make the members aware of some of the important issues that need to be addressed in the process of ERP Implementation. Date presented the total scope of the subject.

NORTHERN REGION

ALLAHABAD CHAPTER

Press Release

Republic Day was celebrated at chapters land at Jhunsi S. M. Anwar Hasan Chairman unfurled the National Flag. Speaking on the occasion, he said, if we don't see even a glimpse of that great India in the India that we witness these days, it obviously means that we are not working up to our potential; and that if we do, we could once again be an eternally unblemished and inspiring country setting a bright path for rest of the world to follow.

NOIDA CHAPTER

Programme on "Implementation of VAT in Uttar Pradesh" organized by Noida Chapter of ICWAI on 9th Jan 2008 at Noida

A Talk on "Implementation of VAT in Uttar Pradesh" was organized by Noida Chapter of ICWAI on 9th Jan 2008 at Main Auditorium, Kribhco Bhawan, Sector 1, Noida. The said programme was organized by Noida Chapter of ICWAI jointly in association with Noida Chapter of ICSI, Noida Branch of ICAI and Noida Management Association. Large no. of members from the four organizing bodies participated in the Meet made the programme a grand success.

The guest speakers on the occasion included CK Malhotra, Advocate, Suraj Prakash, DGM (Indirect Taxation), BHEL & Secretary Noida Chapter of ICWAI & TK Srivastava, Joint Commissioner, Commercial Tax, Noida, R N Chaturvedi, Joint Commissioner, Commercial Tax, Noida also participated and graced the occasion.

The C K Malhotra, Advocate gave an overview of various VAT provisions in Uttar Pradesh highlighting the provisions relating to input tax credit on inputs and capital goods, reverse input tax credit, filing of returns, tax period, types of invoicing including tax invoices, sale invoices etc. He also gave a brief account of provisions relating to refund and assessment.

Suraj Prakash, DGM (Indirect Taxation), BHEL & Secretary Noida Chapter of ICWAI gave a detailed presentation on VAT provisions with focus on industry's perspective in relation to VAT provisions.

T K Srivastava, Joint Commissioner gave a brief account of various provisions of VAT including input credit, reverse input credit, capital goods, invoicing, filing of tax returns, tax period, computation of reverse input credit for stock transfers, goods returned within six months etc.

R N Chaturvedi, Joint Commissioner, Commercial Tax, Noida also spoke on the occasion and shared his views and experiences with the participants.

G P Rao, Chairman Noida Chapter of ICWAI proposed a hearty vote of thanks.

SOUTHERN REGION

Southern India Regional Cost Convention 2007

SIRC Regional Cost Convention was successfully conducted 30th November 2007 and 1st of December 2007 at Cochin under a theme 'Management Accounting- Driving Stakeholder Value. More than 400 delegates attended the convention, which includes practicing Cost Accountants, corporate delegates and student delegates.

The convention was inaugurated by renowned industrialist Kochuouseph Chittilappally, MD V-Guard Industries Ltd in the presence of President of the Institute Chandra Wadhwa as the Guest of Honour. Sunil Chacko, SIRC Chairman chaired the function. Kunal Banarjee, Vice President of Institute, NP Sukumaran, Past President of ICWAI also spoke during the inaugural function. KA Felix, Chairman of Cochin Chapter of ICWAI welcomed the gathering and AVSN Nageswara Rao proposed the Vote of Thanks. The Central Council Members and Regional Council members of ICWAI also graced the function with their presence.

Four technical sessions were conducted with the participation of expert speakers and session chairmen and the interaction of the audience was also very much value adding. The topics for the technical sessions were as follows

- Strategic Management Accounting for Value Creation
- IT- A Performance Management Enabler
- Cost Management in Logistics
- Green Management Accounting

The subject experts includes Prof. Saji Gopinath, IIM Kozhikkode, Thiruvengudum , Deloitte Touche Tohmatsu, AN Raman, CCM of ICWAI, Kattayil Rajinish Menon, Product Evangelist, Microsoft India, Rohit Jaipuria, Consultant, SAS International, Dr. C. Unnikrishnan, Dy. Secretary, Cochin Port Trust, Guy Rabbat, CEO, Global Supply Chain, SFO Technologies Ltd., Emmy De Silva, Sr. General Manager - Materials, Malayala Manorama, Dr. MP Sukumaran Nair, MD, Travancore Cochin Chemicals Ltd., KV Mahidhar, Principal Counsellor, CII GBC and Naveen Somasundaram, Sr. Manager, Senergy Global Pvt. Ltd.

Evening Cultural Dinner showcased different traditional art forms of Kerala. T. Prabhakar, RCM of ICWAI summed up the sessions and Kunal Banarjee, Vice President of the Institute delivered the valedictory address.

HYDERABAD CHAPTER

Training Programme on "Finance for Non Finance Executives" Nagarjuna Construction Company Limited, Hyderabad 17th, 18th and 19th December, 2007

Hyderabad Chapter arranged a Training Programme on "**Finance for Non Finance Executives"** of Nagarjuna Construction Company Ltd., from 17th-19th December, 2007 associating with the Institute of Public Enterprises, Osmania University, Hyderabad. 35 Employees from the company participated the programme. The programme was a grand success.

Training Programme on "Cost Benefit Analysis and decision making" for Finance Executives of Singareni Collieries Company Ltd., during 20th and 21st December, 2007.

On the request of Singareni Collieries Company Ltd., Kothagudem a Training programme was conducted during 21st and 22nd December, 2007 at their premises. 20 employees from various departments were drawn by the company for the training.

Regional Cost Convention 2007-Cochin-30th Nov. and 1st Dec, 2007

The Chapter was adjudged as Best Chapter at the Regional Cost Convention held at Cochin during 30th November and 1st December 2007 at Cochin. M. Kameswara Rao, Chairman, Hyderabad Chapter of Cost Accountants received the award from the hands of Kunal Banerjee, Vice President of the Institute on 1st December, 2007 at Cochin.

Chapter's Formation day cum Members Meet-06.01.2008

Chapter's Formation Day cum Member's Meet was arranged on Sunday the 6th January, 2008 at BM Birla Science Planetarium, Adarsh Nagar, Hyderabad. Distinguished personalities of CMA profession such as CMA R.S. Raju, Vice President (F&A), Nagarjuna Construction Company Limited, Hyderabad, CMA K.R. Venkateswarlu, Director-Finance, National Mineral Development Corporation Ltd., CMA P. Bhaskara Narayana, Director and Chief Financial Officer, Natco Pharma Limited, Hyderabad CMA B.V. Rama Murty, Managing Director, Hyderabad Pharma Infrastructure Technologies Ltd., were honoured on this occasion.

Training Programme on "Finance Matters"-HMT Machine Tools Limited, Balanagar, Hyderabad, Their Executives.

Hyderabad Chapter arranged an In-house Training Programme on **"Finance Matters"** for the Executives of HMT Machine Tools Ltd., Balanagar, Hyderabad during 17th-18th January, 2008 and also 28th and 29th January, 2008 at their premises. The programme covered various subjects like Central Excise and Customs, AP VAT/CST Act, Works Contract, Service Tax , TDS/TCS and Labour Laws. The programme was a grand success from the feed back received from the participants. 50 Executives were trained in two batches.

Soft Skills -Communication Skills:

Ms G. Sraya, B.'l'ech, who is a member of Cognorators Team - Cognizant platform Counselled the Foundation, Inter and Final students of Himayatnagar and Sanathnagar Coaching Centres, by giving tips to improve soft skills and communication skills during 17"', 18"' and 19"" January, 2008. It was much useful for the students who attended the above programme and well received by the students.

Republic Day Celebrations

59th Republic Day Celebration were held at Chapter premises on 26 January 2008. Member, all the the office staff and other members attended the function.

Students programme-Magnitude 2008.1

A Students Quiz Programme **"Magnitude-2008.1"** was organized on 26th January, 2008 by the Chapter for the students of the present batch at Surana Udyog Auditorium. The Federation of A.P. Chambers of Commerce and Industry, Red Hills, Hyderabad. M. Kameswara Rao, Chairman of the Chapter welcomed the gathering. Chief Guest R. Balarami Reddy, Director-Finance and CFO, IVRCL Infrastructure & Projects Ltd., Hyderabad addressed the students, motivated them and guided with valuable inputs.❑

OBITUARY

Shri B R Shah, past Central Council Member of the Institute (1989-92), past Chairman of WIRC-ICWAI (1983-84) and past Chairman of Ahmedabad Chapter passed away on 11 February 2008. Shri Shah was a brilliant professional and well known for his life long devotion to the cause of the Cost & Management Accounting profession in India.

May his soul rest in peace.