

NISM Series V-A Study Material

Module 4: Valuation, Accounting & Taxation

1. NAV Calculation & Total Expense Ratio (TER)

Net Asset Value (NAV)

NAV represents the true market value of a single unit of a mutual fund. It is calculated at the end of every trading day.

$$\text{NAV} = (\text{Total Assets} - \text{Total Liabilities}) / \text{Total Number of Outstanding Units}$$

- **Mark-to-Market:** The process of valuing the portfolio's securities based on their closing market prices every day. This ensures the NAV accurately reflects real-world value.
- **Total Expense Ratio (TER):** This is the percentage of the fund's total assets that the AMC charges annually to cover management, administration, and distribution costs.

Exam Rule: SEBI mandates that as the AUM (size) of a fund increases, the TER percentage must decrease. Equity funds generally have higher TER limits than debt funds.

2. Taxation Rules & Capital Gains

Mutual Fund taxation depends heavily on two factors: the asset class (Equity vs. Non-Equity) and the Holding Period.

Fund Category	Criteria	Short-Term Holding	Long-Term Holding
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Equity-Oriented	Invests > 65% in domestic equities	Less than 1 Year (STCG)	More than 1 Year (LTCG)
Non-Equity (Debt)	Invests < 65% in equities	Less than 36 Months (3 Years)	More than 36 Months (3 Years)

What is Indexation?

Indexation is a tax benefit applied to Long Term Capital Gains (historically for Debt funds/Real Estate). It allows the investor to adjust the purchase price of the asset upwards to account for inflation, using the Cost Inflation Index (CII) provided by the government.

Result: Higher Purchase Price → Lower Capital Gain → Less Tax Paid.

TDS (Tax Deducted at Source) Rules

- **Capital Gains:** For Resident Indians, mutual funds do NOT deduct TDS on capital gains upon redemption. The investor must pay the tax while filing their ITR.
- **Dividends (IDCW):** If the dividend paid to a resident investor exceeds Rs. 5,000 in a financial year, the AMC will deduct a 10% TDS.
- **NRIs:** TDS is strictly deducted on both capital gains and dividends for Non-Resident Indians.

3. Measuring Scheme Performance

Using the correct formula to measure returns is crucial for both the exam and real-world advisory.

- **CAGR (Compound Annual Growth Rate):** Used to calculate the average annual growth rate for a *Lump Sum* investment held for more than 1 year (point-to-point measurement).
- **XIRR (Extended Internal Rate of Return):** The mathematically correct metric to evaluate a *Systematic Investment Plan (SIP)*. It accounts for multiple cash flows occurring on different dates.

- **Rolling Returns:** Evaluates point-to-point returns on a daily/monthly basis over a specified period. It is the best metric to measure a fund manager's *consistency* and removes the bias of a specific start or end date.