SUBJECT :
UGC NET COMMERCE (08)

UNIT – I :
BUSINESS ENVIRONMENT AND INTERNATIONAL BUSINESS

Contents

Chapter No	Title	Page No
1.	**Business Environment** • Concepts and elements of business environment	1-2
2.	**Economic Environment** • Economic systems • Economic policies(Monetary and fiscal policies)	3-13
3.	**Political Enviroenment** • Role of government in business	14-15
4.	**Legal Environment** • Consumer Protection Act, • FEMA • Socio-cultural factors and their influence on business • Corporate Social Responsibility (CSR)	16-31
5.	**International Business** • Scope and importance of international business • Globalization and its drivers • Modes of entry into international business	32-38
6.	**International Trade** • Theories of international trade • Government intervention in international trade • Tariff and non-tariff barriers • India's foreign trade policy	39-52
7.	**Foreign Direct Invesment** • Foreign direct investment (FDI) • Foreign portfolio investment (FPI) • Types of FDI • Costs and benefits of FDI to home and host countries • Trends in FDI • India's FDI policy	53-62
8.	**Balance of Payment** • Balance of payments (BOP) • Importance and components of BOP	63-65

9.	**Economic Integration** • Levels of Regional Economic Integration • Trade creation and diversion effects • Regional Trade Agreements: European Union (EU), ASEAN, SAARC, NAFTA	**66-72**
10.	**International Economic Integration** • IMF • World Bank • UNCTAD	**73-76**
11.	**World Trade Organisation** • Functions and objectives of WTO • Agriculture Agreement • GATS • TRIPS • TRIMS	**77-83**
12	**Multiple choice Question**	**84-97**

CHAPTER 1 : BUSINESS ENVIRONMENT

Business:

Business is an economic activity performed by business firms or organisations often with the objectives of maximising profit. This objective is supplemented by other objectives such as sales maximisation, growth maximisation, maximisation of market share, maximisation of own benefits by the managers, building up an image, and social responsibility. The economic activities performed by business organisations include production (transformation of inputs into outputs), distribution (supply of output in a marketplace) and sales (exchange of products with buyers for money).

Profit Maximisation:

Profit maximisation which is one of the main objectives of business organisations, requires maximisation of revenue. However, resources in the

hands of business organisations are limited. Therefore, firms face the challenge of allocating existing resources among alternative uses in such process of allocation and profit maximisation.

Business Environment and Its Components

The term **Business environment** refers to all those factors that are external to a business unit, but impact business decisions. The business environment is surrounded by the two components of environment, viz. Micro business environment and macro business environment.

TYPES OF ENVIRONMENT :

1. Micro Environment:

- The **micro business environment,** also known as **task environment**, refers to the immediate surroundings of the business. It not only affects the operations of the firm but also gets influenced by its decisions and actions.

- “The micro environment consists of the actors in the company’s immediate environment that affects the performance of the company. These include the suppliers, marketing intermediaries, competitors, customers and the public’s.”

1.Public:

It consists of all those parts of society which can directly or indirectly influence an organisation’s ability to achieve its objectives. Public opinion is important for a company as it can either strengthen or weaken its brand image. For example, satisfied customers are a public that spread good image about the products through word of mouth. On the contrary, activist, consumer forums, non-government agencies and even media protesting against the environmental damage done by a company is a public that can tarnish the image of a company, and weaken its brand image. Thus, managing public opinion is a crucial task for

any company.

2.<u>**Suppliers:**</u>

They are the agents who supply inputs, such as raw materials and intermediate goods to an organisation. They play an important role in operational efficiency. A delay in the supply of inputs can delay all the subsequent operations and the firm may fail in timely delivery of its products to customers, resulting in consumer dissatisfaction and even losing them forever. Therefore, managers need to assess the ability of suppliers for their ability to supply inputs in the required quantities in a given time frame.

3.<u>**Bankers and Financial Institutions:**</u>

Financial Intermediaries include bank insurance companies and credit agencies that help companies raise finance as well as insure against various types of risks involved in production and other business operations.

4.<u>Competitors:</u>

Competitors are rivals who compete with an organisation in the market place. Except monopoly market structure, firms in all other market structures have one or more competitors for their products. As the number of competitors increases the competition becomes intense. Competitors not only compete for customers but also for talented staff. To prevent customers and employees from shifting to
the competitors, a company needs to continuously assess consumer taste and preferences, and design the products accordingly. It also needs to design retention strategies so that the talented staff can be retained for a longer time.

5.<u>Market Intermediaries:</u>

Marketing Intermediaries consists of service agencies and financial intermediaries. **Service agencies** include marketing research and consultancy firms,

advertising agencies and media firms. These agencies help consumers identify the target population and market products in most efficient and influential manner.

6. **Consumers:**

Consumers comprise individuals and households that buy goods and services for personal consumption. Consumers are the most important constituents of the micro business environment as they are the demand side of the market. Without them companies cannot do their business ? Identifying customer needs, retaining customers, and extending products and services to them throughout their lives are important challenges for business organisations.

2. **Macro Environment :**

- **Macro business environment** refers to the general environment. It though influences business decisions, is not affected by the functioning of a business unit,

making it an uncontrollable factor.

- The macro environment consists larger societal forces that affect all the actors in the company's micro environment – namely, the demographic, economic, natural, technical, political and cultural forces."

<u>Social and Cultural Environment:</u>

Social and cultural factors in various countries of the globe affect the international business. These factors include attitude of the people to work, attitude to wealth, family, marriage, religion, education, ethics, human relations, social responsibilities etc.

Culture :

- Derived mostly from the climatic conditions of the geographical region and economic conditions of the country.
- A set of traditional beliefs and values which are transmitted and shared in a given society

 A total way of life and thinking patterns that are passed from generation to generation.

 Norms, customs, art, values etc.

Technological Environment:

 A given set of technologies available for the conduct of business determines the technological environment of business. Technology is the application of science, art and other fields of knowledge in various activities such as designing tools and equipments, producing goods and supplying services, communicating information and enhancing productivity.

 Technological advancements are driving force behind the global developments for centuries, but they are much more rapid in the present era, making the global environment highly dynamic and challenging.

Economic Environment:

Economic environment of a country is affected by the economic system, planning process, economic structure, business fluctuations, and trends in macroeconomic variables, economic policies and international economic environment. These various constituents of economic environment are detailed as follows:

a. **Economic System:**

- It is a set of institutions, principles and mechanisms created by a society to facilitate economic units to address their basic economic problems of allocation of scarce resources and perform their basic economic activities. Every organised society follows some or the other economic system.
- On the basis of ownership of resources, economic systems are classified into capitalism, socialism and mixed economies. Whereas on the basis of market mechanism, the systems are classified as market

economies, planned economies and mixed economies.

b. Planning Process:

Planning is needed for an efficient allocation of resources, which are limited in supply, among alternative uses. The planning process is an integral part of communist and socialist states. However, retaining their basic free market structure, even capitalist economies use planning to some extent. At present, all countries have mixed economic systems and follow planning, to a smaller or greater extent, to stimulate the level of investment, encourage technological innovations, use the resources as per national priorities and evolving economic situation, and reconcile the process of economic growth with the overall socioeconomic development of the country.

c. Economic Structure:

Economic System defines the institutional

framework, whereas economic structure defines the physical framework under which an economy and business units operate. The economic structure is determined by the factors such as total population size, per capita income, demographic profile, factor endowment, technological advancement, and is reflected in the sectoral composition of output and employment, fiscal, financial and trade structure, and population structure.

d. Business Fluctuations and Cycles:

Countries, world over, face wide cyclical fluctuations in output, prices, employment, and other macroeconomic variables due to the fluctuations in various components of aggregate demand and supply. Business fluctuations are recurrent, occur around a long-term growth and of short duration, but without a fixed periodicity. There are broadly three approaches – conventional business cycles, growth cycles and

growth rate cycles that are used for measuring these fluctuations.

Legal Environment / Political Environment:

The functioning of a company impacts its internal stakeholders such as shareholders, managers and workers as well as external stakeholders such as suppliers, consumers and the community at large. Different stakeholders have different interest in the working of an organisation. At times, these interests may conflict with each other. For example, textile industry, trying to maximize its profit, may not internalize the cost of pollution of the nearby water bodies where it's used chemicals are discharged. Such discharges may affect the livelihood of those who are dependent on marine life for their earnings. Hence, world over, the governments enact laws to resolve conflicting interests and minimise the harmful impacts of the functioning of companies.

ACCOUNTING AND AUDITING

(ALL IN ONE)

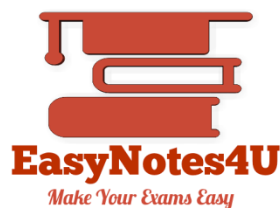
By

Dr. Gaurav Jangra

FOR COMMERCE AND MANAGEMENT

(BBA, B.COM, MBA, M.COM and UGC NET)

- *FINANCIAL ACCOUNTING*
- *PARTNERSHIP ACCOUNTING*
- *CORPORATE ACCOUNTING*
- *MANAGEMENT ACCOUNTING*
- *COST ACCOUNTING*
- *AUDITING*



www.easynotes4u.com

+91-8814931483

Preface

The book ***Accounting and Auditing*** has been written afresh and covered all area of accounting i.e. ***Financial Accounting, Corporate Accounting, Partnership Accounting, Cost and Management Accounting and Auditing and whole syllabus of Unit 2: Accounting and Auditing for UGC NET Commerce*** as per new syllabus 2019. The whole syllabus is divided into different units. Each unit covered all contents /topics in details in order to meet the requirement of almost all universities Syllabus. Several new Concepts and Multi Choice Questions taken as per according to latest examination pattern have been Incorporated as latest practical problems and MCQs with explanation at the end of each unit.

I have made every effort every effort to remove the printing errors from the book. Even then if the readers come across any error they are requested to point out the same to me, I am confident that this book will be very useful for Commerce, Management and UGC NET Aspirants.

Constructive criticism and suggestions for improvement of the book are most welcome.

Dr. Gaurav Jangra

Assistant Professor

Om Sterling Global University

Hisar, Haryana

Acknowledgement

First of all, I would like to thank my family. The constant inspiration and guidance kept me focused and motivated. I am grateful to my father for giving me the life I ever dreamt. I can’t express my gratitude for my Mom in words, whose unconditional love has been my greatest strength. I also express my gratitude for my wife Monika Jangra to help me in editing and formatting the book.

I am also thankful to Dr. Rajneesh Ahlawat, Assistant professor, Department of Business Administration, Chaudhary Devi Lal University, Sirsa for his inspiring guidance and support during writing this book. I express my thanks to Dr. Zafar Zahir, Managing Director, Synetic Business School Ludhiana to give some valuable remarks and suggestions for my book. I am also very thankful to Dr. Ajaipal Sharma, Assistant Professor, Central University of Haryana, Mahendergarh for his motivation and inspiration

I would like to acknowledge the special thanks to all faculty members of Synetic Business School Ludhiana and my colleagues to help me directly or indirectly.

Dr. Gaurav Jangra

Assistant Professor

Om Sterling Global University

Hisar, Haryana

Author's Biography

***Dr. Gaurav Jangra** is Graduate in Business Administration from Maharishi Dayanand University, Rohtak and Post Graduation is also in Business Administration from Central University of Haryana, Mahendergarh with first division, M.Com. from Guru Jambheshwar University of Science and Technology, Hisar. He completed his Doctorate at Department of Business Administration, Chaudhary Devi Lal University Sirsa. He qualified UGC NET and JRF in Management and UGC NET in Commerce. He is currently working as Head of Department, Commerce and Management at Synetic Business School, Ludhiana, Punjab. He has been gaining satisfaction from his profession of teaching and research for more than five years. He published more than a fifteen quality research papers in reputed National and International refereed journals related to finance, marketing and Information Technology. He is attended and contributed in more than twenty Seminars, Workshops, and Conferences. He already published two edited book volumes and UGC NET paper 1 book. Apart from teaching and research he is well expert in Website Designing. His area of specialization is Finance, Marketing and Information Technology. Currently he also maintaining and providing online education for UGC NET Aspirants through his website www.easynotes4u.com and Android Apps "EasyNotes4U and UGC NET eBooks" on Google Play Store*

	CONTENTS	
Chapters	**Titles**	**Page Nos.**
1	**Basic accounting principles:** Concepts and Postulates	**1-6**
2	**Partnership Accounts:** Admission, Retirement, Death, Dissolution and Insolvency of partnership firms	**7-14**
3	**Corporate Accounting:** Issue, forfeiture and reissue of shares	**15-20**
4	**Liquidation of companies:** Acquisition, merger, amalgamation and reconstruction of companies	**21-28**
5	**Holding Company Accounts**	**29-31**
6	**Cost and Management Accounting:** Marginal costing and Break-even analysis	**32-36**
7	**Standard Costing**	**37-60**
8	**Budgetary Control**	**61-69**
9	**Process Costing**	**70-81**
10	**Activity Based Costing (ABC)**	**82-86**
11	**Costing for Decision Making**	**87-89**
12	**Life Cycle Costing and Target Costing**	**90-92**
13	**Kaizen Costing and JIT**	**93-96**
14	**Financial Statement Analysis:** Horizontal and Vertical and Ratio Analysis	**97-104**
15	**Fund Flow and Cash Flow Statement Analysis**	**105-114**
16	**Human Resource and Social Accounting**	**115-123**
17	**Inflation and Environmental Accounting**	**124-130**
18	**Indian Accounting Standards and IFRS**	**131-141**
19	**Auditing:** Independent financial audit; Vouching; Verification ad valuation of assets and liabilities; Audit of financial statements and audit report; Cost audit	**142-156**
20	**Recent Trends in Auditing** Management audit; Energy audit; Environment audit; Systems audit;	**157-168**

	Safety audit	
	MCQs	**169-186**

CHAPTER 1: BASIC ACCOUNTING PRINCIPLES

Accounting

"Accounting is the art of recording, classifying and summarizing in significant manner and in terms of money, transactions and events which are in part, at least of a financial character and interpreting the result thereof".

Accounting Principles:

There are general rules and concepts that govern the field of accounting. These general rules–referred to as basic accounting **principles and guidelines**–form the groundwork on which more detailed, complicated, and legalistic accounting rules are based. For example, the Financial Accounting Standards Board (FASB) uses the basic accounting principles and guidelines as a basis for their own detailed and comprehensive set of accounting rules and standards.

The phrase "generally accepted accounting principles" (or "GAAP") consists of three important sets of rules: (1) the basic accounting principles and guidelines, (2) the detailed rules and standards issued by FASB and its predecessor the Accounting Principles Board (APB), and (3) the generally accepted industry practices.

If a company distributes its financial statements to the public, it is required to follow generally accepted accounting principles in the preparation of those statements. Further, if a company's stock is publicly traded, federal law requires the company's financial statements be audited by independent public accountants. Both the company's management and the independent accountants must certify that the financial statements and the

related notes to the financial statements have been prepared in accordance with GAAP.

GAAP is exceedingly useful because it attempts to standardize and regulate accounting definitions, assumptions, and methods. Because of generally accepted accounting principles we are able to assume that there is consistency from year to year in the methods used to prepare a company's financial statements. And although variations may exist, we can make reasonably confident conclusions when comparing one company to another, or comparing one company's financial statistics to the statistics for its industry. Over the years the generally accepted accounting principles have become more complex because financial transactions have become more complex.

Accounting Principles Definition:

Accounting principles are uniform practices which entities follow to record, prepare and present financial statements. An entity must prepare its financial statements as per acceptable accounting principles in order to present true and fair view of state of affairs of entity.

In India, general accounting principles are accounting standards and Indian Accounting Standards.

Uniform accounting principles assist in comparison of financial statement of entities. If accounting principles followed are same then reader of financial statements can compare financial results of two entities. However, if separate entities follow different accounting principles, they should at first prepare financials as per same accounting principles and then reader should make a comparison.

Benefits of accounting principles given in Accounting Standards or Indian Accounting Standards (Ind AS):

Accounting principles given in Accounting Standards (AS) and Indian Accounting Standards (Ind AS) are of great importance as it provides the basis for:

1. Recognition of an item as income, expense, asset or liability
2. At what amount it shall be recognised in the books of accounts and
3. How to present these items in statement of P and L or Balance sheet
4. It also provides what all disclosures are required to be made with respect to the items recognised.

Accounting principles guide entities on preparation and presentation of financial statements. It reduces the inconsistencies, presents true and fair view of state of affairs and makes comparison easier.

Accounting Principles are different from accounting policies:

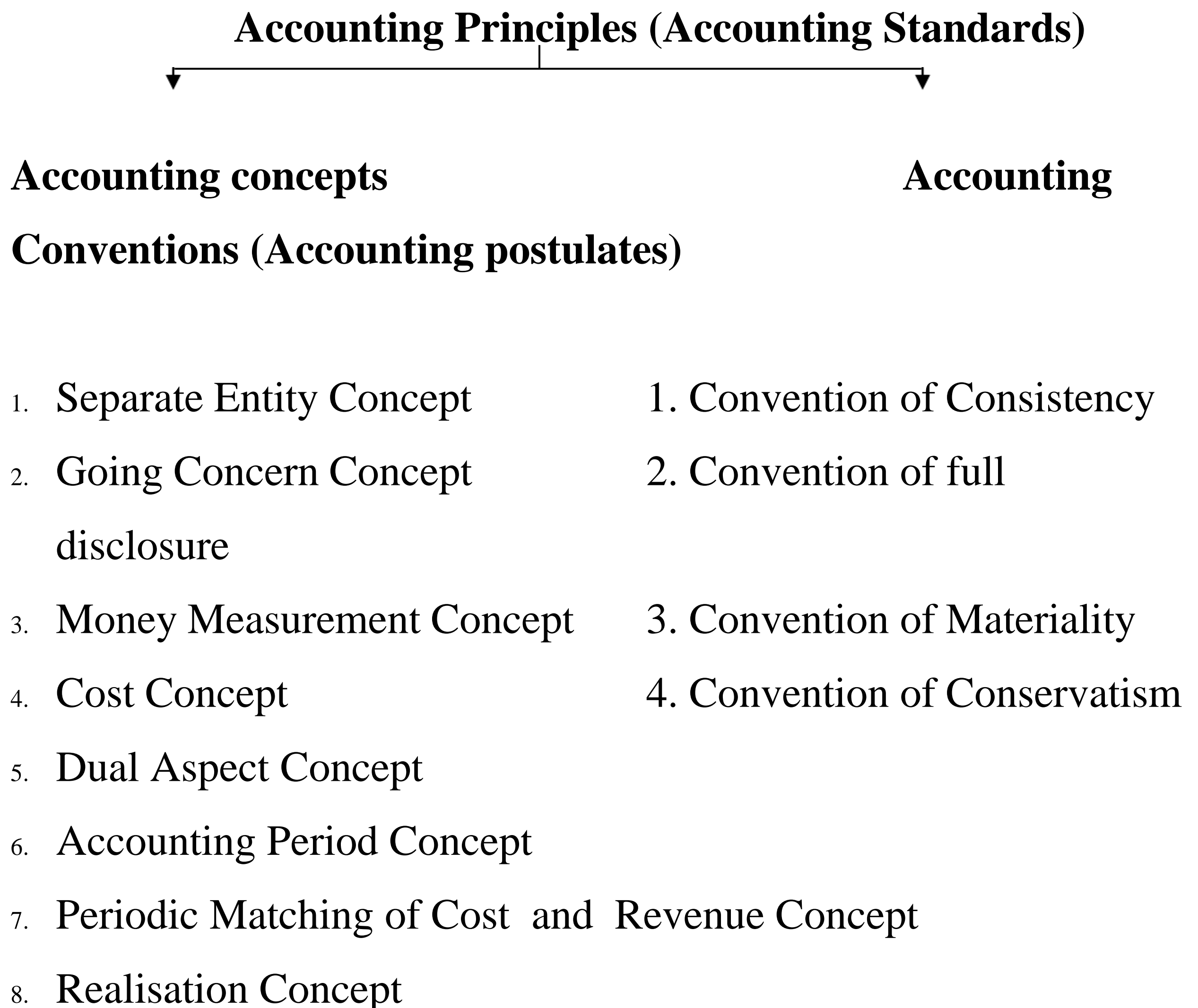
Accounting principles are different from accounting policies. Per se, accounting principles are broader than accounting policies. Accounting principle has been defined above. Accounting policies are accounting principles used in preparing, presenting and disclosing one specific item.

For instance, depreciation is an accounting principle of amortising the amount of tangible asset. Now depreciation can be charged by Straight Line Method (SLM), Written Down Value (WDV) method, etc. Depreciation of tangible asset is an accounting principle whereas following SLM method for depreciation is an accounting policy.

An entity incurred an expense on purchase of a machinery, whose benefit entity will have for the next 5 years. In such case, entire expense

should not be charged in the first year, it will be matched with the benefits derived from such asset over 5 years. Now, entity can either follow a policy to charge depreciation at Straight Line Method (SLM) or Written Down Vale (WDV). If entity's benefits flow in a straight line it can charge depreciation in a SLM. But, if the benefits will be higher in the starting years, entity can charge depreciation using the WDV method.

Accounting principles are the basis on which financial statements are prepared. Uniformity in accounting principles is a key for a reader to read and compare financial statements of two entities.



Accounting Concepts

SUBJECT:
UGC NET COMMERCE

UNIT – 3:
BUSINESS ECONOMICS

Contents

CHAPTER	TITLE	PAGE NO.
1	**Meaning and scope of business economics**	**3-6**
2	**Objectives of business firms**	**7-13**
3	**Demand analysis:** Law of demand; Elasticity of demand and its measurement; Relationship between AR and MR	**14-23**
4	**Consumer behavior:** Utility analysis; Indifference curve analysis	**24-32**
5	**Law of Variable Proportions: Law of Returns to Scale**	**33-42**
6	**Theory of cost:** Short-run and long-run cost curves	**43-49**
7	**Price determination under different market forms:** Perfect competition; Monopolistic competition; Oligopoly- Price leadership model; Monopoly; Price discrimination	**50-69**
8	**Pricing strategies:** Price skimming; Price penetration; Peak load pricing	**70-79**
	MCQs	**80-82**

CHAPTER-1: MEANING AND SCOPE OF BUSINESS ECONOMICS

Meaning:

Managerial economics or business economics is economics applied in decision-making. Business economics, thus, interweaves economic principles and business. Business managers apply economic laws and principles while presenting business problems and their ways of solutions. Thus, business economics can be defined as the application of economic analysis to business problems faced by an enterprise. It provides a link between economic theory and the decision sciences in the analysis of managerial decision-making. It relies heavily on traditional economics and decision sciences.

Definition of Business Economics:

The teaching of economics is, thus, an abstract theorization with little connection to business.

But theoretical models of economics are to be applied in business areas. Once theoretical models of economics are applied in business, the gap between economics and business gets minimized.

The branch of managerial economics or business economics has established links between business and economics.

Business economics is, thus, an applied economics. Economics is the study of human beings (e.g., consumers, firms) in producing and consuming goods and services in the midst of scarcity of resources. Managerial or business economics is an applied branch of organising and allocating a firm’s scarce resources to achieve its desired goals.

Identification of the problems and the solving of the problems are the two crucial elements of decision-making of a business firm. Business economists help business managers in making sound business decisions. Business success, in fact,

greatly depends on appropriate business decisions. However, appropriate decision-making is not an easy job in this changing world.

On the basis of past knowledge and experience, business managers take business decisions and make future plans. But decision-makers are constrained by the 'uncertainty' of the real world where changes occur either in a hidden way or in an open way. In this changing but uncertain world, an accurate decision-making is impossible even if talents of top quality business economists are employed.

It is due to this uncertainty, prediction or estimation relating to the volume of sales of a product, cost of production, profit, etc., is more likely to be imperfect. In other words, against the backdrop of uncertainty and a changing world, business managers will have to anticipate changes so that the impact of unfavorable situations becomes insignificant. Thus, business decision-making is an art.

Cultivation of this art is made through economic principles. In this sense, managerial economics is an applied economics. It is concerned with the application of economic concepts and analytical tools to the process of decision-making of a business enterprise.

Thus, managerial economics or business economics is a 'special branch of economics that bridges the gap between abstract economic theory and managerial practice. Through a process of application of the principles, concepts and tools of economics to solve the managerial problems of a business enterprise, business economists have greatly minimised the problem of uncertainty arising in business.

An Illustration of the Relationship between Economic Theory and Business— Machlup's Overtaking Analogy

The application field of economic theory is popularly known as business economics or managerial economics. Can economic theory be applied in business practice efficiently? Fritz Machlup, in answering this question, gave an analogy

between the behaviour of a motorist deciding whether or not to overtake on a two-lane highway and the behaviour of a profit- maximising firm. Overtaking decision of the motorist involves construction of a very complex set of equations.

While overtaking, the motorist must have a knowledge about the weight, power, speed of the vehicle being driven, the condition of the road, weather, information about the number of vehicles plying on the highway, and a set of assumptions about the behaviour and objectives of other drivers. Unfortunately, even the most expert and cautious drivers do not have all these information.

But the model-builder makes such unrealistic assumptions. Under the circumstance, the decision of overtaking in a two- lane highway seems to be next to impossible. In reality, all the drivers overtake dozens of times every day. Such overtaking decisions are deemed to be 'correct' only if accidents are not met with.

If we compare this behavioural overtaking decision of a motorist with that of the behaviour of a profit- maximising firm, we will reach the same conclusion. A profit-maximising firm assumes that it has perfect information about costs and revenue conditions. But that too is an unrealistic assumption.

Still they assume such and are always guided by profit-maximising motive. "Like the driver taking-the decision to overtake, managers 'behave' as if they had the relevant information, in which case they will behave like the profit- maximising model and that model will be a good predictor of their behaviour. "

Characteristics of Business Economics:

Business economics is essentially concerned with the various decisions of a business enterprise. The unit of study of business economics is the firm. Thus, managerial economics studies decision-making behaviour of a firm or an industry. Microeconomics takes into account the behaviour of smaller economic agents, such as a firm or a consumer or an input owner.

It deals with the operation of a consumer, a firm involving the determination of price of a commodity, revenue, costs and, hence, profit levels, etc. Managerial economics is, thus, essentially microeconomic in character as it has its origin in theoretical microeconomics. Profs. H. C. Petersen and W. C. Lewis suggest that managerial economics should be thought of as applied microeconomics.

- It is an application of that part of microeconomics focusing on those topics which are of great interest and importance to business managers. These topics include theories of demand, production and cost, profit-maximizing model of the firm, optimal prices and advertising expenditures, government regulation, etc. Managerial economics is concerned with finding optimal solutions to business decision problems.

- Secondly, economic concepts and principles of the 'theory of firm' are employed in business economics. Thus, in business economics, the main emphasis is given upon the firm, the environment in which the firm finds itself, and the business decision which firms have to take. In this sense, managerial economics is narrower in scope than pure economic theory.
- Thirdly, broadly there are two main branches of economics—'positive' economics and 'normative' economics. Positive economics deals with 'description' while normative economics deals with 'prescription'. By building up propositions on the basis of a set of assumptions, positive economics tries to explain economic phenomenon.

Normative economics comments on the desirability of that phenomenon and suggests policy measures. Value judgments are, thus, pronounced in normative economics. In the words of Profs. Mote, Paul and Gupta: "Managerial economics is a part of normative economics as its focus is more on prescribing choice and action and less on explaining what has happened.

Managerial economics draws on positive economics by utilizing the relevant theories as a basis for prescribing choices."

- Fourthly, business economics not only seeks to investigate and analyse how and why businesses behave as they do but also the implications of their actions and policies for the industry in which they operate and, finally, for the economy as a whole. In this business environment, both internal and external factors work.

Business economics seeks to analyse various internal and external constraints that businesses experience in their process of growth and survival, draw conclusions as to how and why businesses behave as they do. "Business economics therefore focuses on the issues relevant to a business and its operations, and to the business environment." Thus, business economics is considered as applied economics. It casts away abstract economic theories. Managerial economists look at practical applications of theoretical models.

- Finally, business economics is essentially microeconomic in character. In other words, macroeconomic theory has less relevance for managerial economics. Truly speaking, business economics should also deal with a wider environment—the macro-economy. Macro-economics is concerned with the behaviour of the economic system in totality. It studies the determination of aggregate national income, level of employment, general price level, the international balance of payments, etc.

It is true that aggregating economic trends or external economic factors do not directly affect business decisions of a firm. But what is true is that changing macro-economy not only influences aggregate or national income but also the demand for the product of a business firm. Efficient business managers must have awareness as well as keenness of studying and explaining macro-

economic environment. In this sense, business economics cannot be devoid of macroeconomics.

Subject-Matter and Scope of Business Economics:

We know that managerial economics or business economics is applied microeconomics employed for the purpose of facilitating decision--making and forward planning. As far as decision--making and forward planning are concerned, one has to face the following problems:

Problem of resource allocation seems to be a pressing problem for any organization. Resources are not plentiful. A firm has to organize scarce resources efficiently so that optimal outcomes are obtained. Such resource allocation problem includes production programming, transportation problem, etc. Non-optimal organization of resources may spell disaster to any organization.

Inventory and queuing are important problems to any firm. A firm has to hold an optimal level of stocks of raw materials and finished product so that business uncertainties can be minimized. Business managers must decide an optimal level of inventories. Such decisions are taken by firms after considering demand and supply conditions.

Since forward planning by management is essential, a firm must make decisions—whether new machines are to be installed or more professionals are to be employed. As most of the decisions cannot be implemented simultaneously, the firm manager must make a trade-off between decisions. Taking a particular decision out of a variety of decisions is known as queuing problem. A manager places or queues alternative decisions and picks up a right one. Price fixation is another interrelated problem connected with decision-making. A firm has to take up a right pricing decision.

Finally, the decision-maker faces investment problems for a variety of reasons. Truly speaking, any forward planning by management involves investment problems which are by nature knotty. Investment problems boil down to the

problems of allocating resources over time. A firm has to make decision about the volume of investment. It must decide where to invest, when to invest. It must know the sources of funds, etc.

Anyway, business economics is concerned with decision-making and forward planning.

The scope of business economics (both micro and macro variety) is a wider one since it "uses the logic of Economics, Mathematics and Statistics to provide effective ways of thinking about business decision problems." In view of this saying of Prof. D. C. Hague, we can argue that there are links between managerial economics and management science. In fact, the boundaries between the two subjects are not clear-cut but overlapping.

Managerial economics is largely an applied branch of microeconomics. Its macroeconomic content is not to be belittled. It uses the methods and techniques of microeconomics mostly in the field of management. As Haynes and William Warren state: "The relation of managerial economics to economic theory (of either the micro or macro variety) is much like that of engineering to physics, or of medicine to biology or bacteriology. It is the relation of an applied field to the more fundamental but more abstract basic discipline from which it borrows concepts and analytical tools."

It is to be pointed out here that measurement without theory may lead to false precision and diagnosis while theory without measurement can hardly be operationally useful. Now we are in a position to explain the scope of business economics. By scope of (business) economics we mean the field of the subject, the boundaries that delimit and delineate the topics to be addressed.

Determination of the scope of the subject includes:

(i) Definition of the subject,

(ii) Subject matter of business economics,

(iii) Is business economics a positive or a normative science?

Since business economics is thought of as applied microeconomics, the scope of business economics includes:

i. Analysis, estimation and forecasting of consumer demand for a product;

ii. Analysis of cost and output;

iii. Determination of price of a commodity, work policy and business strategies of a business enterprise;

iv. Long-run planning decisions of a firm that studies capital budgeting and capital management.

Managerial economics now includes 'operations research'—a mathematical technique to solve business problems.

Finally, we must say that there is a great deal of linkages between managerial economics and other disciplines and fields of study. It uses the logic of economics, mathematics and statistics. Managerial economics is related to management science or the decision sciences. Management science is concerned with techniques for improvement of decision-making.

Business economics is related to accounting. Accounting is essentially concerned with recording and analysing the financial activities of a business firm. To quote Prof. D. C. Hague: "The main task of management accounting is now seen as being to provide the sort of data which managers need if they are to apply the idea of managerial economics to solve business problems correctly; accounting data are also to be provided in a form so as to fit easily into the concepts and analysis of managerial economics."

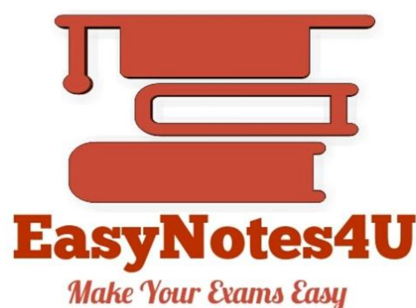
In view of the relationship between managerial economics and other disciplines, it may be called an art, and not a science. Though an art, decision-making in this uncertain world has become more perfect. Better choices, better prediction, etc., are likely to emerge because of the interaction among basic disciplines.

Thus, it is clear from the above discussion that managerial or business economics helps managers of firms, administrators of non-profit and profit-making hospitals,

SUBJECT:
COMMERCE (08)

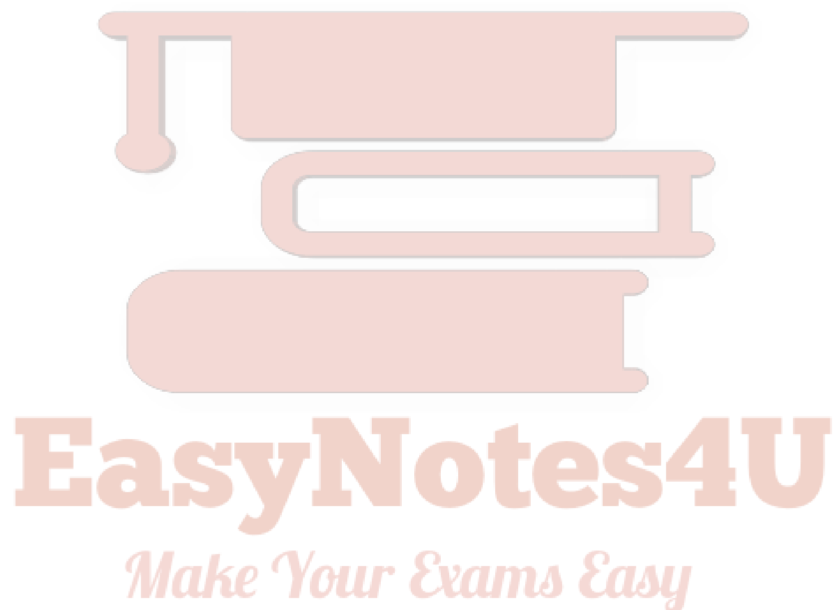
UNIT – 4:
BUSINESS FINANCE

By
Ms. Aksha Memon
Principal, Mindopedia Academy
M.COM(Accountancy), NET, PGDFM, C.S Inter.
Former employee at Clara's college of Commerce
Working as a Visiting faculty for Graduate courses Narsee Monjee college of Commerce
Working as a Visitiong faculty for P.G courses Valia College of Commerce



Website: www.easynotes4u.com
Email: support@easynotes4u.com
Contact: +91-8814931483

Chapter No.	Title	Page No.
1	Scope and Sources of Finance	3-9
2	Lease Financing	10-15
3	Cost of Capital and Time Value of Money	16-21
4	Capital Structure	22-23
5	Capital Budgeting Decisions	24-29
6	Working Capital Management	30-35
7	Dividend Decisions: Theories and Policies	36-39
8	Assets Securitization	40-42
9	International Monetary System	43-53
10	Foreign Exchange Market	54-66
11	International Money Market Instruments	67-74
12	International Arbitrage	75-80
13	Multinational Capital Budgeting	81-83
	MCQs	84-92



CHAPTER 1: SCOPE AND SOURCES OF FINANCE

Financial Management is the art and science of managing money. Financial Management is basically concerned with the duties of the financial managers in the business firm. In the words of **Howard and Upton:** ***Financial management "as an application of general managerial principles to the area of financial decision-making.*** Financial Management is an essential part of the economic and non economic activities which leads to decide the efficient procurement and utilization of finance with profitable manner. In the olden days the subject Financial Management was a part of accountancy with the traditional approaches. Now a days it has been enlarged with innovative and multi dimensional functions in the field of business with the effect of industrialization, Financial Management has become a vital part of the business concern and they are concentrating more in the field of Financial Management. Financial Management also developed as corporate finance, business finance, financial economics, financial mathematics and financial engineering.

Business concern needs finance to meet their requirements in the economic world. Any kind of business activity depends on the finance. Hence, it is called as lifeblood of business organization. Whether the business concerns are big or small, they need finance to fulfil their business activities.

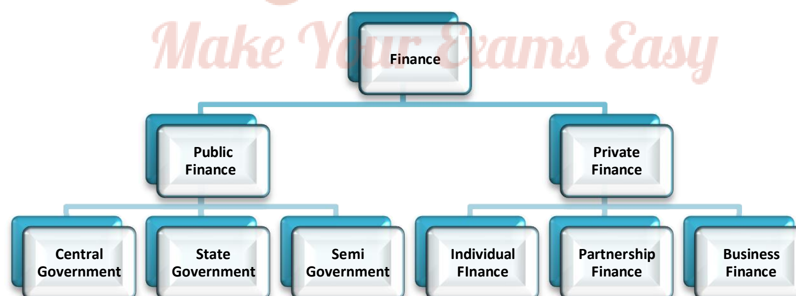
In the modern world, all the activities are concerned with the economic activities and very particular to earning profit through any venture or activities. The entire business activities are directly related with making profit. (According to the economics concept of factors of production, rent given to landlord, wage given to labour, interest given to capital and profit given to shareholders or proprietors), a business concern needs finance to meet all the requirements. Hence finance may be called as capital, investment, fund etc. but main aim of any kind of economic activity.

According to Oxford dictionary, the word 'finance' connotes 'management of money'. ***Webster's Ninth New Collegiate Dictionary defines finance as "the Science on study of the management of funds' and the management of fund as the system that includes the circulation of money, the granting of credit, the making of investments, and the provision of banking facilities.***

According to the Guthumann and Dougall, ***"Business finance can broadly be defined as the activity concerned with planning, raising, controlling, administering of the funds used in the business".***

Finance is one of the important and integral part of business concerns, hence, it plays a major role in every part of the business activities. It is used in all the area of the activities under the different names. Finance can be classified into two major parts:

EasyNotes4U
Make Your Exams Easy



SCOPE OF FINANCIAL MANAGEMENT

Financial management is one of the important parts of overall management, which is directly related with various functional departments like personnel, marketing and production. Financial management covers wide area with multidimensional approaches. The following are the important scope of financial management.

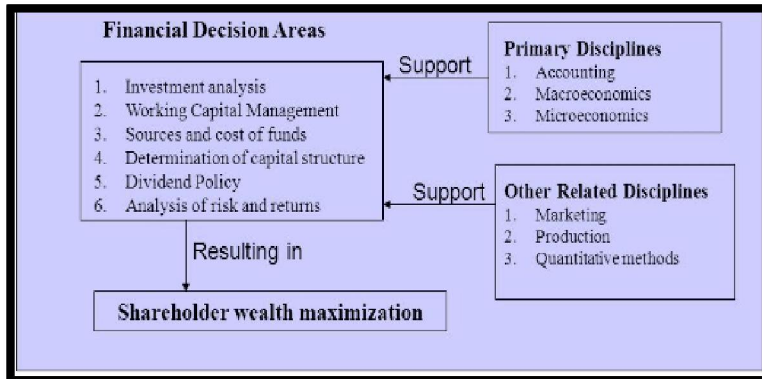
1. Financial Management and Economics
2. Financial Management and Accounting
3. Financial Management or Mathematics
4. Financial Management and Production Management
5. Financial Management and Marketing

6. Financial Management and Human Resource

OBJECTIVES OF FINANCIAL MANAGEMENT

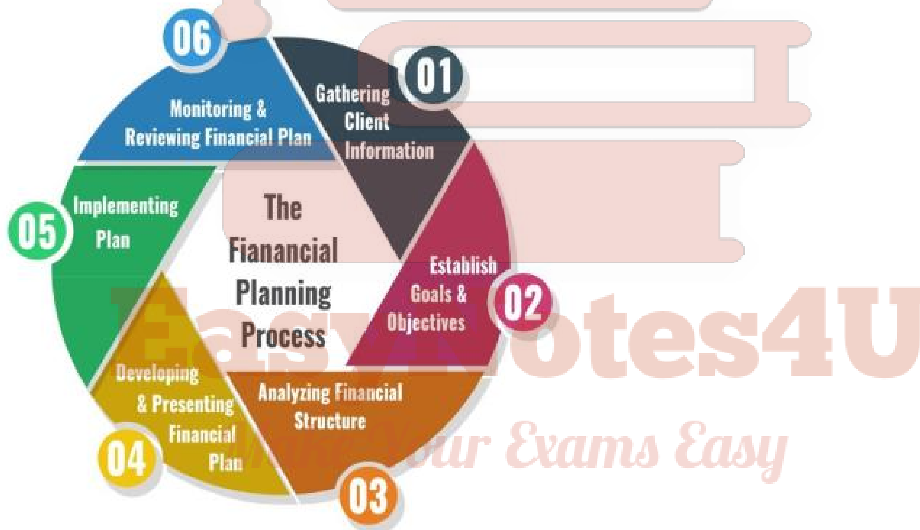
Effective procurement and efficient use of finance lead to proper utilization of the finance by the business concern. It is the essential part of the financial manager. Hence, the financial manager must determine the basic objectives of the financial management. Objectives of Financial Management may be broadly divided into two parts such as:

1. Profit maximization
2. Wealth maximization.



Finance Planning

In the planning phase, finance needs to get a clear perspective on certain aspects, essentially the finance of the company has to be decided on questions like, what are the sources of finance, how much finance is required by the company and will the company be profitable.



.

1) Raising Capital

Making capital investments is perhaps one of the most important tasks of corporate finance, which has serious business implications. To raise the finance, the corporate finance has to raise money from the company with the assistance of sources like shares, debentures, banks, financial institutions, creditors etc.., a company may also choose to sell stocks to equity while raising long-term funds for business expansion. Capital financing is a very delicate balancing act. Corporate finance is also supposed to manage short-term financial management with a goal to have enough liquidity to carry out other operations of the organisation.

2) Investing Capital

There are two types of corporate finance, fixed capital and working capital. As the name suggests fixed capital is used to purchase fixed assets like land, building, property, machinery, etc. while working capital is generally used to purchase raw material and manage day to day fixed expenses like overheads, salaries etc. Financing and investing decisions are like two sides to the same coin. The organisation raises finances only when they have suitable projects. In corporate finance there are various tools and techniques which help take appropriate informed investing decisions, hence it is very vital for the financial health of an organisation.

3) Monitoring the Finance / Managing Risks

Monitoring finance is a science, there is a method to it, it is a very complex job. It requires many tools and techniques. Corporate finance has to control and manage the finance of the company, they have to minimise the risk of investment and at the same time assure maximum returns on the invested capital

The finance function is concerned with three types of decisions:

1) Financing decisions are the decisions regarding the process of raising funds.
2) Investment decisions are the decisions regarding the investment of funds.
3) Dividend Policy decisions are strategic financial decisions and they are based on the profits earned by the organization. As the shareholders are the owners of the organization thus they are entitled to receive profits in the form of dividend.

So to conclude, finance is the bloodline of any business, it is required in all kinds of setups, big or small, it is required across all phases in the lifecycle of an organisation, to initiate, build stability, survival, and also in the growth of an organisation. Promotional finance is required to start a company, long-term finance is required to build assets, and development finance is required for growth, expansion and diversification of a business.

SOURCES OF FINANCE

Sources of finance mean the ways for mobilizing various terms of finance to the industrial concern. Sources of finance state that, how the companies are mobilizing finance for their requirements. The companies belong to the existing or the new which need sum amount of finance to meet the long-term and short-term requirements such as purchasing of fixed assets, construction of office building, purchase of raw materials and day-to-day expenses. Sources of finance may be classified under various categories according to the following important heads:

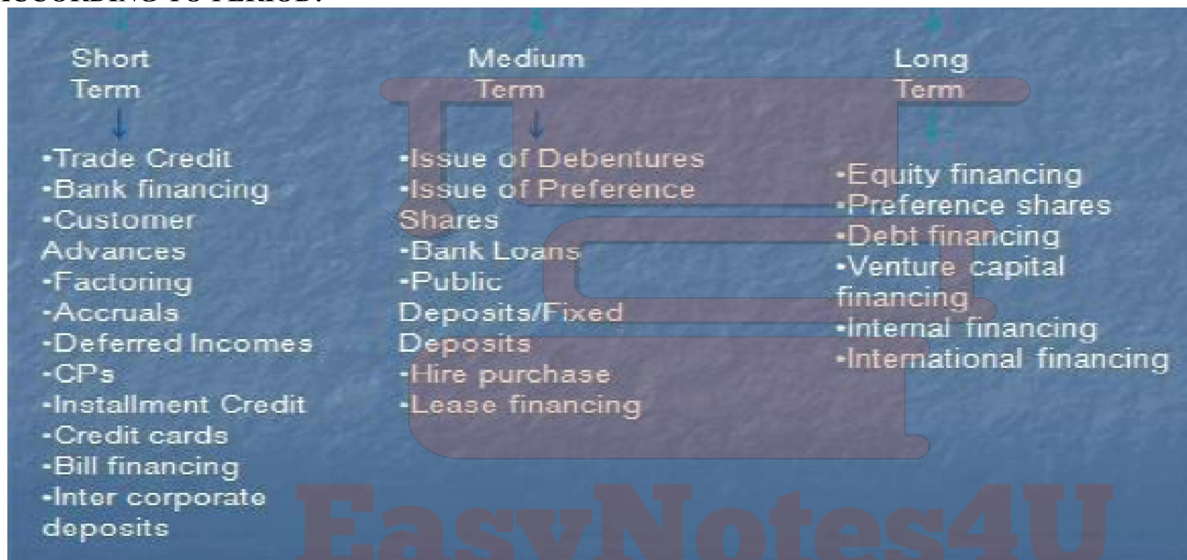
According to Ownership

Owned Capital- Share Capital, Retained Earnings, Profit Surplus etc Borrowed Capital- Debentures, Bonds, Public Deposit, loans.

According to source of Finance

External- Shares, Debentures, Public Deposit, loans etc. Internal- Retained Earnings, Profit Surplus ploughing back of profits, depreciation fund etc

ACCORDING TO PERIOD:



EasyNotes4U
Make Your Exams Easy

I. LONG TERM SECURITY FINANCE

If the finance is mobilized through issue of securities such as shares and debenture, it is called as security finance. It is also called as corporate securities. This type of finance plays a major role in the field of deciding the capital structure of the company.

Characters of Security Finance Security finance consists of the following important characters:

1. Long-term sources of finance.
2. It is also called as corporate securities.
3. Security finance includes both shares and debentures.
4. It plays a major role in deciding the capital structure of the company.
5. Repayment of finance is very limited.
6. It is a major part of the company's total capitalization.

Types of Security Finance Security finance may be divided into two major types:

1. Ownership securities or capital stock.
2. Creditor ship securities or debt capital.

OWNERSHIP SECURITIES The ownership securities also called as capital stock is commonly called as shares. Shares are the most Universal method of raising finance for the business concern. Ownership capital consists of the following types of securities.

● Equity Shares
● Preference Shares
● No par stock
● Deferred Shares

EQUITY SHARES

Equity Shares also known as ordinary shares, which means, other than preference shares. Equity shareholders are the real owners of the company. They have a control over the management of the company. Equity shareholders are eligible to get dividend if the company earns profit. Equity share capital cannot be redeemed during the lifetime of the company. The liability of the equity shareholders is the value of unpaid value of shares.

FEATURES OF EQUITY SHARES Equity shares consist of the following important features:

1. **Maturity of the shares:** Equity shares have permanent nature of capital, which has no maturity period. It cannot be redeemed during the lifetime of the company.
2. **Residual claim on income:** Equity shareholders have the right to get income left after paying fixed rate of dividend to preference shareholder. The earnings or the income available to the shareholders is equal to the profit after tax minus preference dividend.
3. **Residual claims on assets:** If the company wound up, the ordinary or equity shareholders have the right to get the claims on assets. These rights are only available to the equity shareholders.
4. **Right to control:** Equity shareholders are the real owners of the company. Hence, they have power to control the management of the company and they have power to take any decision regarding the business operation.
5. **Voting rights:** Equity shareholders have voting rights in the meeting of the company with the help of voting right power; they can change or remove any decision of the business concern. Equity shareholders only have voting rights in the company meeting and also they can nominate proxy to participate and vote in the meeting instead of the shareholder.
6. **Pre-emptive right:** Equity shareholder pre-emptive rights. The pre-emptive right is the legal right of the existing shareholders. It is attested by the company in the first opportunity to purchase additional equity shares in proportion to their current holding capacity.
7. **Limited liability:** Equity shareholders are having only limited liability to the value of shares they have purchased. If the shareholders are having fully paid up shares, they have no liability.

For example: If the shareholder purchased 100 shares with the face value of Rs. 10 each. He paid only Rs. 900. His liability is only Rs. 100. Total number of shares 100 Face value of shares Rs. 10 Total value of shares 100 × 10 = 1,000 Paid up value of shares 900 Unpaid value/liability 100

Liability of the shareholders is only unpaid value of the share (that is Rs. 100).

PREFERENCE SHARES

The parts of corporate securities are called as preference shares. It is the shares, which have preferential right to get dividend and get back the initial investment at the time of winding up of the company. Preference shareholders are eligible to get fixed rate of dividend and they do not have voting rights. It means a preference shareholder enjoys two rights over equity shareholders :(a) right to receive fixed rate of dividend and (b) right to return of capital. After settling the claims of outsiders, preference shareholders are the first to get their dividend and then the balance will go to the equity shareholders. However, the preference shareholders do not have any voting rights in the annual general body meetings of the company. Preference shares may be classified into the following major types:

1. **Cumulative preference shares**: Cumulative preference shares have right to claim dividends for those years which have no profits. If the company is unable to earn profit in any one or more years, C.P. Shares are unable to get any dividend but they have right to get the comparative dividend for the previous years if the company earned profit
2. **Non-cumulative preference shares:** Non-cumulative preference shares have no right to enjoy the above benefits. They are eligible to get only dividend if the company earns profit during the years. Otherwise, they cannot claim any dividend.
3. **Redeemable preference shares:** When, the preference shares have a fixed maturity period it becomes redeemable preference shares. It can be redeemable during the lifetime of the company. The Company Act has provided certain restrictions on the return of the redeemable preference shares.
4. **Irredeemable Preference Shares:** Irredeemable preference shares can be redeemed only when the company goes for liquidator. There is no fixed maturity period for such kind of preference shares.
5. **Participating Preference Shares** Participating preference shareholders have right to participate extra profits after distributing the equity shareholders.
6. **Non-Participating Preference Shares** Non-participating preference shareholders are not having any right to participate extra profits after distributing to the equity shareholders. Fixed rate of dividend is payable to the type of shareholders.
7. **Convertible Preference Shares** Convertible preference shareholders have right to convert their holding into equity shares after a specific period. The articles of association must authorize the right of conversion.
8. **Non-convertible Preference Shares** There shares, cannot be converted into equity shares from preference shares.

FEATURES OF PREFERENCE SHARES

1. **Maturity period:** Normally preference shares have no fixed maturity period except in the case of redeemable preference shares. Preference shares can be redeemable only at the time of the company liquidation.
2. **Residual claims on income:** Preferential shareholders have a residual claim on income. Fixed rate of dividend is payable to the preference shareholders.
3. **Residual claims on assets:** The first preference is given to the preference shareholders at the time of liquidation. If any extra Assets are available that should be distributed to equity shareholder.
4. **Control of Management:** Preference shareholder does not have any voting rights. Hence, they cannot have control over the management of the company.

DEFERRED SHARES

Deferred shares also called as founder shares because these shares were normally issued to founders. The shareholders have a preferential right to get dividend before the preference shares and equity shares. According to Companies Act 1956 no public limited company or which is a subsidiary of a public company can issue deferred shares. These shares were issued to the founder at small denomination to control over the management by the virtue of their voting rights.

NO PAR SHARES

When the shares are having no face value, it is said to be no par shares. The company issues this kind of shares which is divided into a number of specific shares without any specific denomination. The value of shares can be measured by dividing the real net worth of the company with the total number of shares. Value of no. per share

EasyNotes4U Make Your Exams Easy

=the realnetworth/Total no. Of shares

CREDITORSHIP SECURITIES Creditor ship Securities also known as debt finance which means the finance is mobilized from the creditors. Debenture and Bonds are the two major parts of the Creditors hip Securities.

DEBENTURES

Debenture is a document issued by the company. It is a certificate issued by the company under its seal acknowledging a debt. Debentures are the loans taken by the company. It is a certificate or letter issued by the company under its common seal acknowledging the receipt of loan. A debenture holder is the creditor of the company. A debenture holder is entitled to a fixed rate of interest on the debenture amount. Payment of interest on debenture is the first charge against profits. Apart from the loans from financial institutions, a company may raise loans through debentures. This is an additional source of long-term finance. The payment of interest and principal amounts on these debentures is subject to the terms and conditions of issue of debentures.

According to the Companies Act 1956, "debenture includes debenture stock, bonds and any other securities of a company whether constituting a charge of the assets of the company or not."

Types of Debentures it may be divided into the following major types:

1. Unsecured debentures: Unsecured debentures are not given any security on assets of the company. It is also called simple or naked debentures. This type of debentures is traded as unsecured creditors at the time of winding up of the company.

2. Secured debentures: Secured debentures are given security on assets of the company. It is also called as mortgaged debentures because these debentures are given against any mortgage of the assets of the company.

3. Redeemable debentures: These debentures are to be redeemed on the expiry of a certain period. The interest is paid periodically and the initial investment is returned after the fixed maturity period.

4. Irredeemable debentures: These kinds of debentures cannot be redeemable during the life time of the business concern.

5. Convertible debentures: Convertible debentures are the debentures whose holders have the option to get them converted wholly or partly into shares. These debentures are usually converted into equity shares. Conversion of the debentures may be: Non-convertible debentures Fully convertible debentures Partly convertible debentures

FEATURES OF DEBENTURES

1. Maturity period: Debentures consist of long-term fixed maturity period. Normally, debentures consist of 10–20 years maturity period and are repayable with the principle investment at the end of the maturity period.
2. Residual claims in income: Debenture holders are eligible to get fixed rate of interest at every end of the accounting period. Debenture holders have priority of claim in income of the company over equity and preference shareholders.
3. Residual claims on asset: Debenture holders have priority of claims on Assets of the company over equity and preference shareholders. The Debenture holders may have either specific change on the Assets or floating change of the assets of the company. Specific change of Debenture holders are treated as secured creditors and floating change of Debenture holders are treated as unsecured creditors.
4. No voting rights: Debenture holders are considered as creditors of the company. Hence they have no voting rights. Debenture holders cannot have the control over the performance of the business concern.
5. Fixed rate of interest: Debentures yield fixed rate of interest till the maturity period. Hence the business will not affect the yield of the debenture.

RETAINED EARNINGS

Retained earnings are another method of internal sources of finance. Actually is not a method of raising finance, but it is called as accumulation of profits by a company for its expansion and diversification activities. Retained earnings are called under different names such as; self finance, inter finance, and plugging back of profits. According to the Companies Act 1956 certain percentage, as prescribed by the central government (not exceeding 10%) of the net profits after tax of a financial year have to be compulsorily transferred to reserve by a company before declaring dividends for the year. Under the retained earnings sources of finance, a part of the total profits is transferred to various reserves such as general reserve, replacement fund, reserve for repairs and renewals, reserve funds and secrete reserves, etc.

II. MEDIUM-TERM FINANCE Medium-term finance refers to such sources of finance where the repayment is normally over one year and less than three years. This is normally utilized to buy or lease motor vehicles, computer equipment, or machinery whose life is less than three years. The sources of medium term finance are as given below:

Bank Loans: -

Bank loans are extended at a fixed rate of interest. Repayment of the loan and interest are scheduled at the beginning and are usually directly debited to the current account of the borrower. These are secured loans.

Hire-Purchase: -

It is a facility to buy a fixed asset while paying the price over a long period of time. In other words, the possession of the asset can be taken by making a down payment of a part of the price and the balance will be repaid with a fixed rate of interest in agreed number of installments. The buyer becomes the owner of the asset only on payment of the last installment. The seller is the owner of the asset till the last installment is paid. In case there is any default in payment, the seller can reserve the right of collecting back the asset. Today, most of the consumer durables such as cars, refrigerators, TVs and so on, are sold on hire-purchase basis. It provides an opportunity to keep using the asset much before the full price is paid. **www.easynotes4u.com** Page 43

Leasing or Renting: -

Where there is a need for fixed assets, the asset need not be purchases. It can be taken on lease or rent for specified number of years. The company who owns the asset is called lesser and the company which takes the asset on leas is called lessee. The agreement between the lesser and lessee is called a lease agreement. On the expiry of the lease agreement, the owner takes the asset back into his custody. Under lease agreement, ownership to the asset never passes. Only possession of the asset passes from lesser to the lessee. Lease is not a loan. But when the business wants a certain asset for a short/medium period, lease can significantly reduce the financial requirements of the business to buy the asset.

Venture Capital: -

This form of finance is available only for limited companies. Venture capital is normally provided in such projects where there is relatively a higher degree of risk. For such projects, finance through the conventional sources may not be available. Many banks offer such finance through their merchant banking divisions, or specialist banks which offer advice and financial assistance. The financial assistance may take the form of loans and venture capital. In the case of viable or feasible projects, the merchant banks may participate in the equity also. In return, they expect one or two (depending up on the volume of funs pumped in) director positions on the board to exercise the control on the company matters. The funds, so provided by the venture capital, can be used for acquiring another company or launching a new product or financing expansion and growth.

III. SHORT-TERM FINANCE

Commercial Paper (CP):

It is a new money market instrument introduced in India in recent times. CPs are issued usually in large denominations by the leading, nationally reputed, highly rated and credit worthy, large manufacturing and finance companies in the public and private sector. The proceeds of the issue of commercial paper are used to finance current transactions and seasonal and interim needs for funds. Reliance Industries is one of the early companies which are issued Commercial Paper.

Bank Overdraft:

This is a special arrangement with the banker where the customer can draw more than what he has in this savings/current account subject to a maximum limit. Interest is charged on a day-to-day basis on the actual amount overdrawn. This source is utilized to meet the temporary shortage of funds.

Trade Credit: -

This is a short-term credit facility extended by the creditors to the debtors. Normally, it is common for the traders to buy the material and other supplies from the suppliers on credit basis. After selling the stocks, the traders pay the cash and buy fresh stocks again on credit. Sometimes, the suppliers may insist on the buyer to sign a bill (bill of exchange). This bill is called bills payable.

Debt Factoring or Credit Factoring

Debt Factoring is the arrangement with factor where the trader agrees to sell its accounts receivable or debtors at discount to the specialized dealers called factors. In the case of Credit Factoring, the trader agrees to sell his accounts payables (at premium).

Advance from Customers:

- It is customary to collect full or part of the order amount from the customer in advance. Such advances are useful to meet the working capital needs. Short-term deposited from the customers, sister companies and outsiders

It is normal to find the supermarkets and trading organizations inviting deposits of six months to one year duration. As an incentive, such deposit holders may be given 5-10 precept discounts on the purchases. Internal funds:- Internal funds are generated by the firm itself by way of secret reserve, depreciation provisions, taxation provision, and retained profits and so on and these can be utilized to meet the urgencies.

A BRIEF SURVEY OF FINANCIAL INSTRUMENTS

Financial Instrument is a lawful agreement which involves some monetary value. Financial instruments have unique characteristics and structure. Financial instruments are in the form of cash instruments and derivative instruments. Financial instruments can be categorized into two types. They are:

PRIMARY SECURITIES:

Primary securities are those securities which are sold for the first time in financial markets. They are also termed as direct securities as they are issued directly to the savers by the ultimate investors of funds. Shares and debentures are good examples for primary securities as they are issued directly to the public. Shares: Share is a small part of capital of a company which is widely spread to raise long-term funds from the market. Usually, shares of a company are of two types. They are, equity shares and performance shares:

---- Equity Shares: Equity shares represent the ownership position in the company.

----Preference Shares: Preference shares are those share which enjoy some extra benefits when compare to other types of shares.

-----Debentures: A company can obtain capital for long-term through issue of debentures. Debentures are similar to term loans in which borrower assure to pay interest and principle amount at specified time period, usually, debentures are more adaptable than term loans as it involves many exceptional characteristics.

SECONDARY SECURITIES:

Secondary securities are termed as „indirect securities" as they are sold by intermediaries to the final savers. These financial intermediaries issue securities to the people and the money gathered is invested in companies. Unit Trust of India and mutual funds are the example of financial intermediaries. Commercial Papers: Commercial papers are issued by reputed and praise worthy companies, for short period of time. They are issued in the form of unsecured promissory notes to raise funds for a period of 3 months to 1 year.

Certificates of Deposits: It is a letter of acknowledgement issued by bank to the person or company in return of fixed deposits made for specified period. Certificate of deposits are in the form of negotiable instruments which can be bought and sold in financial market.

Secured Premium Notes: Secured premium notes are form of long term debentures which are redeemable at a price higher than the face value, known as premium.

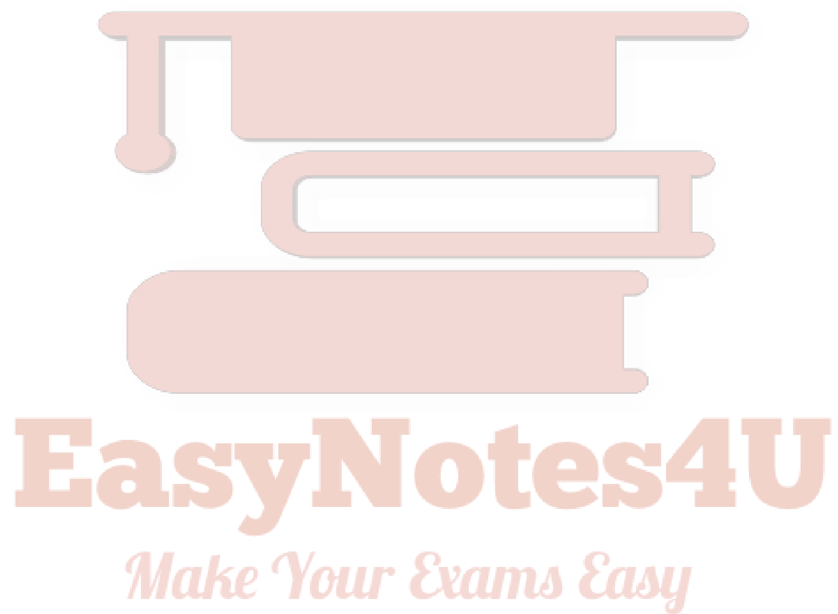
Non-convertible Debentures: Non-convertible debentures are those debentures which cannot be converted into equity shares. Investor gets the interest regularly and principle amount is paid only on maturity.

Zero Coupon Bonds: Zero coupon bonds have become famous in India a few years ago. These bonds do not yield any interest but they are sold to investor on heavy discount rate. Investor gets the profit from the difference of its purchase price and maturity value.

Zero Interest Fully Convertible Debentures Bonds: Zero interest bonds do not provide any interest but they are convertible into equity shares on specified period. They are introduced in India a few years ago.

EasyNotes4U Make Your Exams Easy

Deep Discount Bonds: Deep discount bonds are those bonds which are sold by Issuer Company on heavy discount from its maturity value. But zero discount bonds do not yield any interest. IDBI was the first bank to introduce these bonds in India.



CHAPTER-2: LEASE FINANCING

Meaning of leasing

Leasing is a process by which a firm can obtain the use of a certain fixed assets for which it must pay a series of contractual, periodic, tax deductible payments. The lessee is the receiver of the services or the assets under the lease contract and the lessor is the owner of the assets. The relationship between the tenant and the landlord is called a tenancy, and can be for a fixed or an indefinite period of time (called the term of the lease). The consideration for the lease is called rent.

Lease can be defined as the following ways:

1. A contract by which one party (lessor) gives to another (lessee) the use and possession of equipment for a specified time and for fixed payments.
2. The document in which this contract is written.
3. A great way companies can conserve capital.
4. An easy way vendors can increase sales.

A lease transaction is a commercial arrangement whereby an equipment owner or Manufacturer conveys to the equipment user the right to use the equipment in return for a rental. In other words, lease is a contract between the owner of an asset (the lessor) and its user (the lessee) for the right to use the asset during a specified period in return for a mutually agreed periodic payment (the lease rentals). The important feature of a lease contract is separation of the ownership of the asset from its usage.

Importance of Lease Financing

Lease financing is based on the observation made by Donald B. Grant:

"Why own a cow when the milk is so cheap? All you really need is milk and not the cow."

Leasing industry plays an important role in the economic development of a country by providing money incentives to lessee. The lessee does not have to pay the cost of asset at the time of signing the contract of leases. Leasing contracts are more flexible so lessees can structure the leasing contracts according to their needs for finance. The lessee can also pass on the risk of obsolescence to the lessor by acquiring those appliances, which have high technological obsolescence. Today, most of us are familiar with leases of houses, apartments, offices, etc.

The advantages of leasing include:

a. Leasing helps to possess and use a new piece of machinery or equipment without huge investment.
b. Leasing enables businesses to preserve precious cash reserves.
c. The smaller, regular payments required by a lease agreement enable businesses with limited capital to manage their cash flow more effectively and adapt quickly to changing economic conditions.
d. Leasing also allows businesses to upgrade assets more frequently ensuring they have the latest equipment without having to make further capital outlays.
e. It offers the flexibility of the repayment period being matched to the useful life of the equipment.
f. It gives businesses certainty because asset finance agreements cannot be cancelled by the lenders and repayments are generally fixed.
g. However, they can also be structured to include additional benefits such as servicing of equipment or variable monthly payments depending on a business's needs.
h. It is easy to access because it is secured – largely or entirely – on the asset being financed, rather than on other personal or business assets.
i. The rental, which sometimes exceeds the purchase price of the asset, can be paid from revenue generated by its use, directly impacting the lessee's liquidity.
j. 'ease instalments are exclusively material costs.
k. Using the purchase option, the lessee can acquire the leased asset at a lower price, as they pay the residual or non-depreciated value of the asset.
l. For the national economy, this way of financing allows access to state-of-the-art technology otherwise unavailable, due to high prices, and often impossible to acquire by loan arrangements.

Limitation of leasing

a. It is not a suitable mode of project financing because rental is payable soon after entering into lease agreement while new project generate cash only after long gestation period.
b. Certain tax benefits/ incentives/subsidies etc. may not be available to leased equipments.
c. The value of real assets (land and building) may increase during lease period. In this case lessee may lose potential capital gain.
d. The cost of financing is generally higher than that of debt financing.
e. A manufacturer(lessee) who want to discontinue business need to pay huge penalty to lessor for pre-closing lease agreement
f. There is no exclusive law for regulating leasing transaction.
g. In undeveloped legal systems, lease arrangements can result in inequality between the parties due to the lessor's economic dominance, which may lead to the lessee signing an unfavourable contract.

TYPES OF LEASE

(a) Financial lease
(b) Operating lease.

EasyNotes4U Make Your Exams Easy

SUBJECT:
UGC NET COMMERCE

UNIT - 5:
BUSINESS STATISTICS AND RESEARCH METHODS

CONTENTS

Chapter No.	Title	Page No.
1	**Measures of central tendency**	3-8
2	**Measures of dispersion**	9-11

3	**Measures of skewness**	12-14
4	**Correlation and regression of two variables**	15-28
5	**Probability:** Approaches to probability; Bayes' theorem	29-37
6	**Probability distributions:** Binomial, Poisson and normal distributions	38-42
7	**Research:** Concept and types; Research designs	43-49
8	**Data:** Collection and classification of data	50-52
9	**Sampling and estimation:** Concepts; Methods of sampling - probability and non-probability methods; Sampling distribution; Central limit theorem; Standard error; Statistical estimation	53-60
10	**Hypothesis testing:** z-test; t-test; ANOVA; Chi–square test; Mann-Whitney test (Utest); Kruskal-Wallis test (H-test); Rank correlation test	61-72
11	**Report writing**	73-76

	MCQs	77-82

CHAPTER-1: MEASURES OF CENTRAL TENDENCY

Measures of Central Tendency

According to Prof Bowley "Measures of central tendency (averages) are statistical constants which enable us to comprehend in a single effort the significance of the whole."

The main objectives of **Measure of Central Tendency are**

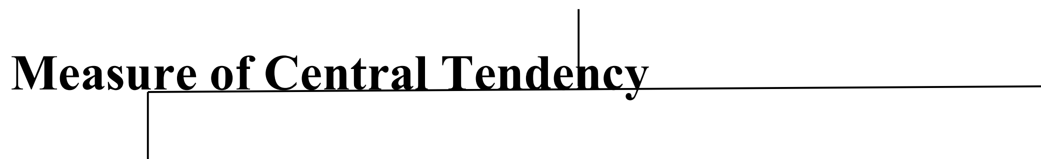
1) **To condense data in a single value.**
2) **To facilitate comparisons between data.**

There are different types of averages, each has its own advantages and disadvantages.

<u>Requisites of a Good Measure of Central Tendency:</u>

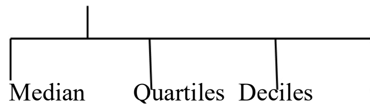
1. It should be rigidly defined.
2. It should be simple to understand & easy to calculate.
3. It should be based upon all values of given data.
4. It should be capable of further mathematical treatment.
5. It should have sampling stability.
6. It should be not be unduly affected by extreme values.

Measure of Central Tendency



Locational (positional) average
Mathematical Average

Partition values **Mode**
Arithmetic **Geometric**
Harmonic



Mean
Mean
Mean

Percentiles

Partition values: The points which divide the data in to equal parts are called Partition values.

MEDIAN

Median: The point or the value which divides the data in to two equal parts., or when the data is arranged in numerical order

The data must be ranked (sorted in ascending order) first. The median is the number in the middle. Depending on the data size we define median as:

It is the middle value when data size N is odd. It is the mean of the middle two values, when data size N is even.

Ungrouped Frequency Distribution

Find the cumulative frequencies for the data. The value of the variable corresponding to which a cumulative frequency is greater than (N+1)/2 for the first time. (Where N is the total number of observations.)

Example 1: Find the median for the following frequency distribution.

X	1	2	3	4	**5**	6	7	8	9

Freq	8	10	11	16	20	25	15	9	6

Solution: Calculate cumulative frequencies less than type.

X	1	2	3	4	**5**	6	7	8	9
Freq	8	10	11	16	20	25	15	9	6
Cum freq	8	18	29	45	**65**	90	105	114	120

N=120, (N+1)/2=60.5 this value is first exceeded by cumulative frequency 65 , this value is corresponding to X-value 5, hence median is 5

<u>Grouped Frequency Distribution</u> First obtain the cumulative frequencies for the data. Then mark the class corresponding to which a cumulative frequency is greater than (N)/2 for the first time. (N is the total number of observations.) Then that class is median class. Then median is evaluated by interpolation formula.

$$median = l_1 + (l_2 - l_1)\frac{(\frac{N}{2} - cf)}{f_m}$$

Where l_1= lower limit of the median class, l_2= upper limit of the median class N= Number of observations.

cf = cumulative frequency of the class proceeding to the median

class. f_m= frequency of the median class.

Quartiles: The data can be divided in to four equal parts by three points. These three points are known as quartiles. The quartiles are denoted by Q_i , i = 1,2,3

Qi is the value corresponding to $(iN/4)^{th}$ observation after arranging the data in the increasing order.

For grouped data: First obtain the cumulative frequencies for the data. Then mark the class corresponding to which a cumulative frequency is greater than (iN)/4 for the first time. (Where N is total number of observations.). Then that class is Qi class. Then Qi is evaluated by interpolation formula.

$$Q_i = l_1 + (l_2 - l_1)\frac{(\frac{iN}{4} - cf)}{f_q} \qquad i= 1, 2, 3$$

Where l_1= lower limit of the Qi class, l_2= upper limit of the Qi class N= Number of observations.

cf = cumulative frequency of the class proceeding to the Qi class. f_q= frequency of the Qi class.

Deciles are nine points which divided the data in to ten equal parts.

Di is the value corresponding to $(iN/10)^{th}$ observation after arranging the data in the increasing order.

For grouped data: First obtain the cumulative frequencies for the data. Then mark the class

corresponding to which a cumulative frequency is greater than (iN)/10 for the first time. (Where N is total number of observations.). Then that class is Di class. Then Di is evaluated by interpolation formula.

$$Di = l_1 + (l_2 - l_1)\frac{(\frac{iN}{10} - cf)}{f_d} \qquad i = 1, 2, \ldots 10.$$

Where l_1= lower limit of the Di class, l_2= upper limit of the Di class N= Number of observations.

cf = cumulative frequency of the class proceeding to the Di class. f_d= frequency of the Di class.

Percentiles are ninety-nine points which divided the data in to hundred equal parts.

Pi is the value corresponding to $(iN/100)^{th}$ observation after arranging the data in the increasing order.

For grouped data: First obtain the cumulative frequencies for the data. Then mark the class corresponding to which a cumulative frequency is greater than (iN)/100 for the first time. (Where N is total number of observations.) Then that class is Pi class. Then Pi is evaluated by interpolation formula.

$$Pi = l_1 + (l_2 - l_1)\frac{(\frac{iN}{100} -}{f_p}$$

Where l_1= lower limit of the Pi class, l_2= upper limit of the Pi class N= Number of observations.
cf = cumulative frequency of the class proceeding to the Pi class. f_p= frequency of the Pi class.

Graphical method for locating partition values: These partition values can be located graphically by using ogives. The point of intersection of both ogives is median.

To locate quartiles, mark N/4 on Y- axis, from that point draw a line parallel to X-axis, it cuts less than type ogive at Q_1 and intersects greater than or equal to curve at Q_3.

To locate Di mark iN/10 on Y-axis , from that point draw line parallel to X-axis, it intersects less than type curve at Di.

Similarly to locate Pi mark iN/100 on Y-axis , from that point draw line parallel to X-axis, it intersects less than type curve at Pi.

Example 2 . Find the median

Daily wages in Rs.	100-200	200-300	300-400	400-500	500-600	600-700
No of workers	4	6	20	10	5	5

Solution: To locate median class we have to calculate cumulative frequencies.

Daily	100-	200-	300-	400-	500-	600-

wages in Rs.	200	300	400	500	600	700
No of workers	4	6	20	10	5	5
Cum Freq	4	10	30	40	45	50

N=50 , N/2= 25 so median class is 300-400

$$median = l_1 + (l_2 - l_1)\frac{\left(\frac{N}{2} - cf\right)}{f_m} = 300 + (400 - 300)\frac{(25-10)}{20} = 300 + 100 * \frac{15}{20} = 375$$

Example 3: Find the median, Q_1, D8,P65 from the following data.

Marks	0-10	10-30	30-50	50-80	80-90	90-100
No of Students	4	12	20	8	4	2

Solution: To locate median class we have to calculate cumulative frequencies.

Marks	0-10	10-30	30-50	50-80	80-90	90-100
No of Students	4	12	20	8	4	2
Cumulative freq	4	16	36	44	48	50

Here N=50 so N/2=25, hence median class is 30-50

$$median \qquad l_1)\frac{\left(\frac{N}{2} - cf\right)}{f_m}$$

$= l_1 + (l_2 -$ $= 30 + \frac{(50 \quad 30)(25 \quad 16)}{20} = 30 + 20 * \frac{}{20} = 39$

$Q1$ $l_1)\frac{\left(\frac{N}{4} - cf\right)}{f_q}$ 8.5

Here N=50 so N/4=12.5, hence Q1 class is 10-30

$= l_1 + (l_2 -$ $= 10 + \frac{(30 \quad 10)(12.5 \quad 4)}{12} = 10 + 20 * \frac{}{12} = 24.16$

Here N=50 so 8*N/10=40 , hence D8 class is 50-80

$$D8 = l_1 + (l_2 - l_1)\frac{\left(\frac{8N}{10} - cf\right)}{f_d} = 50 + (80 - 50) * \frac{40 - 36}{8} = 50 + 30 * \frac{4}{8} = 65$$

$P65$ $- l_1)\frac{(\frac{65N}{100} - cf)}{f_p}$ 16.5

Here N=50 so 65*N/100=32.5 , hence P65 class is 30-50 $= l_1 + (l_2$ $= 30 + (50 - 30) * \frac{32.5 - 16}{20} = 30 + 20 * \frac{}{20} = 46.5$

Use the median to describe the middle of a set of data that *does* have an outlier.

Merits of Median

1. It is rigidly defined.
2. It is easy to understand & easy to calculate.
3. It is not affected by extreme values.
4. Even if extreme values are not known median can be calculated.
5. It can be located just by inspection in many cases.
6. It can be located graphically.
7. It is not much affected by sampling fluctuations.
8. It can be calculated for data based on ordinal scale.

Demerits of Median

1. It is not based upon all values of the given data.
2. For larger data size the arrangement of data in the increasing order is difficult process.
3. It is not capable of further mathematical treatment.
4. It is insensitive to some changes in the data values.

MODE

The mode is the most frequent data value. Mode is the value of the variable which is predominant in the given data series. Thus in case of discrete frequency distribution, mode is the value corresponding to maximum frequency. Sometimes there may be no single mode if no one value appears more than any other. There may also be two modes (bimodal), three modes (trimodal), or more than three modes (multi-modal).

For grouped frequency distributions, the modal class is the class with the largest frequency. After identifying modal class mode is evaluated by using interpolated formula. This formula is applicable when classes are of equal width.

$$mode = l_1 + (l_2 - l_1)\frac{d1}{d1 + d2}$$

Where l_1= lower limit of the modal class, l_2= upper limit

of the modal class"
$d_1 = f_m - f_0$ and $d_2 = f_m - f_1$ where f_m = frequency of the modal class,

f_0 = frequency of the class preceding to the modal class,

f_1 = frequency of the class succeeding to the modal class.

Mode can be located graphically by drawing histogram.

Steps:

1) Draw histogram
2) Locate modal class (highest bar of the histogram
3) Join diagonally the upper end points of the end points of the highest bar to the adjacent bars.
4) Mark the point of intersection of the diagonals.
5) Draw the perpendicular from this point on the X-axis .
6) The point where the perpendicular meets X-axis gives the modal value.

Example 4: Find the mode

Classes	0-10	10-20	20-30	30-40	40-50	50-60
Frequency	12	18	**27**	20	17	6

Modal class : 20-30 d1= fm-f0= 27-18=9   d2= fm-f1= 27-20=7

$$mode = l_1 - (l_2 - l_1)\frac{}{d1 - d2} = 20 - (30 - 20)\frac{}{9 - 7} = 20 - 10 * \frac{}{16} = 25.6$$

SUBJECT:
COMMERCE

UNIT – 6:
BUSINESS MANAGEMENT AND HUMAN RESOURCE MANAGEMENT

TALE OF CONTENTS:

Chapter No.	Title	Page No.
1	**Principles and functions of management:** Planning, Organizing, Staffing and Controlling	3-22
2	**Organization structure:** Formal and informal organizations; Span of control	23-27
3	**Responsibility and authority:** Delegation of authority and decentralization	28-32
4	**Motivation and leadership:** Concept and theories	33-40
5	**Corporate governance and business ethics**	41-52
6	**Human resource management:** Concept, role and functions of HRM; Human resource planning; Recruitment and selection; Training and development; Succession planning	53-66
7	**Compensation management:** Job evaluation; Incentives and fringe benefits	67-82
8	**Performance appraisal including 360 degree performance appraisal**	83-89
9	**Collective bargaining and workers' participation in management**	90-94
10	**Personality:** Perception; Attitudes; Emotions; Group dynamics; Power and politics; Conflict and negotiation; Stress management	95-115
11	**Organizational Culture:** Organizational development and organizational change	116-138
12	**MCQs**	139

CHAPTER 1: PRINCIPLES AND FUNCTIONS OF MANAGEMENT

Principles of Management:

Management has been defined by several theorists in their own way. Henri Fayol defined management as, “Management is to forecast, to plan, to organize, to command, to coordinate and control activities of others.” In simple terms, management is a means of organizing and delegating the work that needs to be done among people who can do it, and then ensuring that said work is done diligently and timely.

14 Principles of Management:

Henri Fayol was a prominent scientist who was considered to be among the first few who laid a foundation for scientific management. He gave us 14 principles of Management which are based on certain fundamental truths and act as guiding principles for decision making and other managerial responsibilities.

1. Division of Work: Dividing work among the workforce helps improve the quality of the overall product. Henri Fayol said that specialization in work increases the productivity and improves efficiency. Division of labour also leads to the specialization, accuracy, and speed of the workers. This principle is applicable both in managerial as well as technical work.

2. Authority and Responsibility: These are the two key things in management. They work hand in hand. While authority enables the management to delegate work, responsibility makes them accountable for any work done under their leadership.
Henri Fayol said that the power of authority accompanying responsibility gives the management the right to order subordinates along with a duty to be liable for acts of their subordinates.

3. Discipline: Nothing good was ever achieved without discipline. The third principle propagated by Henri Fayol was discipline. It is one of the core values in any system. Good behavior and civilized interactions make the management work smoothly and efficiently. Good conduct by employees also helps them smoothly progress in their careers.

4. Unity of Command: It basically means following a chain of command. A person should ideally answer to just one boss. If an employee is given work from more than one boss, there arises a conflict of interest. This can lead to confusion among the employees and hard to pin accountability. Thus, it is very crucial to follow unity of command.

5. Unity of Direction: For any corporate to prosper, there must be a unified goal. This principle is crucial as it incorporates the idea of a workforce working a singular direction with a unified aim. The responsibility of planning falls on the manager and he also must monitor the progress towards said goal.

6. Subordination of Individual Interest: The standard rule for any organization is the work on the collective interest of the organization as a whole rather than personal interest of an individual. This principle states that the interest of an individual will. Be subordinate to the objectives of the organization. This applies to the entire chain of command in the organization.

7. Remuneration: We all love an appreciation for our efforts. Remuneration in an organization play as a motivational force that keeps the employees fuelled to do well. This remuneration should be in tandem with the efforts that they put in. Remuneration may be monetary or non-monetary. At the end, the employee must feel that he was appropriately rewarded for his efforts.

8. Centralization: Depending on the size of the organization, it is important that the power is centralized to an extent that the decision making is judicious at all levels and not arbitrary. This will also depend on the size of the organization. Henri Fayol said that there must be a balance in the hierarchy and division of power.

9. Scalar Chain: Henri Fayol talks about a clear line of hierarchy from the top rung to the lowest. So that every employee knows who is their immediate senior in the times of conflict or crisis. But also the employee must be able to contact any person in the hierarchy without hesitation during a time of crisis.
10. Order: There must be a proper defined order maintained at the work premises so that it makes for a conducive work environment. The right environment in the place of work will boost productivity.
11. Equity: Employees should be treated with equality and respect. This is among the core values of management. It will fall on the manager to ensure that there is no discrimination of any kind happening in the workplace.
12. Stability: An employee is able to deliver better when he is secure in his job. It is the duty of the management to offer job security to their employees along with a promise of growth. Minimizing employee turnover is important and beneficial to the management as well.
13. Initiative: Sometimes groundbreaking ideas come from unexpected places. The management must encourage its employees to take initiatives in the organization. It will make them feel valued and develop their interest.
14. Esprit de Corps: This is one of the core principles. The management must ensure that the team remains constantly motivated and are cooperative with each other. It is very important to develop mutual trust among employees as it leads to a positive work environment.

<u>Functions of Management:</u>

Managers just don't go out and haphazardly perform their responsibilities. Good managers discover how to master five basic functions: planning, organizing, staffing, leading, and controlling.
1. Planning: This step involves mapping out exactly how to achieve a particular goal. Say, for example, that the organization's goal is to improve company sales. The manager first needs to decide which steps are necessary to accomplish that goal. These steps may include increasing advertising, inventory, and sales staff. These necessary steps are developed into a plan. When the plan is in place, the manager can follow it to accomplish the goal of improving company sales.
2. Organizing: After a plan is in place, a manager needs to organize her team and materials according to her plan. Assigning work and granting authority are two important elements of organizing.
3. Staffing: After a manager discerns his area's needs, he may decide to beef up his staffing by recruiting, selecting, training, and developing employees. A manager in a large organization often works with the company's human resources department to accomplish this goal.
4. Leading: A manager needs to do more than just plan, organize, and staff her team to achieve a goal. She must also lead. Leading involves motivating, communicating, guiding, and encouraging. It requires the manager to coach, assist, and problem solve with employees.
5. Controlling: After the other elements are in place, a manager's job is not finished. He needs to continuously check results against goals and take any corrective actions necessary to make sure that his area's plans remain on track.
All managers at all levels of every organization perform these functions, but the amount of time a manager spends on each one depends on both the level of management and the specific organization.

PLANNING

Planning means looking ahead and chalking out future courses of action to be followed. It is a preparatory step. It is a systematic activity which determines when, how and who is going to perform a specific job. Planning is a detailed programme regarding future courses of action.

It is rightly said "**Well plan is half done**". Therefore planning takes into consideration available & prospective human and physical resources of the organization so as to get effective co-ordination, contribution & perfect adjustment. It is the basic management function which includes formulation of one or more detailed plans to achieve optimum balance of needs or demands with the available resources.

According to Urwick, "Planning is a mental predisposition to do things in orderly way, to think before acting and to act in the light of facts rather than guesses". Planning is deciding best alternative among others to perform different managerial functions in order to achieve predetermined goals.

According to Koontz & O'Donell, "Planning is deciding in advance what to do, how to do and who is to do it. Planning bridges the gap between where we are to, where we want to go. It makes possible things to occur which would not otherwise occur".

<u>Steps in Planning Function</u>

Planning function of management involves following steps:-

1. **Establishment of objectives**
   a. Planning requires a systematic approach.
   b. Planning starts with the setting of goals and objectives to be achieved.
   c. Objectives provide a rationale for undertaking various activities as well as indicate direction of efforts.
   d. Moreover objectives focus the attention of managers on the end results to be achieved.

e. As a matter of fact, objectives provide nucleus to the planning process. Therefore, objectives should be stated in a clear, precise and unambiguous language. Otherwise the activities undertaken are bound to be ineffective.
f. As far as possible, objectives should be stated in quantitative terms. For example, Number of men working, wages given, units produced, etc. But such an objective cannot be stated in quantitative terms like performance of quality control manager, effectiveness of personnel manager.
g. Such goals should be specified in qualitative terms.
h. Hence objectives should be practical, acceptable, workable and achievable.

2. Establishment of Planning Premises

a. Planning premises are the assumptions about the lively shape of events in future.
b. They serve as a basis of planning.
c. Establishment of planning premises is concerned with determining where one tends to deviate from the actual plans and causes of such deviations.
d. It is to find out what obstacles are there in the way of business during the course of operations.
e. Establishment of planning premises is concerned to take such steps that avoids these obstacles to a great extent.
f. Planning premises may be internal or external. Internal includes capital investment policy, management labour relations, philosophy of management, etc. Whereas external includes socio-economic, political and economical changes.
g. Internal premises are controllable whereas external are non- controllable.

3. Choice of alternative course of action

a. When forecast are available and premises are established, a number of alternative course of actions have to be considered.
b. For this purpose, each and every alternative will be evaluated by weighing its pros and cons in the light of resources available and requirements of the organization.
c. The merits, demerits as well as the consequences of each alternative must be examined before the choice is being made.
d. After objective and scientific evaluation, the best alternative is chosen.
e. The planners should take help of various quantitative techniques to judge the stability of an alternative.

4. Formulation of derivative plans

a. Derivative plans are the sub plans or secondary plans which help in the achievement of main plan.
b. Secondary plans will flow from the basic plan. These are meant to support and expediate the achievement of basic plans.
c. These detail plans include policies, procedures, rules, programmes, budgets, schedules, etc. For example, if profit maximization is the main aim of the enterprise, derivative plans will include sales maximization, production maximization, and cost minimization.
d. Derivative plans indicate time schedule and sequence of accomplishing various tasks.

5. Securing Co-operation

a. After the plans have been determined, it is necessary rather advisable to take subordinates or those who have to implement these plans into confidence.
b. The purposes behind taking them into confidence are :-
    i. Subordinates may feel motivated since they are involved in decision making process.
    ii. The organization may be able to get valuable suggestions and improvement in formulation as well as implementation of plans.
    iii. Also the employees will be more interested in the execution of these plans.

6. Follow up/Appraisal of plans

a. After choosing a particular course of action, it is put into action.
b. After the selected plan is implemented, it is important to appraise its effectiveness.
c. This is done on the basis of feedback or information received from departments or persons concerned.
d. This enables the management to correct deviations or modify the plan.
e. This step establishes a link between planning and controlling function.
f. The follow up must go side by side the implementation of plans so that in the light of observations made, future plans can be made more realistic.

<u>Characteristics of Planning</u>

1. Planning is goal-oriented.

a. Planning is made to achieve desired objective of business.

   b. The goals established should general acceptance otherwise individual efforts & energies will go misguided and misdirected.
   c. Planning identifies the action that would lead to desired goals quickly & economically.
   d. It provides sense of direction to various activities. E.g. Maruti Udhyog is trying to capture once again Indian Car Market by launching diesel models.

2. **Planning is looking ahead.**
   a. Planning is done for future.
   b. It requires peeping in future, analyzing it and predicting it.
   c. Thus planning is based on forecasting.
   d. A plan is a synthesis of forecast.
   e. It is a mental predisposition for things to happen in future.
3. **Planning is an intellectual process.**
   a. Planning is a mental exercise involving creative thinking, sound judgement and imagination.
   b. It is not a mere guesswork but a rotational thinking.
   c. A manager can prepare sound plans only if he has sound judgement, foresight and imagination.
   d. Planning is always based on goals, facts and considered estimates.
4. **Planning involves choice & decision making.**
   a. Planning essentially involves choice among various alternatives.
   b. Therefore, if there is only one possible course of action, there is no need planning because there is no choice.
   c. Thus, decision making is an integral part of planning.
   d. A manager is surrounded by no. of alternatives. He has to pick the best depending upon requirements & resources of the enterprises.
5. **Planning is the primary function of management / Primacy of Planning.**
   a. Planning lays foundation for other functions of management.
   b. It serves as a guide for organizing, staffing, directing and controlling.
   c. All the functions of management are performed within the framework of plans laid out.
   d. Therefore planning is the basic or fundamental function of management.
6. **Planning is a Continuous Process.**
   a. Planning is a never ending function due to the dynamic business environment.
   b. Plans are also prepared for specific period f time and at the end of that period, plans are subjected to revaluation and review in the light of new requirements and changing conditions.
   c. Planning never comes into end till the enterprise exists issues, problems may keep cropping up and they have to be tackled by planning effectively.
7. **Planning is all Pervasive.**
   a. It is required at all levels of management and in all departments of enterprise.
   b. Of course, the scope of planning may differ from one level to another.
   c. The top level may be more concerned about planning the organization as a whole whereas the middle level may be more specific in departmental plans and the lower level plans implementation of the same.
8. **Planning is designed for efficiency.**
   a. Planning leads to accomplishment of objectives at the minimum possible cost.
   b. It avoids wastage of resources and ensures adequate and optimum utilization of resources.
   c. A plan is worthless or useless if it does not value the cost incurred on it.
   d. Therefore planning must lead to saving of time, effort and money.
   e. Planning leads to proper utilization of men, money, materials, methods and machines.
9. **Planning is Flexible.**
   a. Planning is done for the future.
   b. Since future is unpredictable, planning must provide enough room to cope with the changes in customer's demand, competition, govt. policies etc.
   c. Under changed circumstances, the original plan of action must be revised and updated to male it more practical.

<u>Advantages of Planning</u>

1. **Planning facilitates management by objectives.**
   a. Planning begins with determination of objectives.
   b. It highlights the purposes for which various activities are to be undertaken.
   c. In fact, it makes objectives more clear and specific.
   d. Planning helps in focusing the attention of employees on the objectives or goals of enterprise.
   e. Without planning an organization has no guide.

f. Planning compels manager to prepare a Blue-print of the courses of action to be followed for accomplishment of objectives.
g. Therefore, planning brings order and rationality into the organization.

2. Planning minimizes uncertainties.

a. Business is full of uncertainties.
b. There are risks of various types due to uncertainties.
c. Planning helps in reducing uncertainties of future as it involves anticipation of future events.
d. Although future cannot be predicted with cent percent accuracy but planning helps management to anticipate future and prepare for risks by necessary provisions to meet unexpected turn of events.
e. Therefore with the help of planning, uncertainties can be forecasted which helps in preparing standbys as a result, uncertainties are minimized to a great extent.

3. Planning facilitates co-ordination.

a. Planning revolves around organizational goals.
b. All activities are directed towards common goals.
c. There is an integrated effort throughout the enterprise in various departments and groups.
d. It avoids duplication of efforts. In other words, it leads to better co-ordination.
e. It helps in finding out problems of work performance and aims at rectifying the same.

4. Planning improves employee's moral.

a. Planning creates an atmosphere of order and discipline in organization.
b. Employees know in advance what is expected of them and therefore conformity can be achieved easily.
c. This encourages employees to show their best and also earn reward for the same.
d. Planning creates a healthy attitude towards work environment which helps in boosting employees moral and efficiency.

5. Planning helps in achieving economies.

a. Effective planning secures economy since it leads to orderly allocation ofresources to various operations.
b. It also facilitates optimum utilization of resources which brings economy in operations.
c. It also avoids wastage of resources by selecting most appropriate use that will contribute to the objective of enterprise. For example, raw materials can be purchased in bulk and transportation cost can be minimized. At the same time it ensures regular supply for the production department, that is, overall efficiency.

6. Planning facilitates controlling.

a. Planning facilitates existence of certain planned goals and standard of performance.
b. It provides basis of controlling.
c. We cannot think of an effective system of controlling without existence of well thought out plans.
d. Planning provides pre-determined goals against which actual performance is compared.
e. In fact, planning and controlling are the two sides of a same coin. If planning is root, controlling is the fruit.

7. Planning provides competitive edge.

a. Planning provides competitive edge to the enterprise over the others which do not have effective planning. This is because of the fact that planning may involve changing in work methods, quality, quantity designs, extension of work, redefining of goals, etc.
b. With the help of forecasting not only the enterprise secures its future but at the same time it is able to estimate the future motives of it's competitor which helps in facing future challenges.
c. Therefore, planning leads to best utilization of possible resources, improves quality of production and thus the competitive strength of the enterprise is improved.

8. Planning encourages innovations.

a. In the process of planning, managers have the opportunities of suggesting ways and means of improving performance.
b. Planning is basically a decision making function which involves creative thinking and imagination that ultimately leads to innovation of methods and operations for growth and prosperity of the enterprise.

Disadvantages

Internal Limitations

There are several limitations of planning. Some of them are inherit in the process of planning like rigidity and other arise due to shortcoming of the techniques of planning and in the planners themselves.

1. Rigidity

a. Planning has tendency to make administration inflexible.
b. Planning implies prior determination of policies, procedures and programmes and a strict adherence to them in all circumstances.
c. There is no scope for individual freedom.
d. The development of employees is highly doubted because of which management might have faced lot of difficulties in future.
e. Planning therefore introduces inelasticity and discourages individual initiative and experimentation.

2. **Misdirected Planning**
   a. Planning may be used to serve individual interests rather than the interest of the enterprise.
   b. Attempts can be made to influence setting of objectives, formulation of plans and programmes to suit ones own requirement rather than that of whole organization.
   c. Machinery of planning can never be freed of bias. Every planner has his own likes, dislikes, preferences, attitudes and interests which is reflected in planning.
3. **Time consuming**
   a. Planning is a time consuming process because it involves collection of information, it's analysis and interpretation thereof. This entire process takes a lot of time specially where there are a number of alternatives available.
   b. Therefore planning is not suitable during emergency or crisis when quick decisions are required.
4. **Probability in planning**
   a. Planning is based on forecasts which are mere estimates about future.
   b. These estimates may prove to be inexact due to the uncertainty of future.
   c. Any change in the anticipated situation may render plans ineffective.
   d. Plans do not always reflect real situations inspite of the sophisticated techniques of forecasting because future is unpredictable.
   e. Thus, excessive reliance on plans may prove to be fatal.
5. **False sense of security**
   a. Elaborate planning may create a false sense of security to the effect that everything is taken for granted.
   b. Managers assume that as long as they work as per plans, it is satisfactory.
   c. Therefore they fail to take up timely actions and an opportunity is lost.
   d. Employees are more concerned about fulfillment of plan performance rather than any kind of change.
6. **Expensive**
   a. Collection, analysis and evaluation of different information, facts and alternatives involves a lot of expense in terms of time, effort and money
   b. According to Koontz and O'Donell, ' Expenses on planning should never exceed the estimated benefits from planning. '

External Limitations of Planning

1. **Political Climate-** Change of government from Congress to some other political party, etc.
2. **Labour Union-** Strikes, lockouts, agitations.
3. **Technological changes-** Modern techniques and equipments, computerization.
4. **Policies of competitors-** Eg. Policies of Coca Cola and Pepsi.
5. **Natural Calamities-** Earthquakes and floods.
6. **Changes in demand and prices-** Change in fashion, change in tastes, change in income level, demand falls, price falls, etc.

ORGANIZING

Organizing is the function of management which follows planning. It is a function in which the synchronization and combination of human, physical and financial resources takes place. All the three resources are important to get results. Therefore, organizational function helps in achievement of results which in fact is important for the functioning of a concern. According to *Chester Barnard*, "Organizing is a function by which the concern is able to define the role positions, the jobs related and the co-ordination between authority and responsibility. Hence, a manager always has to organize in order to get results.

A manager performs organizing function with the help of following steps:-

1. **Identification of activities -** All the activities which have to be performed in a concern have to be identified first. For example, preparation of accounts, making sales, record keeping, quality control, inventory control, etc. All these activities have to be grouped and classified into units.

2. **Departmentally organizing the activities -** In this step, the manager tries to combine and group similar and related activities into units or departments. This organization of dividing the whole concern into independent units and departments is called departmentation.
3. **Classifying the authority -** Once the departments are made, the manager likes to classify the powers and its extent to the managers. This activity of giving a rank in order to the managerial positions is called hierarchy. The top management is into formulation of policies, the middle level management into departmental supervision and lower level management into supervision of foremen. The clarification of authority help in bringing efficiency in the running of a concern. This helps in achieving efficiency in the running of a concern. This helps in avoiding wastage of time, money, effort, in avoidance of duplication or overlapping of efforts and this helps in bringing smoothness in a concern's working.
4. **Co-ordination between authority and responsibility -** Relationships are established among various groups to enable smooth interaction toward the achievment of the organizational goal. Each individual is made aware of his authority and he/she knows whom they have to take orders from and to whom they are accountable and to whom they have to report. A clear organizational structure is drawn and all the employees are made aware of it.

Importance:

1. **Specialization -** Organizational structure is a network of relationships in which the work is divided into units and departments. This division of work is helping in bringing specialization in various activities of concern.
2. **Well defined jobs -** Organizational structure helps in putting right men on right job which can be done by selecting people for various departments according to their qualifications, skill and experience. This is helping in defining the jobs properly which clarifies the role of every person.
3. **Clarifies authority -** Organizational structure helps in clarifying the role positions to every manager (status quo). This can be done by clarifying the powers to every manager and the way he has to exercise those powers should be clarified so that misuse of powers do not take place. Well defined jobs and responsibilities attached helps in bringing efficiency into managers working. This helps in increasing productivity.

SUBJECT:
UGC NET COMMERCE (08)

UNIT-7:
Banking and Financial Institutions

By:
Dr. Gaurav Jangra

www.easynotes4u.com
Email: support@easynootes4u.com
+918814931483

CONTENTS

CH. NO.	TITLE	PAGE NO.
1	**Overview of Indian financial system**	
2	**Types of banks:** Commercial banks; Regional Rural Banks (RRBs); Foreign banks; Cooperative banks	
3	**Reserve Bank of India:** Functions; Role and monetary policy management	
4	**Banking sector reforms in India:** Basel norms; Risk management; NPA management	
5	**Financial markets:** Money market; Capital market; Government securities market	
6	**Financial Institutions:** Development Finance Institutions (DFIs); Non-Banking Financial Companies (NBFCs); Mutual Funds; Pension Funds	
7	**Financial Regulators in India**	
8	**Financial sector reforms including financial inclusion**	
9	**Digitisation of banking and other financial services:** Internet banking; mobile banking; Digital payments systems	
10	**Insurance:** Types of insurance- Life and Non-life insurance; Risk classification and management; Factors limiting the insurability of risk; Re-insurance; Regulatory framework of insurance- IRDA and its role	

Financial System of any country consists of financial markets, financial intermediation and financial instruments or financial products. This paper discusses the meaning of finance and Indian Financial System and focus on the financial markets, financial intermediaries and financial instruments. The brief review on various money market instruments are also covered in this study.

The term "finance" in our simple understanding it is perceived as equivalent to 'Money'. We read about Money and banking in Economics, about Monetary Theory and Practice and about "Public Finance". But finance exactly is not money, it is the source of providing funds for a particular activity. Thus public finance does not mean the money with the Government, but it refers to sources of raising revenue for the activities and functions of a Government. Here some of the definitions of the word 'finance', both as a source and as an activity i.e. as a noun and a verb.

The American Heritage Dictionary of the English Language, Fourth Edition defines the term as under-

1:"The science of the management of money and other assets.";
2: "The management of money, banking, investments, and credit. ";
3: "finances Monetary resources; funds, especially those of a government or corporate body"
4: "The supplying of funds or capital."

Finance as a function (i.e. verb) is defined by the same dictionary as under-

1:"To provide or raise the funds or capital for": financed a new car
2: "To supply funds to": financing a daughter through law school.
3: "To furnish credit to".

Another English Dictionary, "WordNet ® 1.6, © 1997Princeton University " defines the term as under-

1:"the commercial activity of providing funds and capital"
2: "the branch of economics that studies the management of money and other assets"
3: "the management of money and credit and banking and investments"

The same dictionary also defines the term as a function in similar words as under-

1: "obtain or provide money for;" " Can we finance the addition to our home?"
2:"sell or provide on credit "

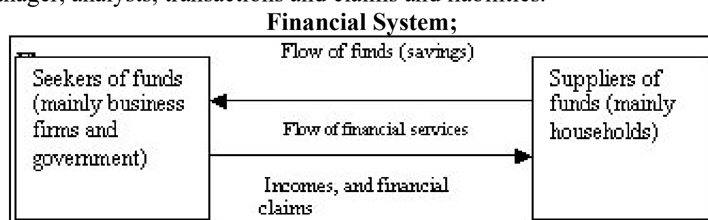
All definitions listed above refer to finance as a source of funding an activity. In this respect providing or securing finance by itself is a distinct activity or function, which results in Financial Management, Financial Services and Financial Institutions. Finance therefore represents the resources by way funds needed for a particular activity. We thus speak of 'finance' only in relation to a proposed activity. Finance goes with commerce, business, banking etc. Finance is also referred to as "Funds" or "Capital", when referring to the financial needs of a corporate body. When we study finance as a subject for generalising its profile and attributes, we distinguish between 'personal finance" and "corporate finance" i.e. resources needed personally by an individual for his family and individual needs and resources needed by a business organization to carry on its functions intended for the achievement of its corporate goals.

INDIAN FINANCIAL SYSTEM

The economic development of a nation is reflected by the progress of the various economic units, broadly classified into corporate sector, government and household sector. While performing their activities these units will be placed in a surplus/deficit/balanced budgetary situations.

There are areas or people with surplus funds and there are those with a deficit. A financial system or financial sector functions as an intermediary and facilitates the flow of funds from the areas of surplus to the areas of deficit. A Financial System is a composition of various institutions, markets, regulations and laws, practices, money manager, analysts, transactions and claims and liabilities.

Financial System;



The word "system", in the term "financial system", implies a set of complex and closely connected or interlined institutions, agents, practices, markets, transactions, claims, and liabilities in the economy. The financial system is concerned about money, credit and finance-the three terms are intimately related yet are somewhat different from each other. Indian financial system consists of financial market, financial instruments and financial intermediation. These are briefly discussed below;

FINANCIAL MARKETS

Financial Markets:

A financial market is a market for creation and exchange of financial assets. If you buy or sell financial assets, you will participate in financial markets in some way or the other.

Classification of Financial Markets:

1. Nature of Claim

a. Debt Market

b. Equity Market

2. Maturity of Claim

a. Money Market

b. Capital Market

3. Seasoning of Claim

a. Primary Market

b. Secondary Market

Timing of Delivery

a. Cash or Spot Market

b. Forward or futures Market

Organisational structure

a. Exchange-traded Market

b. Over-the-counter Market

There are different ways of classifying financial markets.

1. Nature of Claim:

a. The Debt Market:

It is the financial market for fixed claims (debt instruments).

b. The equity Market is the financial market for residual claims (equity instruments).

2. Maturity of Claim:

a. Money Market: The market for short-term financial claims is referred to as the money market. Traditionally the cut off between short-term and long-term has been one year – though this dividing line is arbitrary, it is widely accepted. Since short-term financial claims are almost invariably debt claims, the money market is the market for short-term debt instruments.

b. Capital Market: The market for long-term financial claims is called the capital market. The capital market is the market for long-term debt instruments and equity instruments.

3. Seasoning of Claim:

a. Primary Market:

It is classify financial markets is based on whether the claims represent new issues or outstanding issues. The market where issuers sell new claims is referred to as the primary market

b. Secondary Market:

The market where investors trade outstanding securities is called the secondary market.

4. Timing of Delivery:

a. Cash or spot Market:

It is one where the delivery occurs immediately.

b. Forward or futures Market:

Forward or futures market is one where the delivery occurs at a predetermined time in future.

5. Organisational Structure:

a. Exchange traded Market:

It is characterised by a centralised organisation with standardized procedures.

b. Counter Market:

It is a decentralised market with customized procedures.

A Financial Market can be defined as the market in which financial assets are created or transferred. As against a real transaction that involves exchange of money for real goods or services, a financial transaction involves creation or transfer of a financial asset. Financial Assets or Financial Instruments represents a claim to the payment of a sum of money sometime in the future and /or periodic payment in the form of interest or dividend.

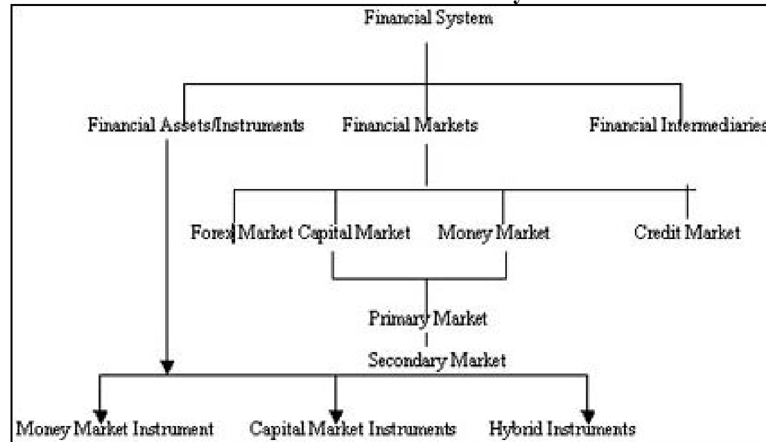
Money Market- The money market ifs a wholesale debt market for low-risk, highly-liquid, short-term instrument. Funds are available in this market for periods ranging from a single day up to a year. This market is dominated mostly by government, banks and financial institutions.

Capital Market - The capital market is designed to finance the long-term investments. The transactions taking place in this market will be for periods over a year.

Forex Market - The Forex market deals with the multicurrency requirements, which are met by the exchange of currencies. Depending on the exchange rate that is applicable, the transfer of funds takes place in this market. This is one of the most developed and integrated market across the globe.

Credit Market- Credit market is a place where banks, FIs and NBFCs purvey short, medium and long-term loans to corporate and individuals.

Constituents of a Financial System



FINANCIAL INTERMEDIATION

Having designed the instrument, the issuer should then ensure that these financial assets reach the ultimate investor in order to garner the requisite amount. When the borrower of funds approaches the financial market to raise funds, mere issue of securities will not suffice. Adequate information of the issue, issuer and the security should be passed on to take place. There should be a proper channel within the financial system to ensure such transfer. To serve this purpose, Financial intermediaries came into existence. Financial intermediation in the organized sector is conducted by a widerange of institutions functioning under the overall surveillance of the Reserve Bank of India. In the initial stages, the role of the intermediary was mostly related to ensure transfer of funds from the lender to the borrower. This service was offered by banks, FIs, brokers, and dealers. However, as the financial system widened along with the developments taking place in the financial markets, the scope of its operations also widened. Some of the important intermediaries operating ink the financial markets include; investment bankers, underwriters, stock exchanges, registrars, depositories, custodians, portfolio managers, mutual funds, financial advertisers financial consultants, primary dealers, satellite dealers, self regulatory organizations, etc. Though the markets are different, there may be a few intermediaries offering their services in move than one market e.g. underwriter. However, the services offered by them vary from one market to another.

Intermediary	Market	Role
Stock Exchange	Capital Market	Secondary Market to securities
Investment Bankers	Capital Market, Credit Market	Corporate advisory services, Issue of securities
Underwriters	Capital Market, Money Market	Subscribe to unsubscribed portion of securities
Registrars, Depositories, Custodians	Capital Market	Issue securities to the investors on behalf of the company and handle share transfer activity
Primary Dealers Satellite Dealers	Money Market	Market making in government securities
Forex Dealers	Forex Market	Ensure exchange ink currencies

FINANCIAL INSTRUMENTS

Money Market Instruments

The money market can be defined as a market for short-term money and financial assets that are near substitutes for money. The term short-term means generally a period upto one year and near substitutes to money is used to denote any financial asset which can be quickly converted into money with minimum transaction cost.

Some of the important money market instruments are briefly discussed below;

1. Call/Notice Money
2. Treasury Bills
3. Term Money
4. Certificate of Deposit
5. Commercial Papers

1. Call /Notice-Money Market

Call/Notice money is the money borrowed or lent on demand for a very short period. When money is borrowed or lent for a day, it is known as Call (Overnight) Money. Intervening holidays and/or Sunday are excluded for this purpose. Thus money, borrowed on a day and repaid on the next working day, (irrespective of the number of intervening holidays) is "Call Money". When money is borrowed or lent for more than a day and up to 14 days, it is "Notice Money". No collateral security is required to cover these transactions.

2. Inter-Bank Term Money

Inter-bank market for deposits of maturity beyond 14 days is referred to as the term money market. The entry restrictions are the same as those for Call/Notice Money except that, as per existing regulations, the specified entities are not allowed to lend beyond 14 days.

3. Treasury Bills.

Treasury Bills are short term (up to one year) borrowing instruments of the union government. It is an IOU of the Government. It is a promise by the Government to pay a stated sum after expiry of the stated period from the date of issue (14/91/182/364 days i.e. less than one year). They are issued at a discount to the face value, and on maturity the face value is paid to the holder. The rate of discount and the corresponding issue price are determined at each auction.

4. Certificate of Deposits

Certificates of Deposit (CDs) is a negotiable money market instrument nd issued in dematerialised form or as a Usance Promissory Note, for funds deposited at a bank or other eligible financial institution for a specified time period. Guidelines for issue of CDs are presently governed by various directives issued by the Reserve Bank of India, as amended from time to time. CDs can be issued by (i) scheduled commercial banks excluding Regional Rural Banks (RRBs) and Local Area Banks (LABs); and (ii) select all-India Financial Institutions that have been permitted by RBI to raise short-term resources within the umbrella limit fixed by RBI. Banks have the freedom to issue CDs depending on their requirements. An FI may issue CDs within the overall umbrella limit fixed by RBI, i.e., issue of CD together with other instruments viz., term money, term deposits, commercial papers and intercorporate deposits should not exceed 100 per cent of its net owned funds, as per the latest audited balance sheet.

5. Commercial Paper

CP is a note in evidence of the debt obligation of the issuer. On issuing commercial paper the debt obligation is transformed into an instrument. CP is thus an unsecured promissory note privately placed with investors at a discount rate to face value determined by market forces. CP is freely negotiable by endorsement and delivery. A company shall be eligible to issue CP provided - (a) the tangible net worth of the company, as per the latest audited balance sheet, is not less than Rs. 4 crore; (b) the working capital (fund-based) limit of the company from the banking system is not less than Rs.4 crore and (c) the borrowal account of the company is classified as a Standard Asset by the financing bank/s. The minimum maturity period of CP is 7 days. The minimum credit rating shall be P-2 of CRISIL or such equivalent rating by other agencies. (for more details visit www.indianmba.com faculty column)

Capital Market Instruments

The capital market generally consists of the following long term period i.e., more than one year period, financial instruments; In the equity segment Equity shares, preference shares, convertible preference shares, non-convertible preference shares etc and in the debt segment debentures, zero coupon bonds, deep discount bonds etc.

Hybrid Instruments

Hybrid instruments have both the features of equity and debenture. This kind of instruments is called as hybrid instruments. Examples are convertible debentures, warrants etc.

Functions of the Financial System:

The financial system performs the following interrelated functions that are essential to a modern economy:

- It provides a payment system for the exchange of goods and services
- It enables the pooling of funds for undertaking large scale enterprises
- It provides a mechanism for spatial and temporal transfer of resources
- It provides a way for managing uncertainty and controlling risk
- It generates information that helps in coordinating decentralised decision making
- It helps in dealing with the incentive problem when one party has an informational advantage.

SUBJECT:
UGC NET COMMERCE

UNIT-8
MARKETING MANAGEMENT

TABLE OF CONTENTS

Chapter No.	Title	Page No.
1	Marketing Concepts and Approaches	3-7
2	Marketing channels	8-11
3	Strategic Marketing Planning	12-17
4	Marketing Mix	18-21
5	Marketing Environment	22-23
6	Market Segmentation	24-30
7	Product Decision	31-38
8	Pricing Decision	39-46
9	Promotion Decision	47-58
10	Sales Promotion, Personal Selling & Publicity	59-66
11	Distribution Decision	67-72
12	Consumer Behaviour	73-79
13	Service Marketing	80-83
14	Trends in Marketing	84-91
15	Logistics Management	92-98
	MCQs	99-105
	References	106

CHAPTER-1: MARKETING: CONCEPTS AND APPROACHES

Marketing is about identifying and meeting human and social needs. One of the shortest good definitions of marketing is “meeting needs profitably.

Coping with these exchange processes calls for a considerable amount of work and skill. Marketing management takes place when at least one party to a potential exchange thinks about the means of achieving desired responses from other parties. Thus, we see marketing management as the art and science of choosing target markets and getting, keeping, and growing customers through creating, delivering, and communicating superior customer value.

DEFINITION OF MARKETING:

1. **Traditional Concept: “**The term ‘traditional marketing’ can be expressed as the business activity through which goods and services directly move from producers to consumers or users.”
2. **Modern Concept: “**The term ‘modern marketing’ can be expressed as the achievement of corporate goals through meeting and exceeding customer needs better than the competition.”
3. **Philip Kotler: “**The term ‘marketing’ is a social and managerial process by which individual groups obtain what they need and want through creating, offering and freely exchanging product and services of value with others.”
4. **The American Marketing Association**: "Marketing is the activity, set of institutions, and process for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large."

NATURE OF MARKETING

The Nature of Marketing (or Modern marketing) may be studied under the following points:

1.Human activity: Originally, the term marketing is a human activity under which human needs are satisfied by human efforts. It’s a human action for human satisfaction.

2. Consumer-oriented: A business exists to satisfy human needs, hence business must find out what the desire of customer (or consumer) and thereby produce goods & services as per the needs of the customer. Thus, only those goods should be produce that satisfy consumer needs and at a reasonable profit to the manufacturer (or producer).

3. Art as well as science: In the technological arena, marketing is the art and science of choosing target markets and satisfying customers through creating, delivering, and communicating superior customer value. It is a technique of making the goods available at right time, right place, into right hands, right quality, in the right form and at right price.

4. Exchange Process: All marketing activities revolve around commercial exchange process. The exchange process implies transactions between buyer and seller. It also involves exchange of technology, exchange of information and exchange of ideas.

5. Starts and ends with customers: Marketing is consumer oriented and it is crucial to know what the actual demand of consumer is. This is possible only when required information related to the goods and services is collected from the customer. Thus, it is the starting of marketing and the marketing end as soon as those goods and services reach into the safe hands of the customer.

6.Creation of Utilities: Marketing creates four components of utilities viz. time, place, possession and form. The form utility refers to the product or service a company offers to their customers. The place utility refers to the availability of a product or service in a location i.e. Easier for customers. By time utility, a company can ensure that products and services are available when customers need them. The possession utility gives customers ownership of a product or service and enables them to derive benefits in their own business.

7. Goal oriented: Marketing seeks to achieve benefits for both buyers and sellers by satisfying human needs. The ultimate goal of marketing is to generate profits through the satisfaction of the customer.

8. Guiding element of business: Modern Marketing is the heart of industrial activity that tells what, when, how to produce. It is capable of guiding and controlling business.

9. System of Interacting Business Activities: Marketing is the system through which a business enterprise, institution or organization interacts with the customers with the objective to earn profit, satisfy customers and manage relationship. It is the performance of business activities that direct the flow of goods and services from producer to consumer or user.

10 Marketing is a dynamic process: It is a series of interrelated functions. Marketing is a complex, continuous and interrelated process. It involves continuous planning, implementation and control.

MARKETING SCOPE

Some of the most important scope of marketing are as follows:

1. Goods
2. Services
3. Events
4. Experiences
5. Persons

6. Places
7. Properties
8. Organizations
9. Information
10. Idea.

The scope of marketing deals with the question, 'what is marketed?' **According to Kotler**, marketing people are involved with ten types of entities.

1. Goods: Physical goods constitute the major part of a country's production and marketing effort. Companies market billions of food products, and millions of cars, refrigerators, television and machines.

2. Services: As economies advance, a large proportion of their activities is focused on the production of services. Services include the work of airlines, hotels, car rental firms, beauticians, software programmers, management consultants, and so on. Many market offerings consist of a mix of goods and services. For example, a restaurant offers both goods and services.

3. Events: Marketers promote events. Events can be trade shows, company anniversaries, entertainment award shows, local festivals, health camps, and so on. For example, global sporting events such as the Olympics or Common Wealth Games are promoted aggressively to both companies and fans.

4. Experiences: Marketers create experiences by offering a mix of both goods and services. A product is promoted not only by communicating features but also by giving unique and interesting experiences to customers. For example, Maruti Sx4 comes with Bluetooth technology to ensure connectivity while driving, similarly residential townships offer landscaped gardens and gaming zones.

5. Persons: Due to a rise in testimonial advertising, celebrity marketing has become a business. All popular personalities such as film stars, TV artists, and sportspersons have agents and personal managers. They also tie up with PR agencies for better marketing of oneself.

6. Places: Cities, states, regions, and countries compete to attract tourists. Today, states and countries are also marketing places to factories, companies, new residents, real estate agents, banks and business associations. Place marketers are largely real estate agents and builders. They are using mega events and exhibitions to market places. The tourism ministry is also aggressively promoting tourist spots locally and globally.

7. Properties: Properties can be categorized as real properties or financial properties. Real property is the ownership of real estates, whereas financial property relates to stocks and bonds. Properties are bought and sold through marketing.

Marketing enhances the need of ownership and creates possession utility. With improving income levels in the economy, people are seeking better ways of saving money. Financial and real property marketing need to build trust and confidence at higher levels.

8. Organizations: Organizations actively work to build image in the minds of their target public. The PR department plays an active role in marketing an organization's image. Marketers of the services need to build the corporate image, as exchange of services does not result in the ownership of anything. The organization's goodwill promotes trust and reliability. The organization's image also helps the companies in the smooth introduction of new products.

9. Information: Information can be produced and marketed as a product. Educational institutions, encyclopedias, non-fiction books, specialized magazines and newspapers market information. The production, packaging, and distribution of information is a major industry. Media revolution and increased literacy levels have widened the scope of information marketing.

10. Idea: Every market offering includes a basic idea. Products and services are used as platforms for delivering some idea or benefit. Social marketers widely promote ideas. Maruti Udyog Limited promoted safe driving habits, need to wear seat belts, need to prohibit children from sitting near the driver's seat, and so on.

MARKETING MYOPIA

The term 'marketing myopia' was first expressed in a famous article of the same name written by **Theodore Levitt** for the **Harvard Business Review in 1960**.

In 'Marketing Myopia,' Levitt argued that many companies incorrectly take a **shortsighted approach to marketing**, viewing it as merely a tool for selling products. Instead, he argued that companies should look at marketing from the consumer's point of view.

For example, a company that sells hiking boots should not define its marketing in terms of sales of hiking boots, but market itself as a company concerned with outdoor exploration and adventure.

When does marketing myopia strike in?

1.Company more focused on selling rather than building relationships with the customers.
2. Predicting growth without conducting proper research.
3. Mass production without knowing the demand.
4. Giving importance to just one aspect of the marketing attributes without focusing on what customer actually wants.
5. Not changing with the dynamic consumer environment

Business, according to Levitt, is actually a customer satisfying institution and hence should be based on customers' needs and desires.

Examples of Marketing Myopia:

1.Kodak lost much of its share to Sony cameras when digital cameras boomed and Kodak didn't plan for it.

2. Nokia losing its marketing share to android and IOS.

3. Hollywood didn't even tap the television market as it was focused just on movies.

4. Yahoo (worth $100 billion dollars in 2000) lost to Google and was bought by Verizon at approx. $5 billion (2016).

Marketing Myopia

Overseeing a broader holistic picture in business makes it more sustainable. Organizations should not only take care of their own product into account while gauging competition but also factor in other threats which might pop up because of being in that business. We should not fall a prey of myths like – population will grow our sales will grow. While diversifying, companies should look at all possibilities which serve the purpose of the business to their consumer rather than just looking at honing skills in one product.

IMPORTANT FEATURES OF MARKETING

Satisfy Needs and Wants: The main focus of all marketing activities is consumer satisfaction. When a group of individuals (potential customers) express their needs, the companies strive to satisfy these needs via marketing activities.

Creating a Market Offering: Then the companies must dedicate their efforts to create an ideal market offering based on their study of potential customers. This product/service offered must try to fulfil all of the requirements of the potential customer in a given market.

Customer Value: The customers buying decisions will be greatly dependant on the price of the product. It must satisfy their needs at the cost that they think is fair. So the sellers must add value to the product and price it accordingly, so the customer is willing and gets value for his price,

Exchange Mechanism: Marketing is not a one-way process. The seller must satisfy the needs of the buyer. And the buyer in an exchange must provide consideration for the goods/services, which can be money or something else. It must be an exchange mechanism

Difference between Market and Marketing

Market	Marketing
In this comparison Market is the narrower concept	Marketing is a much wider concept than market
Market is the point of interaction between buyers and sellers	Marketing is the social process by which human needs are identified and eventually satisfied
Market is a set-up, or a place, or a point of interaction	Marketing is a process involving roughly 12 activities
Market can be of many types based on the goods traded, quantity traded, geographical location etc	Marketing philosophy is generally uniform for any type of goods or services.

MARKETING CONCEPTS

There are 5 different concepts of marketing, each of which vary in the function that they deal with. For example – production concept deals with production and selling concept deals with selling. Each of the concept was developed as per the need of the market. As the market changed, so did the concepts of marketing. And today, we have an opportunity to look at all 5 concepts of marketing and what they represent.

- Production concept
- Product concept
- Selling concept
- Marketing concept
- Societal marketing concept

The article lists out the concepts of marketing in a very brief manner. You can click on each link to know more about each individual concept of marketing.

1) Production Concept
Consumers prefer products that are widely available and inexpensive. The production concept is more operations oriented than any other concept. Click here to read more about the Production Concept
2) Product Concept
Consumers favor products that offer the most quality, performance, or innovative features. The product concept believes in the consumer and it says the consumers are more likely to be loyal if they have more options of products or they get more benefits from the product of the company. Click here to read more about the Product Concept
3) Selling Concept
Consumers will buy products only if the company aggressively promotes or sells these products. Off course, in this era of marketing, we know that selling is not the only tactic to sell your product. You have to focus on marketing as well. Click here to read more about the Selling Concept
4) Marketing Concept
Focuses on needs/wants of target markets & delivering value better than competitors. The marketing concept believes in the pull strategy and says that you need to make your brand so strong that customers themselves prefer your brand over every other competitor. This can be achieved through marketing. Click here to read more about the Marketing Concept
5) Societal Marketing concept
Focuses on needs / wants of target markets & delivering value better than competitors that preserves the consumer's and society's well-being. Click here to read about the Societal Marketing concept.

Concept	Focus	Means	Ends
1. Product	Products	Quality product, reasonable price, little marketing effort	Achieve profits or objectives by products generating consumer demand
2. Selling	Products	Aggressive advertising and selling efforts	Achieve profits or objectives by generating sales volume
3. Marketing	Customer needs	Integrated marketing	Achieve profits or objectives through customer satisfaction
4. Societal-Marketing	Customer satisfaction and long run public welfare	Constant search for better products in terms of appeal and benefit	Satisfy organizational goals and responsibilities for society

MARKETING APPROACHES

The study of marketing has been approached in more than one way. To some it has meant to sell something at a shop or market place; to some it has meant the study of individual product and its movement in the market; to some it has meant the study of persons-wholesalers, retailers, agents etc., who move the products and to some it has meant the study of behaviour of commodity movement and the way the persons involved to move

them. The approach to the study of marketing has passed through several stages before reaching the present stage. There is a process of evolution in the development of these approaches.

To facilitate the study, these different approaches may be broadly classified as follows:

1. Product or Commodity Approach:

Under the commodity approach the focus is placed on the product or it is an approach on the marketing on commodity wise basis. In other words, the study relates to the flow of a certain commodity and its movement from the original producer right up to the ultimate customer. The subject-matter, under this study, is commodity.

When one studies the marketing on this basis—commodity approach, one must begin to study and analyses the problems relating to a commodity i.e., sources and conditions of supply, nature and extent of demand, mode of transporting, storage, standardization, packing etc. Again, take an example of a commodity, say rice.

One has to study the sources of rice, location, people involved in buying and selling, means of transport, problems of selling the product, financing, storage, packing etc. Thus, we get a full picture of the marketing from the original producer to the ultimate consumer. The method of study is repeated for each item.

The system claims that it is simple and gives good result over the marketing of each product; description study is possible. But at the same time this approach is time-consuming and repetitive process which is a drawback.

2. Institutional Approach:

In the institutional approach, the focus is on the study of institutions- middlemen, wholesalers, retailers, importers, exporters, agencies, warehousing etc., engaged in the marketing during the movement of goods. The approach is also known as middlemen approach. Here, emphasis is given to understand and analyses the functions of institutions, who are discharging their marketing functions.

The activities of each institution form a part of marketing and collectively complete the marketing functions. In the process of moving the goods from the producer to the final consumers, a large number of persons are engaged. This system pays attention to the problems and functions of marketing institutions-transporting, banks and other financial institutions, warehousing, advertising, insurance etc. This method does not give adequate knowledge of the entire marketing functions and also' fails to explain the interrelations of different institutions.

3. Functional Approach:

The functional approach gives importance on the various functions of marketing. In other words, one concentrates attention on the specialized services or functions performed by marketers. In this approach, marketing splits into many functions-buying, selling, pricing, standardization, storage, transportation, advertising, packing etc. This may be studied one after another. Here each function is studied in detail in order to understand it and analyses the nature, need and importance of each function.

In this approach, marketing is regarded as "business of buying and selling and as including those business activities involved in the flow of goods and services between producers and customers." This system gives too much importance to various marketing functions and fails to explain how such functions are applied to the specific business operations.

4. Management Approach:

This approach is the latest and scientific. It concentrates upon the activities or marketing functions and focuses on the role of decision-making at the level of firm. This approach is mainly concerned with how managers handle specific problems and situations. It aims through evaluation of current market practices to achieve specific marketing objectives.

Generally there are two factors-controllable and uncontrollable, which are more concerned with the decision-making. Controllable include price adjustment, advertisement etc. Uncontrollable-economical, sociological, psychological, political etc. are the basic causes for market changes. And these changes cannot be controlled by any firm.

But controllable can be controlled by the firm. The uncontrollable limit the marketing opportunities. As such, managerial approach is concerned with the study of uncontrollable and then taking decisions for controllable within the scope set by uncontrollable. Managerial or decision-making approach emphasizes on the practical aspects of marketing, but ignores the theoretical aspects of marketing. At the same time, this approach, provides an overall information of the entire business.

5. System Approach:

The system approach can be defined as "a set of objects together with the relationships among them and their attributes." Systems focus on interrelations and interconnections among the functions of marketing. The system examines marketing connections (linkage) inside as well as outside the firm. Inside the firm there is a co-ordination of business activities-engineering, production, marketing, price etc.

On the basis of feedback information proper control is exercised to modify or alter in the producing process, so that the desired output can be produced. Here, the aim is to secure profit through customer-satisfaction. Markets can be understood only through the study of marketing information. For instance, business is composed of many functions, which are composed of sub functions. Each function or sub-function is independent, but interrelated and enables the other to achieve marketing objectives.

6. Societal Approach:

This approach has been originated recently. The marketing process is regarded as a means by which society meets its own consumption needs. This system gives no importance as to how the business meets the consumer's needs. Therefore, attention is paid to ecological factors (sociological, cultural, legal etc.) and marketing decisions and their impact on the society's well-being.

7. Legal Approach:

This approach emphasizes only one aspect i.e., transfer of ownership to buyer: It explains the regulatory aspect of marketing. In India, the marketing activities are largely controlled by Sales of Goods Act, Carrier Act etc. The study is concentrated only on legal aspects, leaving other important aspects. This does not give an idea of marketing.

8. Economic Approach:

This approach deals with only the problems of supply, demand and price. These are important from the economic point of view, but fail to give a clear idea of marketing.

MARKETING UTILITIES

Four marketing utilities, which are the capacities of the product offering to satisfy the needs of a customer, are enhanced when exchange occurs.

These include:

Form Utility - The product is produced, or modified for the customer. An example of this might be a car manufacturer designing their car so that a driver will be able to plug in his I-pod or other devices.

Time Utility - The consumers ability to buy the product when he or she wants to buy the product. A grocer may store certain amounts of certain foods until the prime season they are bought. It is ensuring customers will have access to the food when they most desire them.

Place Utility - This describes when a consumer is able to buy the product at a location that is convenient to him or her. The best example of this is online sales. Home is the most convenient location for a consumer.

Possession Utility - Ownership of the product is transferred from the marketer to the buyer. An example is a getting a loan and then buying a car.

TRADITIONAL VS. INTEGRATED MARKETING

To understand the fundamentals of marketing, it is important to understand two different approaches used when a company chooses to introduce a new product. Here we see traditional and integrated marketing.

There are typically 5 different departments directly involved with the product during creation and launch: Development, Engineering, Production, Marketing, and Distribution.

If a company opts to use a **traditional approach**, all of these departments work as separate entities. For example, development will draw up a product and then pass it along to engineering to create it. Engineering will then pass it along to production mass produce it. They will afterwards pass it to marketing, who will eventually move the product to distribution for a product launch.

If a firm opts to utilize an **integrated marketing approach**, all of the departments work together as a single unit. Engineering will not begin a product without ensuring that production has the capabilities to produce it. Development will check with marketing to ensure the product is line with the company image and approach. Basically, every department will at some point integrate their work with all other departments in the process.

Clearly, integrated marketing is the better approach. While it may take longer to launch a product, the likelihood of success is greater. The traditional approach leaves much room for interdepartmental conflicting interest and is therefore regarded as an outdated approach in marketing. It all too often ignores the consumers needs. The integrated marketing approach helps a business work collectively as one unit.

PERCEIVED VALUE AND SATISFACTION

A customers perceived value is equal to the benefits derived divided by the costs.

Value = Benefits/Costs

Further, benefits can include functional and emotional benefits. Costs may include monetary costs, time costs, energy costs, and psychic costs.

So,

Value =

Functional benefits + emotional benefits / monetary cost + time cost + energy cost + psychic costs

Satisfaction is a person's feelings of pleasure or disappointment resulting from comparing a products performance in relation to the person's expectations of performance.

Most expectations are derived from past buying experiences, friends, the marketer, peers, competitors, and promises of performance. It is also important to keep in mind that a person is twice as likely to tell others about a negative product or experience than they are about a good product or positive experience. Dissatisfied customers can also have a negative impact on employee morale.

UNIT-9: LEGAL ASPECTS OF BUSINESS

UGC NET COMMERCE

Dr. Gaurav jangra
www.easynotes4u.com
EasyNotes4U Academy, Hisar, Haryana

LEGAL ASPECTS OF BUSINESS
UNIT-I
LAW OF CONTRACT

Indian Contract Act 1872

Nature of Contract

A contract is a written or expressed agreement between two parties to provide a product or service. There are essentially six elements of a contract that make it a legal and binding document. In order for a contract to be enforceable, it must contain:

a. An offer that specifically details exactly what will be provided
b. Acceptance, which is the agreement by the other party to the offer presented
c. Consideration, money or something of interest being exchanged between the parties
d. Capacity of the parties in terms of age and mental ability
e. The intent of both parties to carry out their promise
f. Legally enforceable terms and conditions, also called object of the contract

In other words, a contract is enforceable when both parties agree to something, back the promise up with money or something of value, both are in sound mind and intend to carry out their promise and what they promise to do is within the law.

A contract is written and signed by the parties. However, there are several other types of contracts that are considered enforceable. There are even some that are not considered enforceable and serve only as a way for a court to determine the obligation on the part of either party.

Express Contract

An express contract is the most common contract type. In this type of contract, all elements are specifically stated. This can be written or done orally. Either way, offer, acceptance and consideration must bind the parties together legally. And both parties must clearly understand the terms and conditions each is agreeing to.

An oral contract works the same way. In an oral contract, like negotiating the price of a new car, the parties agree on a set price, a monthly payment schedule if applicable and any warranties or guaranties included in the offer. Once acceptance is made and consideration is exchanged, the contract for the vehicle is binding and enforceable. As long as both parties uphold their promise, the car cannot be returned at a later date, nor can the salesman request the car back from the new owner.

Implied In-Fact Contract

Not every contract is as transparent as an expressed contract. An implied in-fact contract binds parties together through a mutual agreement and intent, but there are no expressed terms of the agreement. The agreement holds mutual intention based on facts and

circumstances and a reasonable assumption from the circumstances and relations between the parties. For an implied in-fact contract to be enforceable, there are a few elements that must be present:

1. An unambiguous offer and acceptance
2. Mutuality of both parties to be bound to the contract

Consideration

The elements can be determined by the behaviors of the parties. For example, when a guest orders a steak at a restaurant, it is assumed that the steak will be cooked and served to the guest's liking and the guest has every intention of paying for the meal.

Implied In-Law Contract

An implied in-law contract, also known as a quasi-contract, works differently. In this type of contract, the elements are not specifically written or expressed. In fact, this type of contract is used as a remedy in a situation when one party to the quasi-agreement received unjust enrichment resulting from not paying for a product or service rendered. This sounds confusing but it really boils down to this - if a product or service is rendered to a party without paying, it becomes inequitable for the rendering party.

Contract Act

The Indian Contract Act, 1872 defines the term “Contract” under its section 2 (h) as “An agreement enforceable by law”. In other words, we can say that a contract is anything that is an agreement and enforceable by the law of the land.
This definition has two major elements in it i.e. – “agreement” and “enforceable by law”. So in order to understand a contract in the light of The Indian Contract Act, 1872 we need to define and explain these two pivots in the definition of a contract.

Agreement

The Indian Contract Act, 1872 defines what we mean by “Agreement”. In its section 2 (e), the Act defines the term agreement as “every promise and every set of promises, forming the consideration for each other”. Now that we know how the Act defines the term “agreement”, there may be some ambiguity in the definition of the term promise.
Examples

1. Mohan and Rishabh decided to go for lunch on Sunday. Mohan did not come for lunch, and this resulted in the waste of Rishabh’s time. Now Rishabh cannot compel Mohan for the damages as the decision to go for the lunch is not a contract but a domestic agreement.
2. Varun promises his younger brother Anuj to pay his debts, and the agreement was in writing as well as registered. This is a valid agreement and can be enforceable.

Promise

This ambiguity is removed by the Act itself in its section 2(b) which defines the term “promise” here as: “when the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. Proposal when accepted becomes a promise”.
In other words, an agreement is an accepted promise, accepted by all the parties involved in the agreement or affected by it. This definition thus introduces a flow chart or a sequence of steps that need to be triggered in order to establish or draft a contract. The steps may be described as under:
The definition requires a person to whom a certain proposal is made.
The person (parties) in step one has to be in a position to fully understand all the aspects of a proposal. “Signifies his assent thereto” – means that the person in point one accepts or agrees with the proposal after having fully understood it. Once the “person” accepts the proposal, the status of the proposal changes to “accepted proposal”.
“Accepted proposal” becomes a promise. Note that the proposal is not a promise. For the proposal to become a promise, it has to be accepted first.
Thus, in other words, an agreement is obtained from a proposal once the proposal, made by one or more of the participants affected by the proposal, is accepted by all the parties addressed by the agreement. To sum up, we can represent the above information below:

Agreement = Offer + Acceptance.

Enforceable By Law
Thus we can say that for an agreement to change into a Contract as per the Act, it must give rise to or lead to legal obligations or in other words must be within the scope of the law. Thus we can summarize it as Contract = Accepted Proposal (Agreement) + Enforceable by law (defined within the law)

Difference between Agreement and Contract

1. Promises and commitments forming consideration for the parties to the same consent are known as an agreement. The agreement, which is legally enforceable, is known as a contract.
2. The agreement is defined in section 2 (e) while a Contract is defined in section 2 (h) of the Indian Contract Act, 1872.
3. The major elements of an agreement are the offer and its acceptance by the same person to whom it is made, for adequate consideration. Conversely, the major elements of an agreement are agreement and its enforceability by law.
4. Every agreement is not a contract, but every contract is an agreement.
5. An agreement needs not to be given in writing, but the contracts are normally written and registered.
6. The agreement does not legally bind any party for the performance. In the Contract, the people are legally bound to perform their part.

7. The scope of the agreement is wider than a contract because it covers all types of agreement as well as contract. On the contrary, the scope of a contract is relatively narrower than an agreement because it covers only that agreement which have legal enforceability.

Types of contracts

1. Legal validity Express - Parties state the terms of the agreement to which they will be found, usually in writing.
2. Implied - Terms of agreement can be reasonably inferred by acts of the parties, even if not expressed in writing or orally.
3. Bilateral - All parties exchange promises to perform.
4. Unilateral - One party makes a promise in anticipation of some act. There is no reciprocal promise.
5. Executed - All parties have completed their promises.
6. Executory - Contract only partially performed or totally unperformed by the parties.

LEGAL VALADITY

1. Valid and enforceable - All elements of legal and binding contract present.
2. Void - Contract without legal force or effect.
3. Voidable - Contact that can be annulled by either party after signing because it is legally defective or allows one party to rescind the contract.
4. Unenforceable - A contract that cannot be verified for legal enforcement or fails to meet certain requirements.

Intention to Contract

There is no provision in the Indian Contract Act requiring that an offer or its acceptance should be made with the intention of creating a legal relationship. But in English law it is a settled principle that “to create a contract there must be a common intention of the parties to enter into legal obligations.”

Case law: Balfour v Balfour

The defendant and his wife were enjoying leave in England. When the defendant was due to return to Ceylon, where he was employed, and his wife was advised, by reason of her health, to remain in England. The defendant agreed to send her an amount of 30 pound a month for the probable expenses of maintenance. He did send the amount for some time, but afterwards differences arose which resulted in their separation and the allowance fell into arrears. The wife’s action to recover the arrears was dismissed.

General Offers: Performance of the conditions of a proposal, or the acceptance of any consideration for a reciprocal promise which may be offered with a proposal, is an acceptance of the proposal.

CASE: Carlil v Carbolic Smoke Ball Co

A company offered by advertisement to pay 100 pound to anyone “who contracts the increasing epidemic influenza, colds or any disease caused by taking cold, after having used the ball according to printed directions.” It was added that 1000 pound is deposited with the Alliance Bank showing our sincerity in the matter”. The plaintiff used the smoke balls according to the directions but she nevertheless subsequently suffered from influenza. She was held entitled to recover the promised reward.

General offer of continuing nature

Where a general offer is of continuing nature, as it was, for example, in the Smoke Ball case, it will be open for acceptance to any number of persons until it is retracted. But where an offer requires some information as to a missing thing, it is closed as soon as the first information comes in.

Offer and Invitation to Treat

An offer should be distinguished from an invitation to receive offers. When a man advertises that he has got a stock of books to sell, or houses to let, there is no offer to be bound by any contract. “Such advertisements are offers to negotiate – offers to receive offers – offers to chaffer”.

Essential Elements of a Contract

Essential Elements of a Contract as defined in Section 10 of the Indian Contract Act 1872

1. Agreement - Offer and Acceptance
2. Legal purpose
3. Lawful Consideration
4. Capacity to contract
5. Consent to contract
6. Lawful object
7. Certainty
8. Possibility of Performance
9. Not expressly declared void
10. Legal formalities like Writing, Registration etc

Acceptance – Section 2(b)

Introduction of Acceptance – Sec. 2 (b)

When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise.

Thus “acceptance” is the assent given to a proposal, and it has the effect of converting the proposal into promise.

This is another way of saying that an agreement is an accepted proposal. Every agreement, in its ultimate analysis, is the result of a proposal from one side and its acceptance by the other.

There are three factors in Acceptance:

1. Communication to Offeror
2. Communication to Acceptor
3. When Communication is not necessary

CASE: Brogden v Metropolitan Railway co.

B had been supplying coal to a railway company without any formal agreement. B suggested that a formal agreement should be drawn up. The agents of both the parties met and drew up a draft agreement. It had some blanks when it was sent to B for his approval. He filled up the blanks including the name of an arbitrator and then returned it to the company. The agent of the company put the draft in his drawer and it remained there without final approval having been signified. B kept up his supply of coals but on the new terms and also received payment on the new terms. A dispute having arisen B refused to be bound by the agreement.

WHEN COMMUNICATION NOT NECESSARY

In certain cases, communication of acceptance is not necessary. The offeror may inform a particular mode of acceptance, then all that the acceptor as to do is to follow that particular mode.

Case law: Carlil v Carbolic Smoke Ball

BOWEN LJ observed as: "But there is this clear gloss to be made upon that doctrine, that as notification of acceptance is required for the benefit of the person who makes the offer, he may dispense with notice to himself… and there can be no doubt that where the offeror expressly or impliedly intimates a particular mode of acceptance as sufficient to make the bargain binding it is only necessary for the other person to follow the indicated method of acceptance; and if the person making the offer expressly or impliedly intimates in his offer that it will be sufficient to act on the proposal without communicating acceptance of it to himself, performance of the condition is a sufficient acceptance without notification".

MODE OF COMMUNICATION

Acceptance should be made in prescribed manner. Acceptance has to be made in the manner prescribed or indicated by the offeror. An acceptance given in any other manner may not be effective. Particularly where the offeror clearly insists that the acceptance shall be made in the prescribed manner. For example, A offered to buy flour from B requesting that acceptance should be sent by the wagon which brought the offer. B sent his acceptance by post, thinking that this would reach the offeror more speedily. But the letter arrived after the time of the wagon. A was held to be not bound by the acceptance.

Absolute and Unqualified

Section 7: Acceptance Must Be Absolute

In order to convert a proposal into a promise, the acceptance must — (1) be absolute and unqualified, (2) be expressed in some usual and reasonable manner, unless the proposal prescribes the manner in which it is to be accepted.

EFFECT OF DEPARTURE FROM PRESCRIBED MANNER

A departure from that manner does not of itself invalidate the acceptance. A duty is cast on the offeror to reject such acceptance within reasonable time. A minor departure from the prescribed mode of communication should not upset the fact of acceptance provided that the communication is made in an equally expeditious way.

Where no manner prescribed: reasonable and usual manner

Where no mode of acceptance is prescribed, acceptance must "be expressed in some usual and reasonable manner". As per Indian Contract Law, post is a reasonable mode.

Counter proposals- An acceptance containing additions, limitations, or other modifications shall be rejection of the offer and shall constitute a counter-offer. However, a reply to an offer which purports to be an acceptance but which contains additional or different terms which do not materially alter the terms of the offer shall constitute an acceptance unless the offeror promptly objects to the discrepancy; if he does not object, the terms of the contract shall be the terms of the offer with the modifications contained in the acceptance.

If the proposal prescribes a manner in which it is to be accepted, and the acceptance is not made in such manner, the proposer may, within a reasonable time after the acceptance is communicated to him, insist that his proposal shall be accepted in the prescribed manner, and not otherwise; but if he fails to do so, he accepts the acceptance.

PARTIAL ACCEPTANCE

Acceptance should be of the whole of the offer. The offeree cannot accept a part of its terms which are favorable to him and reject the rest. Such an acceptance is another kind of counter proposal and does not bind the offeror.

INQUIRY INTO TERMS OF PROPOSAL

A mere inquiry into the terms of a proposal is not the same thing as a counter-proposal. On acceptance of the proposal, the contract will be created on the basis of the terms and conditions of the original proposal including arbitration clause.

ACCEPTANCE WITH CONDITION SUBSEQUENT

If an acceptance carries a condition subsequent, it may not have the effect of a counter-proposal. Thus, where an acceptance said: "terms accepted, remit cash down Rs.25, 000 by February 5, otherwise acceptance subject to withdrawal, this was not a counter-proposal, but an acceptance with a warning that if the money was not sent the contract would be deemed to have been broken.

ACCEPTANCE OF COUNTER PROPOSAL

Even "where the acceptance of a proposal is not absolute and unqualified the proposer may become bound, if, by his subsequent conduct, he indicates that he has accepted the qualifications set up".

Hargopal v People's Bank of Northern India-An application for shares was made conditional on an undertaking by the bank that the applicant would be appointed a permanent director of the local branch. The shares were allotted to him without fulfilling the

condition. The applicant accepted the position as a shareholder by accepting dividends, filing a suit to recover it and by pledging his shares.It was, therefore, held "that he could not content that the allotment was void on the ground of non-fulfillment of the condition as he had by his conduct waived the conditions.

Lapse of Offer

1. Notice of revocation
2. Lapse of Time
3. By failure to accept condition precedent
4. By death or insanity of offerer
5. Revocation of Acceptance

Revocation of proposals and acceptances (Section-5)-A proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards. An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

NOTICE OF REVOCATION
Withdrawal before expiry of fixed period where an offeror gives the offeree an option to accept within a fixed period, he may withdraw it even before the expiry of that period.
CASE LAW: Alfred Schonlank v. Muthunayna Chetti
The defendant left an offer to sell a quantity of indigo at the plaintiff's office allowing him eight days' time to give his answer. On the 4th day however the defendant revoked his proposal. The plaintiff accepted it on the 5th day. Holding the acceptance was useless.
CASE LAW: Mount ford v Scott
Communication of Revocation should be from Offerer Himself. It is necessary that the communication of revocation should be from the offeror or from his duly authorized agent. But it has been held in the case of Dickinson v. Dodds that it is not enough if the offeree knows reliably that the offer has been withdrawn.
Revocation of General Offers-Where an offer of a general nature is published through newspapers, it can be withdrawn by the same media and the revocation will be effective even if a particular person, subsequent to the withdrawal, happened to perform its terms in ignorance of the withdrawal.
CASE LAW: Skarsm Ramanathan v NTC Ltd
Superseding proposals by Fresh Proposal Where before acceptance a proposal is renewed in some parts of it and not in its entirety as proposed earlier and the letter purports it to supersede the earlier communication, such proposal is no longer available for acceptance.
LAPSE OF TIME
An offer lapses on the expiry of the time, if any, fixed for acceptance. Where an offer says that it shall remain open for acceptance up to a certain date, it has to be accepted within that date. For example, where an offer was to last until the end of March and the offeree sent a telegram accepting the offer on 28th March which was received by the offeror on 30th March, it was held that the option was duly exercised.
FAILURE TO ACCEPT CONDITION PRECEDENT
Where the offer is subject to a condition precedent, it lapses if it is accepted without fulfilling the condition. Where a salt lake was offered by way of lease on deposit of a sum of money within a specified period, and the intended lessee did not deposit the amount for 3 long years, it was held that this entailed cancellation of the allotment.
DEATH OR INSANITY OF OFFEROR
An offer lapses on the death or insanity of the offeror, provided that the fact comes to the knowledge of the offeree before he makes his acceptance. In the case of Dickinson v Dodds, it was held that an offer cannot be accepted after the death of the offeror.

SECTION 6: Revocation how made
A proposal is revoked —

1. By the communication of notice of revocation by the proposer to the other party;
2. By the lapse of the time prescribed in such proposal for its acceptance or, if no time is so prescribed, by the lapse of a reasonable time, without communication of the acceptance;
3. By the failure of the acceptor to fulfill a condition precedent to acceptance; or
4. By the death or insanity of the proposer, if the fact of his death or insanity comes to the knowledge of the acceptor before acceptance.

Revocation of Acceptance: An acceptor may cancel his acceptance by a speedier mode of communication which will reach earlier than the acceptance itself. Section 5 is the relevant provision.

Consideration [SECTION 2 (d) and SECTION 25]

Section 25 of the Indian Contract Act, 1872 starts with a declaration that "an agreement made without consideration is void"
Consideration is a price of the promise
Definitions
In the words of Pollock, "Consideration is the price for which the promise of the other is bought, and the promise thus given for value is enforceable."

Section 2(d) of the Indian Contract Act defines consideration as: When, at the desire of the promisor, the promisee or any other person has done or abstained from doing or does or abstains from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise.
It means price for which the promise of the other is bought – a valuable considerations a price of the promise – some of value received by the promisee as an inducement of the promise quid pro quo (something in return) – may be of some benefit to the plaintiff or some detriment to the defendant.
Abdul Aziz Vs. Masum Ali
A promise to subscribe Rs.500 for re-building a mosque – not fulfilled – secretary of mosque committee filed a suit for enforcement of promise – Held, the promise not enforceable as no consideration in the sense of benefit for the promisor – the secretary of the committee suffered no detriment as nothing has been done to carry out the repairs – no contract.
Essential Elements of a Valid Consideration

1. It must move at the desire of promisor
2. It may move from promisee or any other person (Privity of consideration)
3. It must be real, not illusory
4. It need not be adequate
5. It may be past, present or future
6. It must not be illegal, immoral or opposed to public policy

PROMISSORY ESTOPPEL-The doctrine of promissory estoppels prevents one party from withdrawing a promise made to a second party if the latter has reasonably relied on that promise.
Promissory estoppels require:

a. an unequivocal promise by words or conduct
b. evidence that there is a change in position of the promisee as a result of the promise (reliance but not necessarily to their detriment)
c. inequity if the promisor were to go back on the promise

In general, estoppels is ‘a shield not a sword’ — it cannot be used as the basis of an action on its own. It also does not extinguish rights.
ACTS DONE AT REQUEST:
An act done at the promisors desire furnishes a good consideration for his promise even though it is of no personal significance or benefit to him.
PROMISES OF CHARITABLE NATURE
Doraswami Iyer v Arunachala Ayyar
Facts: The repair of a temple was in progress. As the work proceeded, more money was required and to raise this money subscription were invited and a subscription list raised. The defendant put himself down on the list for Rs. 125 and it was to recover this sum that the suit was filed. The plaint found the consideration for the promise as a reliance on the promise of the subscriber that they have incurred liabilities in repairing the temple.
Judgment: The learned judge held that there was no evidence of any request by the subscriber to the plaintiff to do the temple repairs. Since, the temple repairs were already in progress when the subscriptions were invited. The action was not induced by the promise to subscribe but was rather independent of it. Hence, no recovery was allowed.
UNILATERAL PROMISES
A unilateral promise is a promise from one side only and is intended to induce some action by the other party. The promisee is not bound to act, for he gives no promise from his side. But if he carries out the act desired by the promisor, he can hold the promisor to his promise. “An act done at the request of the offeror in response to his promise is consideration, and consideration in its essence is nothing else but response to such a request.”
PROMISSORY ESTOPPEL AND GOVERNMENT AGENCIES
In Pournami Oil Mills v State of Kerala, the Government was not permitted to go back on its earlier promise of wider exemption from sales tax in pursuance of which certain industries were set up. A subsequent notification curtailing the exemption was held to be applicable to industries established after the notification. A promise which is against public policy or in violation of a statutory prohibition cannot be the foundation of estoppels.
Privity of Contract and of Consideration
“PROMISEE OR ANY OTHER PERSON”
It means that as long as there is a consideration for a promise, it is immaterial who has furnished it. It may move from the promisee, or, if the promisor has no objection, from any other person.
Dutton v Poole
Facts: A person had a daughter to marry and in order to provide her a marriage portion, he intended to sell a wood of which he was possessed at the time. His son (the defendant) promised that if “the father would forbear to sell at his request he would pay the daughter £1000”. The father accordingly forbore but the defendant did not pay. The daughter and her husband sued the defendant for the amount.
Judgment: The court held that if a man should say, ‘Give me a horse, I will give your son £10’, the son may bring the action, because the gift was upon the consideration of a profit to the son, and the father is obliged by natural affection to provide for his children. There was such apparent consideration of affection from the father to his children, for whom nature obliges him to provide, that the consideration and promise to the father may well extend to the children.

PRIVITY OF CONSIDERATION
According to Section 2(d), it is not necessary that consideration should be finished by the promisee. A promise is enforceable if there is some consideration for it and it is quite immaterial whether it moves from the promisee or any other person.
Chinnaya v Ramayya
An old lady, by deed of gift, made over certain landed property to the defendant, her daughter. By the terms of the deed, which was registered, it was stipulated that an annuity of Rs.653 should be paid every year to the plaintiff, who was the sister of the old woman. The defendant on the same day executed in plaintiff's favour an agreement promising to give effect to the stipulation. The annuity was however not paid and the plaintiff sued to recover it.
It was held that the deed of gift and the defendant's promise to pay the annuity were executed simultaneously and, therefore, they should be regarded as one transaction and there was sufficient consideration for that transaction.
EXECUTORY CONSIDERATION
"Such Act, Abstinence or Promise is called Consideration"
CONSIDERATION MUST BE OF SOME VALUE
Consideration as defined in the Act means some act, abstinence or promise on the part of the promisee or any other which has been done at the desire of the promisor. E.g., A promises to give his new Rolls-Royce car to B, provided B will fetch it from the garage. The act of fetching the car cannot by any stretch of imagination be called a consideration for the promise. Even though it is the only act, the promisor desired the promisee to do. Such an act no doubt satisfies the words of the definition, but it does not catch its spirit. It is for this reason that English common law insisted that "consideration must be of some value in the eyes of the law." It must be real and not illusory, whether adequate or not as long as the consideration is not unreal, it is sufficient if it be of slight value only.
VALUE NEED NOT BE ADEQUATE (ADEQUACY OF CONSIDERATION)
It is not necessary that consideration should be adequate to the promise. The courts cannot assume the job of settling what should be the appropriate consideration for a promise. It is up to the parties.
INADEQUACY AS EVIDENCE OF IMPOSITION
The act in Explanation 2 to Section 25 states that "inadequacy of consideration may be taken into account by the court in determining the question whether the consent of promisor was freely given. E.g.
A agrees to sell a horse worth Rs.1000 for Rs.10. A denies that his consent to the agreement was freely given. The inadequacy of the consideration is a fact which the court should take into account in considering whether or not A's consent was freely given.
FORBEARANCE TO SUE
Forbearance to sue has always been regarded as valuable consideration. It means that the plaintiff has a certain right of action against the defendant or any other person and on a promise by the defendant, he refrains from bring the action.
COMPROMISE GOOD IRRESPECTIVE OF MERITS
Compromise of a pending suit is a good consideration for the agreement of compromise. But the dispute should be bona fide. A compromise is a good consideration "irrespective of merits of the claim of either side" and even where there is some doubt in the minds of the parties as to their respective rights.
Performance of Existing Duties
PERFORMANCE OF LEGAL OBLIGATIONS
Consideration must be something more than what the promisee is already bound to do. Performance of a legal duty is no consideration for a promise.
PERFORMANCE OF CONTRACTUAL OBLIGATIONS
A. Pre-existing Contract with Promisor: Compliance with legal obligation imposed by a contract with the promisor can be no consideration for a promise.
Promise to pay less than amount due: A promise to pay less than what is due under a contract cannot be regarded as a consideration.
CONSIDERATION AND MOTIVE
Consideration should be distinguished from motive or a pious desire to fulfil an obligation. "Motive is not the same thing with consideration."
Thomas v Thomas
Facts: "A testator, on the death of his death, had verbally said in front of witnesses that he was desirous that his wife should enjoy certain premises for her life. The executors, who were also the assignees, "in consideration of such desire and of the premises," agreed with the widow to convey the premises to her provided she would pay to the executors the sum of 1 pound yearly towards the ground rent and keep the said house in repair.
Court Held: On the question of consideration for the agreement between the executors and the widow the court pointed out that the motive for the agreement was, unquestionably, respect for the wishes of the testator. But that was no part of the legal consideration for the agreement. Motive should not be confounded with consideration. The agreement was, however, held to be binding as the undertaking to pay the ground rent was a sufficient consideration.
Exceptions to Consideration
An agreement made without consideration is void unless –
(1) It is in writing and registered
(2) Or is a promise to compensate for something done

Natural love and affection: A written and registered agreement based on natural love and affection between near relatives is enforceable without consideration. E.g., A family settlement between a man and his wife was made for providing maintenance to wife. This was held to be enforceable because it was meant for deriving satisfaction and peace of mind from family harmony.
Past voluntary service: A promise to compensate wholly or in part, a person who has already voluntarily done something for the promisor, is enforceable.
Time-barred debt: A promise to pay a time-barred debt is enforceable. The promise should be in writing. It should also be signed by the promisor or by his agent generally or specially authorized in that behalf.

One of the most essential elements of a valid contract is the competence of the parties to make a contract. Section 11 of the Indian Contract Act, 1872, defines the capacity to contract of a person to be dependent on three aspects; attaining the age of majority, being of sound mind, and not disqualified from entering into a contract by any law that he is subject to. In this article, we will look at all aspects in a detailed manner.

Capacity to Contract

One of the most essential elements of a valid contract is the competence of the parties to make a contract. Section 11 of the Indian Contract Act, 1872, defines the capacity to contract of a person to be dependent on three aspects; attaining the age of majority, being of sound mind, and not disqualified from entering into a contract by any law that he is subject to. In this article, we will look at all aspects in a detailed manner. According to Section 11, "Every person is competent to contract who is of the age of majority according to the law to which he is subject, and who is of sound mind and is not disqualified from contracting by any law to which he is subject."
The three main aspects:

- Attaining the age of majority
- Being of sound mind
- Not disqualified from entering into a contract by any law that he is subject to

1] Attaining the Age of Majority

According to the Indian Majority Act, 1875, the age of majority in India is defined as 18 years. For the purpose of entering into a contract, even a day less than this age disqualifies the person from being a party to the contract. Any person, domiciled in India, who has not attained the age of 18 years, is termed as a minor. Certain laws governing a minor's agreement:

A Contract made with a Minor is Void

Since any person less than 18 years of age does not have the capacity to contract, any agreement made with a minor is void ab-initio (from the beginning).
Peter is 17 years and 6 months old. He needs some money to go for a vacation with his friends. He approached a moneylender and borrows Rs 25,000. As security, he signs some papers mortgaging his laptop and motorcycle. Six months later, when he attains the age of majority, he files a suit declaring that the mortgage executed by him when he was a minor is void and should be canceled. The Court agrees and relieves Peter of all liability to repay the loan.
Also, if a minor enters into a contract, then he cannot ratify it even after he attains majority since the contract is void ab-initio. And, a void agreement cannot be ratified.

A Minor can be a Beneficiary of a Contract

While a minor cannot enter a contract, he can be the beneficiary of one. Section 30 of the Indian Partnership Act, 1932, also specifies that while a minor cannot become a partner in the partnership firm, the benefits of the firm can be extended to him.
Peter lends some money to his neighbor, John and asks him to mortgage his house as security. John agrees and the mortgage deed is made favoring Peter's 10-year-old son – Oliver. John fails to repay the loan and Peter, as the natural guardian of Oliver, files a suit against John to recover his money. The Court holds the case since a minor an be a beneficiary of a contract.

A Minor is always given the Benefit of being a Minor

Even if a minor falsely represents himself as a major and takes a loan or enters into a contract, he can plead minority. The rule of estoppels cannot be applied against a minor. He can plea his minority in defense.

Contract by Guardian

Under certain circumstances, a guardian of a minor can enter into a valid contract on behalf of the minor. Such a contract, which the guardian enters into, for the benefit of the minor, can also be enforced by the minor.
However, guardians cannot bind a minor by a contract for buying immovable property. But, a contract entered into by a certified guardian of a minor, appointed by the Court, with an approval from the Court for the sale of a minor's property can be enforced.

Insolvency

A minor cannot be declared insolvent as he cannot avail debts. Also, if some dues are pending from the properties of the minor and he is not personally liable for the same.

Joint contract by a Minor and an Adult

In case of a joint contract between an adult and a minor, executed by the guardian on behalf of the minor, the liability of the contract falls on the adult.

2] Person of Sound Mind

According to Section 12 of the Indian Contract Act, 1872, for the purpose of entering into a contract, a person is said to be of sound mind if he is capable of understanding the contract and being able to assess its effects upon his interests. It is important to note that a

person, who is usually of an unsound mind, but occasionally of a sound mind, can enter a contract when he is of sound mind. No person can enter a contract when he is of unsound mind, even if he is so temporarily. A contract made by a person of an unsound mind is void.

3] Disqualified Persons

Apart from minors and people with unsound minds, there are other people who cannot enter into a contract. i.e. do not have the capacity to contract. The reasons for disqualification can include political status, legal status, etc. Some such persons are foreign sovereigns and ambassadors, alien enemy, convicts, insolvents, etc.

Disqualified Persons

Persons not eligible to enter into a contract: Apart from minors and persons of unsound mind, the following persons are not eligible to enter into a contract in certain circumstances:

- Alien Enemies,
- Foreign Sovereigns,
- Insolvents,
- Body Corporate,
- Convicts.

Agreements with Disqualified Persons

1. Aliens: Alien means a person of a foreign country.
a. Alien friend: Contracts with alien friend (persons of a foreign country which is in peace with India) are valid subject to some restrictions.
b. Alien enemy: Contracts with alien enemy (persons of a country which is in war with India) are void subject to following rules:
i. Contracts made during war period: During war period (i.e., after the war is declared), an alien enemy can neither make a contract with an Indian, nor can sue in an Indian court, unless permitted by Central Government.
ii. Contracts made before war: Such contracts may be suspended (or dissolved if against public policy or it would benefit the enemy country).
2. Foreign Sovereigns: Diplomatic staff may enter into contract and can sue. They enjoy some special privilege and cannot be sued in Indian court unless they voluntarily submit to the court or when permitted by Central Government to be sued.
3. Insolvents: Insolvent cannot enter into a contract. When a debtor is adjudged insolvent, his property is vested with the official assignee, which only can then enter into contracts relating to the property of the insolvent.
4. Body Corporate: A Company or Body Corporate may enter into contract as permitted by its Memorandum of Association & Articles of Association.
5. Convicts: A convict undergoing imprisonment cannot enter into a contract unless permitted by Central Govt. He can enter into a contract when he is lawfully at large, when he is pardoned or when his period of sentence expires. A contract already entered with a person who undergoes imprisonment cannot be enforced until the conviction is completed, unless permission from Central Government is obtained.

Free Consent

In the Indian Contract Act, the definition of Consent is given in Section 13, which states that "it is when two or more persons agree upon the same thing and in the same sense". So the two people must agree to something in the same sense as well. Let's say for example A agrees to sell his car to B. A owns three cars and wants to sell the Maruti. B thinks he is buying his Honda. Here A and B have not agreed upon the same thing in the same sense. Hence there is no consent and subsequently no contract. Free Consent has been defined in Section 14 of the Act. The section says that consent is considered free consent when it is not caused or affected by the following,

- Coercion
- Undue Influence
- Fraud
- Misrepresentation
- Mistake

Elements Vitiating Free Consent

The following are the essentials of Free Consent:

1] Coercion (Section 15): Coercion means using force to compel a person to enter into a contract. So force or threats are used to obtain the consent of the party under coercion, i.e it is not free consent. Section 15 of the Act describes coercion as

- committing or threatening to commit any act forbidden by the law in the IPC
- unlawfully detaining or threatening to detain any property with the intention of causing any person to enter into a contract

For example, A threatens to hurt B if he does not sell his house to A for 5 lakh rupees. Here even if B sells the house to A, it will not be a valid contract since B's consent was obtained by coercion. Now the effect of coercion is that it makes the contract voidable. This means the contract is voidable at the option of the party whose consent was not free. So the aggravated party will

decide whether to perform the contract or to void the contract. So in the above example, if B still wishes, the contract can go ahead. Also, if any monies have been paid or goods delivered under coercion must be repaid or returned once the contract is void. And the burden of proof proving coercion will be on the party who wants to avoid the contract. So the aggravated party will have to prove the coercion, i.e. prove that his consent was not freely given.

2] Undue Influence (Section 16)

Section 16 of the Act contains the definition of undue influence. It states that when the relations between the two parties are such that one party is in a position to dominate the other party, and uses such influence to obtain an unfair advantage of the other party it will be undue influence. The section also further describes how the person can abuse his authority in the following two ways,

- When a person holds real or even apparent authority over the other person. Or if he is in a fiduciary relationship with the other person
- He makes a contract with a person whose mental capacity is affected by age, illness or distress. The unsoundness of mind can be temporary or permanent

For example A sold his gold watch for only Rs 500/- to his teacher B after his teacher promised him good grades. Here the consent of A (adult) is not freely given, he was under the influence of his teacher. Now undue influence to be evident the dominant party must have the objective to take advantage of the other party. If influence is wielded to benefit the other party it will not be undue influence. But if consent is not free due to undue influence, the contract becomes voidable at the option of the aggravated party. And the burden of proof will be on the dominant party to prove the absence of influence.

3] Fraud (Section 17): Fraud means deceit by one of the parties, i.e. when one of the parties deliberately makes false statements. So the misrepresentation is done with full knowledge that it is not true, or recklessly without checking for the trueness, this is said to be fraudulent. It absolutely impairs free consent. According to Section 17, a fraud is when a party convinces another to enter into an agreement by making statements that are

- suggesting a fact that is not true, and he does not believe it to be true
- active concealment of facts
- a promise made without any intention of performing it
- any other such act fitted to deceive

Example- A bought a horse from B. B claims the horse can be used on the farm. Turns out the horse are lame and A cannot use him on his farm. Here B knowingly deceived A and this will amount to fraud.

One factor to consider is that the aggravated party should suffer from some actual loss due to the fraud. There is no fraud without damages. Also, the false statement must be a fact, not an opinion. In the above example if B had said his horse is better than C's this would be an opinion, not a fact. And it would not amount to fraud.

4] Misrepresentation (Section 18)

Misrepresentation is also when a party makes a representation which is false, inaccurate, incorrect etc. The difference here is the misrepresentation is innocent, i.e. not intentional. The party making the statement believes it to be true. Misrepresentation can be of three types

- A person makes a positive assertion believing it to be true
- Any breach of duty gives the person committing it an advantage by misleading another. But the breach of duty is without any intent to deceive
- When one party causes the other party to make a mistake as to the subject matter of the contract. But this is done innocently and not intentionally.

5] Mistake

When one of the parties has given its consent to the contract under some kind of misunderstanding then the consent is said to be have been given by mistake. If it wasn't for the misunderstanding the party would not have entered into the agreement. Under contract law, a mistake can of two kinds: 1) Mistake of Law and 2) Mistake of Fact.

Mistake of Law

When the party has any misunderstanding with regards to the legal provisions, it is called Mistake of Law. Now, the party can be confused regarding the law of the Homeland or law of a foreign land. If it is a mistake regarding the law of the homeland, the contract cannot be avoided. The party cannot take the plea of having no knowledge of laws of his homeland. But if it is a mistake regarding the law of a foreign country, he can be excused.

Mistake of Fact

When the parties have any misunderstanding regarding the subject matter or terms of the contract, it is said to be a Mistake of fact. The misunderstanding can be on the part of one party or both of them.

Bilateral Mistake – When both the parties are under any misunderstanding/mistake relating to a matter of fact essential to the agreement, the agreement becomes void.

Unilateral Mistake – When the misunderstanding/mistake is on the part of one party to the contract, the agreement remains valid. Only when the party is mistaken about the parties to agreement or nature of the transaction, the agreement becomes void.

Conclusion

Free Consent is absolutely essential to make an agreement a valid contract. The importance of free consent cannot be stressed enough. Consent of the parties to the contract must be free and voluntarily. Consent to the contract has to be given without any kind of pressure or delusions. It is important that the consent given by the parties is free as this can affect the validity of the

SUBJECT:
UGC NET COMMERCE

UNIT-10:
INCOME TAX AND CORPORATE TAX PLANNING

Chapter No.	Title	Page No.
1	**Income-tax: Basic concepts –** Residential status and tax incidence; Exempted incomes; Agricultural income; Computation of taxable income under various heads; Deductions from Gross total income; Assessment of Individuals; Clubbing of incomes	**3-21**
2	**Corporate Tax Planning:** Concepts and significance of corporate tax	**22-30**

	planning; Tax avoidance versus tax evasion; Techniques of corporate tax planning	
3	**Tax Planning and Financial Management Decisions:** Retain; Renewal or replacement of asset; Shut down or continue operations	**31-33**
4	**Tax Management with Reference to-** planning; Tax considerations in specific business situations: Make or buy decisions; Own or lease an asset;	**34-36**
5	**International Taxation:** Double taxation and its avoidance mechanism; Transfer pricing	**37-39**
6	**Deduction and collection of tax at source**	**40-42**
7	**Advance payment of tax**	**43-49**
8	**E-filing of income-tax returns**	**50-55**
	MCQs	**56-65**
	Special Notes	**66-69**

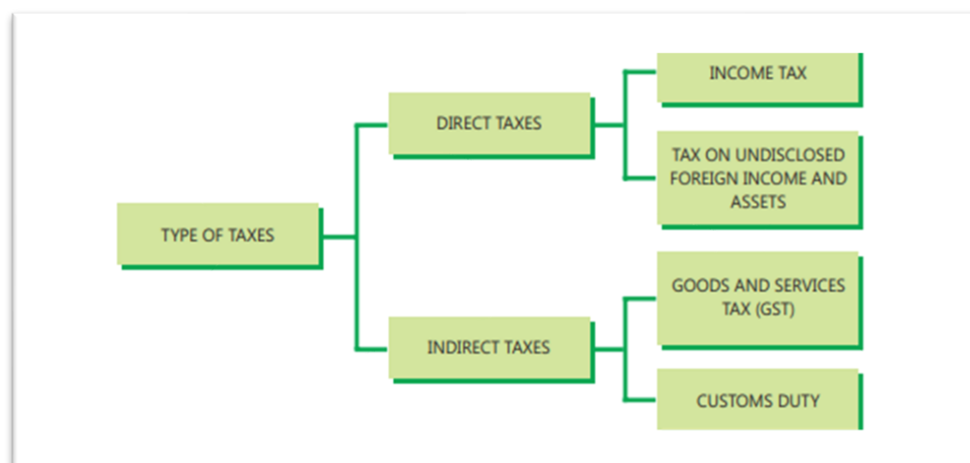
CHAPTER-1: INCOME-TAX- BASIC CONCEPTS

INTRODUCTION

Tax is a fee charged by a Government on a product, income or activity. There are two types of taxes – direct taxes and indirect taxes.

Direct Taxes: If tax is levied directly on the income or wealth of a person, then, it is a direct tax e.g. income-tax.

Indirect Taxes: If tax is levied on the price of a good or service, then, it is an indirect tax e.g. Goods and Services Tax(GST) or Custom Duty. In the case of indirect taxes, the person paying the tax passes on the incidence to another person.

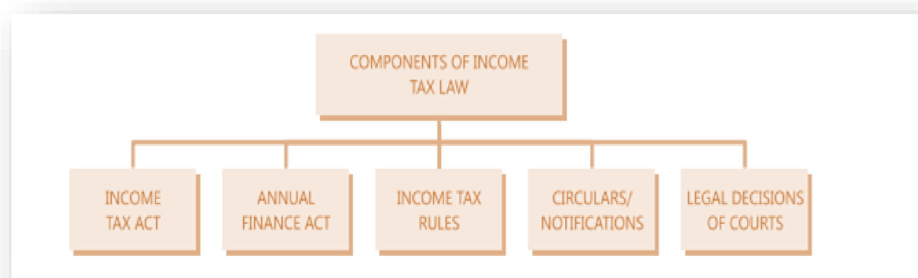


The reason for levy of taxes is that they constitute the basic source of revenue to the Government. Revenue so raised is utilized for meeting the expenses of Government like defence, provision of education, health-care, infrastructure facilities like roads, dams etc. Constitution of India gives the power to levy and collect taxes, whether direct or indirect, to the Central and State

Government. The Union and State Government are empowered to levy taxes by virtue of Article 246 of the Constitution of India.
Seventh Schedule to Article 246 contains three lists which enumerate the matters under which the Union and the State Governments have the authority to make laws for the purpose of levy of taxes.
The following are the lists:
(i) Union List: Central Government has the exclusive power to make laws on the matters contained in Union List.
(ii) State List: State Government has the exclusive power to make laws on the matters contained in the State List.
(iii) Concurrent List: Both Central and State Governments have the power to make laws on the matters contained in the Concurrent list.
Income-tax is the most significant direct tax. Entry 82 of the Union List i.e., List I of Seventh Schedule to Article 246 of the Constitution of India has given the power to Central Government to levy taxes on income other than agricultural income.

OVERVIEW OF INCOME-TAX LAW IN INDIA

In this material, we would be introducing the students to the Income-tax law in India.
The income-tax law in India consists of the following components–



The various instruments of law containing the law relating to income-tax are explained below:

Income-tax Act, 1961

The levy of income-tax in India is governed by the Income-tax Act, 1961. In this book we shall briefly refer to this as the Act.
- It came into force on 1st April, 1962.
- It contains 298 sections and XIV schedules.

A section may have sub-sections, clauses and sub-clauses. For example,
The clauses of section 2 define the meaning of terms used in the Income-tax Act, 1961. Clause (1A) defines "agricultural income", clause (1B) defines "amalgamation" and so on.
Likewise, the clauses of section 10 contain the exemptions in respect of certain income, like clause (1) provides for exemption of agricultural income and clause

(2) provides for exemption of share income of a member of a hindu undivided family and so on.
Section 5 defining the scope of total income has two sub-sections (1) and (2). Sub-section (1) defines the scope of total income of a resident and sub-section (2) defines the scope of total income of a non-resident.

A section may also have Provisos and Explanations.

The Proviso(s) to a section/sub-section/clause spells out the exception(s) to the provision contained in the respective section/subsection/clause.

The Explanation to a section/sub-section/clause gives a clarification¬ relating to the provision contained in the respective section/subsection/clause.

For example,

Sections 80GGB and 80GGC provides for deduction from gross total income in respect of contributions made by companies and other persons, respectively, to political parties or an electoral trust

The proviso to sections 80GGB and 80GGC provide that no deduction shall be allowed under those sections in respect of any sum contributed by cash to political parties or an electoral trust. Thus, the proviso to these sections spells out the circumstance when deduction would not be available thereunder in respect of contributions made.

o The Explanation below section 80GGC provides that for the purposes of sections 80GGB and 80GGC, "political party" means a political party registered under section 29A of the Representation of the People Act, 1951. Thus, the Explanation clarifies that the political party has to be a registered political party.

• The Income-tax Act, 1961 undergoes change every year with additions and deletions brought out by the annual Finance Act passed by Parliament.

The Finance Act

Every year, the Finance Minister of the Government of India introduces the Finance Bill in the Parliament's Budget Session. When the Finance Bill is passed by both the houses of the Parliament and gets the assent of the President, it becomes the Finance Act. Amendments are made every year to the Income-tax Act, 1961 and other tax laws by the Finance Act.

The First Schedule to the Finance Act contains four parts which specify the rates of tax –

• Part I of the First Schedule to the Finance Act specifies the rates of tax applicable for the current Assessment Year.

• Part II specifies the rates at which tax is deductible at source for the current Financial Year.

• Part III gives the rates for calculating income-tax for deducting tax from income chargeable under the head "Salaries" and computation of advance tax.

• Part IV gives the rules for computing net agricultural income.

Income-tax Rules, 1962

The administration of direct taxes is looked after by the Central Board of Direct Taxes (CBDT).

• The CBDT is empowered to make rules for carrying out the purposes of the Act.

• For the proper administration of the Income-tax Act, 1961, the CBDT frames rules from time to time. These rules are collectively called Income-tax Rules, 1962.

• Rules also have sub-rules, provisos and Explanations. The proviso to a Rule/ Sub-rule spells out the exception to the limits, conditions, guidelines, basis of valuation, as the case may be, spelt out in the Rule/Sub-rule. The Explanation gives clarification for the purposes of the Rule.

• It is important to keep in mind that along with the Income-tax Act, 1961, these rules should also be studied.

Circulars and Notifications

Circulars

• Circulars are issued by the CBDT from time to time to deal with certain specific problems and to clarify doubts regarding the scope and meaning of certain provisions of the Act.

• Circulars are issued for the guidance of the officers and/or assessees.

• The department is bound by the circulars. While such circulars are not binding on the assessees, they can take advantage of beneficial circulars.

Notifications

Notifications are issued by the Central Government to give effect to the provisions of the Act. The CBDT is also empowered to make and amend rules for the purposes of the Act by issue of notifications.

Case Laws

The study of case laws is an important and unavoidable part of the study of Income-tax law. It is not possible for Parliament to conceive and provide for all possible issues that may arise in the implementation of any Act. Hence the judiciary will hear the disputes between the assessees and the department and give decisions on various issues. The Supreme Court is the Apex Court of the country and the law laid down by the Supreme Court is the law of the land. The decisions given by various High Courts will apply in the respective states in which such High Courts have jurisdiction.

An assesses may get income from different sources, eg:- salaries-house property income-profits and gains of business or profession - capital gains income from other sources like interest on securities , lottery winnings, races etc.

Income from each of these sources calculated first to find out the gross total income, and then permissible deduction allowed arriving in total income according to sec 80 c to 80 u. Every person whose taxable income in the previous

year exceeds the minimum taxable limit is liable to pay income tax during the current financial year at the rates applicable to the current financial year.

ASSESSMENT YEAR SEC 2(9)

Assessment year means the period of 12 months commencing on the first day of April every year and ending on 31st march of the next year.

PREVIOUS YEAR SEC 3

Previous year means the financial year immediately preceding the assessment year

PERSONS SEC 2(34)

1. Individual
2. Hindu undivided family
3. Company
4. Firm
5. Association of persons or body of individual
6. Local authority
7. Artificial juridical person

ASSESSEE SEC 2(7)

Assessee is a person, who has liability to pay tax or any other sum of money under Income Tax act of 1961, so the afore said persons include in the category of Assessee. Every Assessee whose taxable income in the previous year exceeds the minimum taxable limit is liable to pay income tax during the current financial year at the rates applicable to the current financial year.

EXCEPTIONS TO THE GENERAL RULE

Generally income earned in the previous year is taxed in the assessment year. But there are certain exceptions to the general rule. Ie the previous year and assignment year are same; the Assessee is liable to be assessed in the same year in which he earns the income in the following case,

1. Income from non-resident shipping company
2. Income of person leaving India
3. Income of person likely to transfer assets to avoid tax
4. Income from discontinued business.

GROSS TOTAL INCOME

It is the aggregate taxable income under the different heads of income such as income from salary, income from house property, income from profits or gains of business, capital gains and income from other sources. Ie total income computed in accordance with the provision of the act before making any deductions under Sec 80 C to 80 U

TOTAL INCOME SEC 2(45)

Total income is arrived after making various deductions from gross total income under section 80 C to 80 U. It is computed on the basis of residential status of an Assessee

RESIDENTIAL INCOME AND TAX INCIDENCE

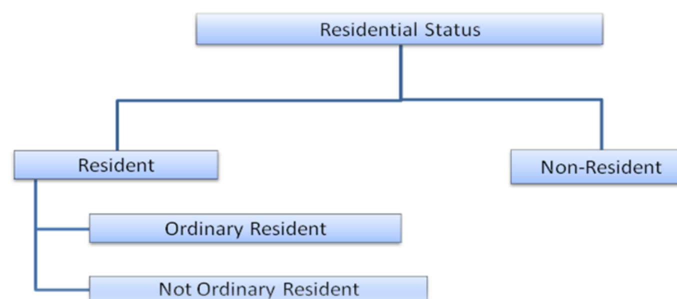
RESIDENTIAL STATUS

The residential status of a person is required to be determined for each assessment year in order to determine the scope of total income. The basis of determination of residential status in respect of each person is laid down under the provisions of section 6 which are analyzed hereinafter.

Residential status of an Individual under Income Tax Act, 1961

Residential status of an individual for income-tax purposes depends on the physical stay of the individual in India. Based on the period of stay in India in a given financial year, an individual may be classified as:

- Resident
- Not ordinarily resident (NOR)
- Non-resident (NR).



Tax incidence of an assessee depends upon his residential status rather than on his citizenship.

However, two types of categories of assessee (i.e., individual and HUF), if resident in India, will be either:

i. Resident and ordinarily resident in India; or
ii. Resident but not ordinarily resident in India.

The following points should be noted in this regard:

1. All taxable entities are divided in the following categories for the purpose of determining residential status:
   - An individual;
   - A Hindu undivided family;
   - A firm or an association of persons;
   - A joint stock company; and
   - Every other person.
2. Residential status of an assessee is to be determined in respect of each previous year as it may vary from previous year to previous year.
3. In view of section 6(5), if a person is resident in India for one of the sources of income, he will be deemed to be resident in India for all other sources of income in the same assessment year.

4. An assessee may enjoy different residential status for different assessment years.
5. It is not necessary that a person who is "resident" in India cannot become "resident" in any other country for the same assessment year. A person may be resident in two (or more) countries at the same time. It is, therefore, not necessary that a person who is resident in India will be non-resident in all other countries for the same assessment year.
6. Whether an assessee is a resident or a non-resident is a question of fact and it is the duty of the assessee to place all relevant facts before the income-tax authorities.

How to determine residential Status of an individual (Sec. 6):

An individual may be resident or non-resident. Further, if an individual is resident, he may be resident and ordinarily resident or resident but not ordinarily resident.

Following are the rules to determine the residential status of an individual:

a. Resident and ordinarily resident (ROR):
Must satisfy at least one of the basic conditions and both of the additional conditions

b. Resident but not ordinarily resident (RNOR):
Must satisfy at least one of the basic conditions and one or none of the additional conditions

c. Non-resident (NR):
Must not satisfy any of the basic conditions

Basic conditions [Sec. 6(1)]:

a. He is in India in the previous year for a period of 182 days or more; or

b. He is in India for a period of 60 days or more during the previous year and 365 days or more during 4 years immediately preceding the previous year.

<u>Exception:</u>

In the following two situations, basic condition (b) is not applicable:

1. An **Indian citizen** who **leaves** India during the previous year
- for the purpose of employment outside India or
- as a member of crew of an Indian ship.

2. An **Indian citizen or a person of Indian origin** who **comes** on a visit to India during the previous year.

Additional conditions [Sec. 6(6)]:

a. He has been **resident** in India in at least 2 out of 10 previous years immediately preceding the relevant previous year.

b. He has been in India for a period of 730 days or more during 7 years immediately preceding the relevant previous year.

Points to be noted:

- For the first point of exception, the requirement is not leaving India for taking employment outside India but leaving India for the purpose of employment (the employment may be in India or outside India).

- A person is deemed to be of **Indian origin** if he, or either of his parents or any of his grand-parents, was born in undivided India. It may be noted that grand-parents include both maternal and parental grand-parents.

- Where a person is in India only for a part of a day, the calculation of physical presence in India in respect of such broken period should be made on hourly basis. A total of 24 hours of stay spread over a number of days is to be counted as being equivalent to the stay of one day. If, However, data is not available to calculate the period of stay of an individual in India in terms of hours, then the day on which he enters India as well as the day on which he leaves India shall be taken into account as stay of the individual in India.

How to determine the residential status of a HUF [Sec. 6(2)]:

A Hindu undivided family (like an individual) is either resident in India or non-resident in India. A resident Hindu undivided family is either ordinarily resident or not ordinarily resident.

Following are the rules to determine the residential status of a Hindu undivided family:

a. A Hindu undivided family is said to be **resident** in India if control and management of its affairs are situated –
   - Wholly in India or
   - Partly in India and partly outside India

   A resident Hindu Undivided family is an **ordinarily resident** in India if **karta or manager** of the family (including successive kartas) satisfies the two additional conditions given above.

b. A Hindu undivided family is said to be **non-resident** in India if control and management of its affairs are situated wholly out of India.

Control and management for this purpose refers to the decisions taken regarding affairs of the HUF. The control and management is situated at a place where the head, the seat and the directing powers are situated.

How to determine the residential status of firm and association of persons [Sec. 6(2)]:

a. A partnership firm and an association of persons are said to be **resident** in India if control and management of their affairs, during the relevant previous year, are situated –
   - Wholly in India or

- Partly in India and partly outside India

b. A partnership firm and an association of persons are said to be **non-resident** in India if control and management of their affairs, during the relevant previous year, are situated wholly out of India.

Control and management for this purpose is usually situated at a place where the head, the seat and the directing powers are situated. While in the case of a firm, control and management is vested in partners, in the case of an association of persons it is vested in principal officer.

How to determine the residential status of a company [Sec. 6(3)]:

a. An **Indian company** is **always resident** in India.

b. A **foreign company** is **resident** in India only if, control and management of its affairs, during the relevant previous year, is situated **wholly** in India.

c. A foreign company is **non-resident** in India, if control and management of its affairs, during the relevant previous year, is situated –

- wholly out of India or
- partly in India or partly outside India.

Control and management for this purpose refers to "head and brain" which directs the affairs of policy, finance, disposal of profits and vital things concerning the management of a company. Usually control and management of a company's affairs is situated at a place where meeting of its board of directors are held. Therefore, in the case of a foreign company, if all the meetings of the Board of Directors are generally held in India and crucial decisions regarding the management of the company are taken in India, then the foreign company shall be a resident in India.

How to determine the residential status of every other person [Sec. 6(4)]:

a. Every other person is **resident** in India if control and management of its affairs, during the previous year, is situated –

- Wholly in India or
- Partly in India and partly outside India

b. Every other person is **non-resident** in India if control and management of its affairs, during the previous year, is situated wholly out of India.

Relationship between residential status and incidence of tax (Sec. 5):

Under the Act, incidence of tax on a taxpayer depends on his residential status and also on the place and time of accrual or receipt of income.

MEANING OF "INDIAN INCOME":

Any of the following three is an Indian income:

1. If income is received (or deemed to be received) in India during the previous year and at the same time it accrues or arises (or is deemed to accrue or arise) in India during the previous year.

2. If income is received (or deemed to be received) in India during the previous year but it accures or arises (or is deemed to accure or arise) outside India during the previous year.
3. If income is received outside India during the previous year but it accrues or arises (or is deemd to accrue or arise) in India during the previous year.

Meaning of "Foreign Income":

If the following two conditions are satisfied, then such income is "foreign income" –

1. Income is not received (or not deemed to be received) in India and
2. Income does not accrue or arise (or is deemed to accrue or arise) in India.

Conclusions regarding taxability:

1. **Indian Income:** Indian income is always taxable in India irrespective of the residential status of the taxpayer.
2. **Foreign Income:** Foreign income is taxable in the hands of resident (in case of a firm, an association of persons, a joint stock company and every other person) or resident and ordinarily resident (in case of an individual and a Hindu Undivided Family) in India. Foreign income is not taxable in the hands of non-resident in India.
   In the hands of resident but not ordinarily resident taxpayer, foreign income is taxable only in any of the following two situations –
   a. If it is **business income** and business is controlled wholly or partly from India, or
   b. If it is **professional income** and profession is set up in India.
   In any other case (like salary, rent, interest etc.), foreign income is not taxable in the hands of resident but not ordinarily resident taxpayers.

Points to be noted regarding the concept of "receipt of income":

Income received in India is taxable in all cases irrespective of residential status of an individual.

The following points should be noted in this regard:

1. The term "receipt" of income refers to the first occasion when the recipient gets the money under his control. Once an amount is received as income, any remittance or transmission of the amount to another place does not result in "receipt" at the other place. In other words, it can be said that an assessee after receiving an income outside India cannot be said to have received the same again when he brings or remits the same to India.
2. It is not necessary that income should be received in cash. Income may be received in cash or in kind.
3. Receipt is not the sole test of chargeability to tax. If an income is not taxable on receipt basis, it may be taxable on accrual basis.

4. It is not necessary that an income should be actually received in India in order to attract tax liability. An income deemed to be received in India in the previous year is also included in the taxable income of the assessee. The Act enumerates the following as income deemed to be received in India –
   a. Interest credited to recognized provident fund account of an employee in excess of 9.5%;
   b. Excess contribution of employer in the case of recognized provident fund (i.e., the amount contributed in excess of 12% of salary);
   c. Transfer balance from the unrecognized fund to a recognized provident fund;
   d. Contribution by the Central Government or any other employer to the account of an employee under a notified pension scheme referred to in section 80CCD;
   e. Tax deducted at source;
   f. Deemed profit under section 41 and 59.

Points to be noted regarding the concept of "accrual of income":

Income accrued in India is chargeable to tax in all cases irrespective of residential status of an assessee. Income is said to be received when it reaches the assessee; when the right to receive the income becomes vested in the assessee, it is said to accrue or arise.

Points to be noted regarding the concept of "income deemed to accrue or arise in India":

In some cases, income is deemed to accrue or arise in India under **section 9** even though it may actually accrue or arise outside India. Section 9 applies to all assessees irrespective of their residential status and place of business.

The categories of income which are deemed to accrue or arise in India are as under –

1. **Income from business connection in India:**

   If the following two conditions are satisfied, then the income which arises outside India because of "business connection" in India, is deemed to accrue or arise in India-
   a. The taxpayer has a "business connection" in India and
   b. By virtue of "business connection" in India, income actually arises outside India.

<u>Meaning of business connection</u>

It includes a person acting on behalf of a non-resident and who performs any one or more of the following –

- He exercises in India an authority to conclude contracts on behalf of the non-resident (it does not cover only purchase of goods or merchandise for the non-resident).

- He has no such authority but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident.
- He habitually secures order in India (mainly or wholly) for the non-resident or for non-residents under the same management.

2. Income through or from any property, asset or source of income in India

3. Income through the transfer of capital asset situated in India

4. Income under the head "Salaries":

Income of an individual which falls under the head "Salaries" is deemed to accrue or arise in India if service is rendered in India. Any salary payable for rest period or leave period which is both preceded and succeeded by service in India, will also be regarded as salary earned in India.

5. Salary payable abroad by the Government to a citizen of India

6. Dividend paid by an Indian company:

Any dividend paid by an Indian company outside India is deemed to accrue or arise in India. In case of a company, other than an Indian company, dividend shall be deemed to accrue or arise at a place where the register of members is kept.

7. Income by way of interest:

Interest income of the following types are deemed to accrue or arise in India –

a. Received from Government:

Interest received from the Central Government or any State Government is deemed to accrue/ arise in India in the hands of recipient.

b. Received from resident:

Income received from a resident shall be deemed to accrue/ arise in India in the hands of recipient in all cases**except** in the following:

- Interest received from a resident in respect of any debt incurred, or any money borrowed and used by the payer of the interest, for the purpose of a business or profession carried on by the payer outside India; and
- Interest received from a resident in respect of any debt incurred, or any money borrowed and used by the payer of interest for the purpose of making or earning any income from any source outside India.

c. Received from a non-resident:

Interest received from a non-resident shall be deemed to accrue/ arise in India in the hands of recipient if it is in respect of any debt incurred, or money borrowed and used, for the purpose of a business or profession carried on by the payer in India.

8. Income by way of royalty:

Royalty income in the following situations is deemed to accrue or arise in India in the hands of the recipient –

a. **Received from Government:**
Royalty received from the Central Government or any State Government is deemed to accrue/ arise in India in the hands of recipient.

b. **Received from resident:**
Royalty received from a resident (**except** where the payment is relatable to a business or profession carried on by the payer outside India or to any other source of his income outside India) shall be deemed to accrue/ arise in India in the hands of recipient.

c. **Received from a non-resident:**
Royalty received from a non-resident (if the payment is relatable to a business or profession carried on by the payer in India or any other source of his income in India) is deemed to accrue/ arise in India in the hands of recipient.

9. Income by way of fees for technical services:

Income by way of "fess for technical services" of the following types are deemed to accrue or arise in India in the hands of the recipient –

a. **Received from Government:**
Fees for technical services received from the Central Government or any State Government is deemed to accrue/ arise in India in the hands of recipient.

b. **Received from resident:**
Fees for technical services received from a resident (**except** where the payment is relatable to a business or profession carried on by the payer outside India or to any other source of his income outside India) is deemed to accrue/ arise in India in the hands of recipient.

c. **Received from a non-resident:**
Fees for technical services received from a non-resident (if the payment is relatable to a business or profession carried on by the payer in India or any other source of his income in India) is deemed to accrue/ arise in India in the hands of recipient.