



A STUDY OF MUTUAL FUND ACCOUNTING IN PERSPECTIVE OF BUILDING NATION

Prof. (Dr.) Badal Barai

Asst. Professor of Commerce, Acharya Girish Chandra Bose college, Kolkata

ABSTRACT

Mutual Fund is a fund establishment in the form of a trust to raise money through the sale of units to the public or a section of the public under one or more schemes for investing in securities, including money market instrument. The investors want to know about the present and past performance of the selected mutual funds. This information must be supported by certified documents. The system of accounting for Mutual Fund is different from conventional system of accounting which is followed in industrial sectors. Hence, only proper accounting for mutual funds can show the real picture of risk and return of a specific mutual fund. An investor may compare accounting information relating to a mutual fund with its benchmark return. He can do the comparison with confidence on the basis of audited report of a particular fund. Moreover proper system of mutual fund accounting leads the fund manager to minimize cost

KEYWORDS : Mutual Fund (MF), SEBI, Net Asset Value (NAV), Asset Management Company (AMC),

INTRODUCTION

Mutual Fund (MF) investments have become a very popular way of investment for the last few decades. Mutual Fund investment companies collect funds from investors and invest them into different types of securities and/or in other assets. Each investor is entitled to a share of the portfolio established by the investment company in proportion to the amount they invested. This can be beneficial for investors, as it gives them access to diversification. Moreover, as the funds are professionally managed, investors who do not have sufficient knowledge of the market may be benefited from the fund being run in a more profitable way than could be done by them.

The investors want to know about the present and past performance of the selected mutual funds. The information must be supported by certified documents. The system of accounting for Mutual Funds is different from conventional system of accounting which is followed in industrial sectors. SEBI has specified some guidelines regarding the disclosures of accounting information and accounting system to be followed for mutual fund.

Mutual funds are the common names for open-end managed investment companies, which are investment companies that allow investors to buy or sell back shares at any moment of time. Mutual funds can be classified into different types according to their investment policy. One such type is sector mutual funds, which can be defined as equity funds that seek capital appreciation by investing primarily in companies in related fields. Due to their narrow focus, sector funds have a higher volatility than other equity funds and therefore do not provide the same diversification benefits. However, investors can be benefited from sector funds in other ways. For example, the funds can be used to reduce the risk of an already diversified portfolio which is under represented in certain sectors. They can also help speculative investors in establishing an industry position which has some diversification within the industry.

Conceptual Idea and Legal Framework

SEBI has specified some guidelines regarding the disclosures of accounting information and accounting system to be followed for mutual fund. SEBI proposed that Mutual Funds, should prepare scheme wise Balance Sheets as per Annexure IA and IB of Eleventh Schedule of SEBI (Mutual Funds) Regulations 1996. As per regulation 54, every mutual fund or asset management company shall prepare an annual report and annual statement of accounts of the schemes and funds in respect of each financial year. As per Regulation (57), every mutual fund is responsible to forward a copy of annual report and other information containing details of investments and

deposits held by the fund so that the entire scheme wise portfolio of the fund is disclosed to SEBI within six months from the date of closure of the financial year. The reports required to be submitted to SEBI are as specified in Regulation (54) above.

Mutual Fund investors should go through the annual report, its contents and auditor's report carefully. They also keep a track of NAV and investment portfolio. Therefore the accounting information of mutual funds plays a role of key factor to make the investors confident about their investment. Investors take their investment decision on the basis of the information provided by the system of mutual fund accounting. Hence only a proper and appropriate system of accounting can provide the right information to them because any false information may lead them to take wrong decision and loose their money. As the total mutual fund investment in our country plays a vital role in capital formation, therefore the role of proper system of accounting for mutual fund has also an important role in infrastructural development of our country.

Measures and Performance Evaluation

Any meaningful evaluation of performance will necessarily have to measure total return per unit of risk or the ability to earn superior returns for a given risk class. There are various statistical techniques to measure this factor. One of the techniques estimates the realized portfolio returns in excess of the risk free return, as a multiple of the factor of the portfolio. The factor of portfolio, in return, measures the systematic or undiversifiable risk of the portfolio, the relation to the market index.

Mutual Funds sell their shares to public and redeem them to current net asset value (NAV) which is calculated as under-

$$\text{NAV of MF} = \frac{\text{Total market value of all MF holdings} - \text{All MF liabilities}}{\text{No. of MF units or shares}}$$

OR

$$\text{NAV of MF} = \frac{\text{Market value of Scheme's Investments} + \text{Receivables} + \text{Accrued Income} + \text{Other Assets} - \text{Accrued Expenses} - \text{Payables} - \text{Other Liabilities}}{\text{No. of Units outstanding under the Scheme}}$$

The Net Asset Value of a mutual fund scheme is basically the per unit market value of all the assets of the scheme. To illustrate this better, a simple example will help.

Scheme name	UTI Balanced Fund
-------------	-------------------

Scheme size	Rs. 20,00,00,000 (Rs. Twenty crores)
Face value of units	Rs10
No. Of Units (Scheme size)	2,00,00,000
Investments	In shares
Market value of shares	Rs. 50,00,00,000 (Rs Fifty crores)
NAV(Market value of	
	Rs. 50,00,00,000
Investments/No.of units) =-----	
	2,00,00,000
	= Rs.25

Thus, each unit of Rs. 10 is worth Rs. 25.

Simply stated, NAV is the value of the assets of each unit of the scheme, or even simpler value of one unit of the scheme. Thus, if the NAV is more than the face value (Rs. 10), it means the money has appreciated and vice versa.

NAV also includes dividends, interest accruals and reduction of liabilities and expenses, besides market value of investments.

Policies and Presentation of Accounts:

Accounting policies of Mutual Fund schemes are somewhat different from those of an industrial concern. Ninth schedule to SEBI (Mutual Fund) Regulations 1996 deals with accounting policies and standards to be adopted by a Mutual Fund.

The accounting policies generally cover the following areas

1. Basis of Accounting: The fund maintains its books of account on an accrual basis.

2. Portfolio Valuation: Investment is stated at market/fair value at the balance sheet date/date of determination in valuing the scheme's investments.

(i) Securities listed on a recognized stock exchange are valued at the last quoted price on the principal exchange on which the security is traded.

(ii) Money market instruments are valued at fair value as determined in good faith by Asset Management Company (AMC)

3. Securities Transactions: Investment in securities transactions are accounted for on a trade date basis. The scheme uses the average cost method for determining the realized gain or loss on sale of investments.

4. Investment Income: Dividend and interest income are recorded on an accrual basis.

5. Deferred Revenue Expenditure: Initial issue costs comprise those costs directly associated with the issue of units of the scheme and include brokerage/incentive fees on issue of units, advertising and marketing costs, registrar fees and expenses and printing and despatch cost, which are being amortized over a period of ten financial years.

6. Dividend Equalization Reserve: The net distributable income relating to units issued/repurchased is transferred from/to Dividend Equalization Reserve for Dividend Plan for determining the net surplus/deficit transferred to /from Unit Premium Reserve.

The Scheme does not intend to declare dividends or make any other distribution in respect of units held under the Growth Plan and accordingly has not accounted for Dividend Equalization in respect of this plan during the year.

7. Unit Premium Reserve: Depending upon issue and redemption of units, the net premium or discount to face value of units is adjusted against the Unit Premium Reserve of the

Scheme, after an appropriate portion of the issue proceeds and redemption payout is credited or debited respectively to the Dividend Equalization Reserve.

The Unit Premium Reserve is available for dividend distribution except to the extent it is presented by unrealized net appreciation in value of investments and deferred revenue expenditure.

8. Agent's Commission: Agents commission expenses are not considered as distribution charges.

Mutual Funds, should prepare scheme wise balance sheet as per Annexure IA and IB of Eleventh Schedule of SEBI (Mutual Funds) Regulations 1996. As per regulation 54, every mutual fund or asset management company shall prepare in respect of each financial year an annual report and annual statement of accounts of the schemes and funds.

The balance sheet shall give scheme wise particulars of its assets and liabilities and shall contain particulars as per Eleventh Schedule. It should also disclose accounting policies relating to valuation of investments and other important items. Under each type of investment, the aggregate carrying value and market value of non-performing investments shall be disclosed. It should also indicate the extent of provision made in revenue account for the depreciation /loss in the value of non-performing investments. It shall also disclose per unit Net Asset Value (NAV) as at the end of accounting year. Previous year figures should also be given against each item.

It should also indicate the appropriation of surplus by way of transfer to reserves and dividend distributed. It should also contain

- Provision for aggregate value of doubtful deposits, debts and outstanding and accrued income.
- Profit or loss in sale and redemption of investment may be shown on a net basis.
- Custodian and registrar fees.
- Total income and expenditure expressed as a percentage of average net assets, calculated on a weekly basis.

Scheme wise balance sheet normally contains the information under following groups -

Asset side- Investments, Deposits, Other Current Assets, Fixed Assets, Deferred revenue expenditure

Liability side- Unit capital, Reserves and surpluses, Loans, Current liabilities,

Annual Report:

According to Regulation 54 of SEBI regulation, every mutual fund of the asset management company shall prepare in respect of each financial year an annual report and annual statement of accounts for all schemes and fund as specified in Eleventh Schedule.

An Annual Report should contain the followings:

- report of the board of trustees on the operations
- balance sheet
- revenue account
- auditor's report
- brief statement of board of trustees on liabilities and responsibilities of the trustees, objective of investments, basis and policy of investments and comments of the trustees on performance of scheme
- a statement to the effect that "the price and redemption value of the units, and income from them, can go up as well as down with the fluctuation in the market value of its underlying investments."
- Statement giving relevant perspective historical per unit statistics

- Statement to the effect that "on written request, present and prospective unit holder/ investors can obtain copy of the trust deed, the annual report at a price and the text of relevant scheme."

As per Regulation (57), every mutual fund is responsible to forward a copy of annual report and other information containing details of investments and deposits held by the fund so that the entire scheme wise portfolio of the fund is disclosed to SEBI within six months from the date of closure of the financial year. The reports required to be submitted to SEBI are as specified in Regulation (54) above

Mutual Fund investors should go through the annual report, its contents and auditor's report carefully. They should also keep a track of NAV and investment portfolio.

Mutual Fund Accounting Role:

Mutual Funds play an important role in the development of the financial system. First, they pool the resources of small investors together, increasing their participation in financial markets, which helps both inclusion and the efficient functioning of markets. Hence only proper accounting for mutual funds can show the real picture of risk and return of a specific mutual fund. An investor may compare accounting information relating to a mutual fund with its benchmark return. He can do the comparison with confidence on the basis of audited report of a particular fund. Moreover proper system of mutual fund accounting leads the fund manager to minimize cost.

The economy like India will make its path for next few years very successfully. The fundamentals of the Indian economy are relatively strong. The purchasing power of consumer has also increased unbelievably. Mutual funds are going to be key of resource mobilization for Indian financial system over the next few years. The only thing is the India need just proper structure whether it may be the case of black money may be the case of financial reforms or strong regulatory frame work for the protection of small and retail investors. In short, Indian mutual fund industry is going to observe good growth rate in upcoming future. It will achieve the sustainable and profitable growth provided the said improvements measures are applied properly and it would play a key role in financial resource mobilization.

The backbone of any economy is its financial system. Stronger the financial system stronger the economy is. The financial system consists of financial markets, financial intermediaries, financial instruments etc. Mutual Fund is one of the emerging financial instruments that mobilize the savings of millions of small and retail investors by creating gigantic capital formation for the economy. Mutual fund is one of the convenient financial instruments for investment for small and retail investor and country like India small investment forms major part of capital, it would be beneficial for the country. The study will identify the relationship between proper mutual fund accounting with the growth and development of the country. It will explore the relationship between development of proper and user/investors oriented mutual fund accounting system and economy, hence new steps can be taken for development and growth of the mutual fund accounting system and thereby economy as whole.

Concluding Thoughts

The present endeavor focuses upon relevance of mutual fund accounting to partner the process of nation building. As discussed, capital formation is sine to perpetual economic growth. The intervention of mutual funds is being anticipated to play dominant role in this mechanism on the grounds of convenience, diversification of risks, expert management and economies of scale. Hence a stringent legal and regulatory framework is indispensable for boosting the confidence of

marginal investors to attract additional quantum of investments. The governance on accounting reporting system to ensure objectivity of statements can be largely effective as one of the considerable factors to facilitate the transfer process. Thus, the primitive objective of overall socio-economic development at large can be achieved.

REFERENCES

1. www.amfiindia.com (visited on 23.09.2015)
2. Chandra, Prasanna, " The investment Game". Tata Mc.Graw-hill publication, New Delhi
3. Dave, S.A., "Mutual fund growth and development" The journal of Indian institute of Bankers, Jan-march, 1992.
4. Delia-Elena DIACONAȘU (2011), "The Role of Mutual Fund in U.S. economy", Alexandru Ioan Cuza University Faculty of Economics and Business Administration Iași, Romania
5. Dr. Subir Gokarn (2011), "Mutual Fund and Market Development in India", CII 7th editions of Mutual Fund Summit 2011, Deputy Governor, RBI, Mumbai 22 June 2011
6. Guclery and Shaw, 'Financial aspects of Development', - IC Renew, v0145, 1955, pp 515-539.
7. Gupta Shasi k. and Sharma R.K., Financial Management, Kalyani Publishers,
8. Hsieh, C. and P.Klenow, 2007, " Misallocation and Manufacturing TFT in China and India", NBER Working Paper No. 13290 (Cambridge, Massachusetts: National Bureau of Economic research)
9. IMF, working paper Asia and Pacific Department, "Financial Development and Growth in India: A Growing Tiger in cage" by Hiroko Oura, March 2008
10. Misra and Puri (2008) " Economic Environment " Himalaya Publication, New Delhi
11. Misra and Puri (2010) " Indian Economy " Himalaya Publication, New Delhi.
12. Oura, H., 2007, " Wild or Tamed? India's Potential growth," IMF working Paper 07/224 (Washington: IMF)
13. Phanumantha Rao, Vidhyasagar university journal of commerce, volume 12th march 2007
14. Rohit Shukla 2006, "36th Conference of Gujarat Economic Association 28-29th January 2006 Abhinav International Monthly Refereed Journal of Research In Management & Technology 91 ISSN – 2320-0073 Volume II, December'13
14. www.abhinavjournal.com
15. Shukla, Sharad, " Mutual Funds: past performance is no indicator of the future" Economic times, June 6, 1992
16. The Indian mutual fund industry – the future in dynamic environment outlook for 2015, June 2009 by KPMG and CII
17. The Kanfman Fund Inc. "No Load Small Company Growth Fund" Annual Report, 1986.
18. The Reserve Bank of India – 2011 reports www.rbi.org.
19. Van Horne, J C (1995), Financial Management & policy, prentice hall International.
20. World Bank, 2006, Developing Indian Corporate Bond Market, (Washington).
21. Yasaswy, N.j. "personal investment and Tax planning year book" Vision Books, New Delhi.
22. www.moneycontrol.com (visited on 30.08.2015)
23. www.mutualfundindia.com (visited on 3.09.2015)
24. www.sebi.gov.in (visited on 13.09.2015)