Test Series: September, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

*Question No. **1** is compulsory.*

*Answer any **five** questions from the remaining **six** questions.*

Wherever necessary suitable assumptions may be made and disclosed by way of a note.

Working Notes should form part of the answer.

(Time allowed: three hours) **(Maximum Marks: 100)**

1. (a) A Company is in the process of setting up a production line for manufacturing a new product. Based on trial runs conducted by the company, it was noticed that the production lines output was not of the desired quality. However, company has taken a decision to manufacture and sell the sub-standard product over the next one year due to the huge investment involved.

In the background of the relevant accounting standard, advise the company on the cut-off date for capitalization of the project cost.

(b) In 2011, Royal Ltd. issued 12% fully paid debentures of Rs. 100 each, interest being payable half yearly on 30th September and 31st March of every accounting year.

On 1st December, 2012, M/s. Kumar purchased 10,000 of these debentures at Rs. 101 cum-interest price, also paying brokerage @ 1% of cum-interest amount of the purchase. On 1st March, 2013 the firm sold all of these debentures at Rs. 106 cum-interest price, again paying brokerage @ 1 % of cum-interest amount. Prepare Investment Account in the books of M/s. Kumar for the period 1st December, 2012 to 1st March, 2013.

(c) An item of machinery was purchased on 1-4-2011 for Rs. 2,00,000. The WDV depreciation rate applicable to the machinery was 15%. The written down value of the machinery as on 31-3-2013 was Rs. 1,44,500. On 1-4-2013, the enterprise decided to change the method from written down value (WDV) to straight line method (SLM). The enterprise decided to write off the book value of Rs. 1,44,500, over the remaining useful life of machinery i.e. 5 years. Out of the total useful life of 7 years, 2 years have already elapsed.

Comment, whether the accounting treatment is correct. If not, give the correct accounting treatment with reasons.

(d) On 1st April, 2012, Libra Motors Co. sells a truck on hire purchase basis to Hari Transport Co. for a total hire purchase price of Rs. 9,00,000 payable as to Rs. 2,40,000 as down payment and the balance in three equal annual instalments of

Rs. 2,20,000 each payable on 31st March 2013, 2014 and 2015. The hire vendor charges interest @ 10% per annum.

You are required to ascertain the cash price of the truck for Hari Transport Co. Calculations may be made to the nearest rupee. *(4 x 5 = 20 Marks)*

2. K Ltd.and L Ltd.were amalgamated on and from 1st April, 2012. A new company C Ltd. was formed to take over the business of the existing companies. The summarized Balance Sheets of K Ltd.and L Ltd.as on 31st March, 2012 are given below:

	(Rs. in lakhs)			*(Rs. in lakhs)*	
Liabilities	*K Ltd.*	*L Ltd.*	*Assets*	*K Ltd.*	*L Ltd.*
Share Capital			*Fixed Assets*		
Equity Shares of Rs. 100 each	800	750	Land and Building	550	400
12% Preference shares of Rs. 100 each	300	200	Plant and Machinery	350	250
Reserves and Surplus			*Investments*	150	50
Revaluation Reserve	150	100	*Current Assets, Loans and Advances*		
General Reserve	170	150			
Investment Allowance Reserve	50	50	Inventory	350	250
Profit and Loss Account	50	30	Trade Receivable	300	350
Secured Loans			Cash and Bank	300	200
10% Debentures (Rs. 100 each)	60	30			
Current Liabilities and Provisions					
Trade payables	420	190			
	2,000	1,500		2,000	1,500

Details of Trade payables and Trade receivables are as under:

	(Rs. in lakhs) *K Ltd.*	*(Rs. in lakhs)* *L Ltd.*
Trade payables		
Sundry Creditors	270	120
Bills Payable	150	70
	420	190
Trade receivables		
Sundry Debtors	250	300
Bills Receivable	50	50
	300	350

Additional Information:

(1) 10% Debentureholders of K Ltd. and L Ltd. are discharged by C Ltd. issuing such number of its 15% Debentures of Rs. 100 each so as to maintain the same amount of interest.

(2) Preference shareholders of the two companies are issued equivalent number of 15% preference shares of C Ltd. at a price of Rs. 150 per share (face value of Rs. 100).

(3) C Ltd. will issue 5 equity shares for each equity share of K Ltd. and 4 equity shares for each equity share of L Ltd. The shares are to be issued @ Rs. 30 each, having a face value of Rs. 10 per share.

(4) Investment allowance reserve is to be maintained for 4 more years.

Prepare the Balance Sheet of C Ltd. as on 1st April, 2012 after the amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

(16 Marks)

3. ABC Ltd. took over a running business with effect from 1st April, 2013. The company was incorporated on 1st August, 2013. The following summarized Profit and Loss Account has been prepared for the year ended 31.3.2014:

		Rs.		Rs.
To	Salaries	48,000	By Gross profit	3,20,000
To	Stationery	4,800		
To	Travelling expenses	16,800		
To	Advertisement	16,000		
To	Miscellaneous trade expenses	37,800		
To	Rent (office buildings)	26,400		
To	Electricity charges	4,200		
To	Director's fee	11,200		
To	Bad debts	3,200		
To	Commission to selling agents	16,000		
To	Tax Audit fee	6,000		
To	Debenture interest	3,000		
To	Interest paid to vendor	4,200		
To	Selling expenses	25,200		
To	Depreciation on fixed assets	9,600		

To Net profit	87,600		
	3,20,000		3,20,000

Additional information:

(a) Total sales for the year, which amounted to ₹ 19,20,000 arose evenly upto the date of 30.9.2013. Thereafter they spurted to record an increase of two-third during the rest of the year.

(b) Rent of office building was paid @ ₹ 2,000 per month upto September, 2013 and thereafter it was increased by ₹ 400 per month.

(c) Travelling expenses include ₹ 4,800 towards sales promotion.

(d) Depreciation include ₹ 600 for assets acquired in the post incorporation period.

(e) Purchase consideration was discharged by the company on 30th September, 2013 by issuing equity shares of ₹ 10 each.

Prepare Statement showing calculation of profits and allocation of expenses between pre and post incorporation periods. *(16 Marks)*

4. On 31st December 2013, the Balance Sheet of A, B, and C who were sharing profits and losses in proportion to their capital stood as follows:

Liabilities	Rs.	Assets	Rs.	Rs.
Creditors	20,000	Cash at bank		16,000
Employees' provident fund	1,600	Debtors	20,000	
A's capital A/c	72,000	*Less* : Provision	400	19,600
B's capital A/c	48,000	Inventory		18,000
C's capital A/c	24,000	Machinery		48,000
Contingency reserve	30,000	Land & building		1,00,000
Workmen compensation reserve	6,000			
	2,01,600			2,01,600

B retires and the following adjustments of the assets and liabilities have been agreed upon before the ascertainment of the amount payable to B:

(a) Out of the amount of insurance which was debited entirely to Profit and Loss Account, Rs. 2,000 to be carried forward as an unexpired insurance.

(b) Land and building to be appreciated by 10%.

(c) Provision for doubtful debts to be brought up to 5% on debtors.

(d) Machinery to be depreciated by 5%.

(e) Provision of Rs. 3,000 to be made in respect of an outstanding bill of repairs.

(f) Goodwill of the entire firm be fixed at Rs. 36,000 and B's share of the same be adjusted into the accounts of A and C who are going to share future profits in the proportion of 3/4 and 1/4 respectively. (No Goodwill account being raised).

(g) The entire capital of the firm as newly constituted be fixed at Rs. 1,20,000 between A and C in the proportion of 3/4 and 1/4 after passing entries in their accounts for adjustments i.e. actual cash to be paid off or to be brought in by the continuing partners as the case may be.

(h) B to be paid Rs. 6,000 in cash and the balance to be transferred to his loan account.

Prepare Revaluation Account, Capital Accounts of the partners and the Balance Sheet of the firm of A and C after retirement. *(16 Marks)*

5. Perfect Society (not registered under the Companies Act) showed the following position on 31st March, 2012:

Balance Sheet as on 31st March, 2012

Liabilities	Rs.	Assets	Rs.
Capital fund	7,93,000	Electrical fittings	1,50,000
Expenses payable	7,000	Furniture	50,000
		Books	4,00,000
		Investment in securities	1,50,000
		Cash at bank	25,000
		Cash in hand	25,000
	8,00,000		8,00,000

The receipts and payment account for the year ended on 31st March, 2013 is given below:

		Rs.		Rs.
To Balance b/d			By Electric charges	7,200
Cash at bank	25,000		By Postage and stationary	5,000
Cash in hand	25,000	50,000	By Telephone charges	5,000
To Entrance fee		30,000	By Books purchased	60,000
To Membership subscription		2,00,000	By Outstanding expenses paid	7,000
To Sale proceeds of old papers		1,500	By Rent	88,000
To Hire of lecture hall		20,000	By Investment in securities	40,000
To Interest on securities.		8,000	By Salaries	66,000
			By Balance c/d	
			Cash at bank	20,000
			Cash in hand	11,300
		3,09,500		3,09,500

You are required to prepare income and expenditure account for the year ended 31st March, 2013 and a balance sheet as at 31st, March, 2013 after making the following adjustments:

Membership subscription included Rs. 10,000 received in advance.

Provide for outstanding rent Rs. 4,000 and salaries Rs. 3,000.

Books to be depreciated @ 10% including additions. Electrical fittings and furniture are also to be depreciated at the same rate.

75% of the entrance fees is to be capitalized.

Interest on securities is to be calculated @ 5% p.a. including purchases made on 1.10.2012 for Rs. 40,000. *(16 Marks)*

6. (a) Prepare the General Ledger Adjustment Account as will appear in the Debtors' Ledger from the information given below:

	Dr.	Cr.
	Rs.	Rs.
Debtors' Ledger Balance on 1.4.2012	94,400	480
Transactions for the year ended 31.3.2013:		
Total sales	2,40,000	
Cash sales	16,000	
Received from debtors (in full settlement of Rs. 1,18,000)	1,16,400	
Returns from debtors	5,200	
Bills accepted by customers	40,200	
Bills receivables dishonoured	3,000	
Bills receivable discounted	10,000	
Bills receivable endorsed to creditors	8,000	
Endorsed bills dishonoured	2,000	
Bad debts written off (after deducting bad debts recovered Rs. 600)	4,400	
Provision for doubtful debts	1100	
Transfer from debtors' ledger to creditors' ledger	2,200	
Transfer from creditors' ledger to debtors' ledger	3,800	
Balance on 31.3.2013		
Debtors' ledger	760	

(b) On 29th August, 2012, the godown of a trader caught fire and a large part of the stock of goods was destroyed. However, goods costing Rs. 1,08,000 could be salvaged incurring fire fighting expenses amounting to Rs. 4,700.

The trader provides you the following additional information:

	Rs.
Cost of stock on 1st April, 2011	7,10,500
Cost of stock on 31st March, 2012	7,90,100
Purchases during the year ended 31st March, 2012	56,79,600
Purchases from 1st April, 2012 to the date of fire	33,10,700
Cost of goods distributed as samples for advertising from 1st April, 2012 to the date of fire	41,000
Cost of goods withdrawn by trader for personal use from 1st April, 2012 to the date of fire	2,000
Sales for the year ended 31st March, 2012	80,00,000
Sales from 1st April, 2012 to the date of fire	45,36,000

The insurance company also admitted firefighting expenses. The trader had taken the fire insurance policy for Rs. 9,00,000 with an average clause.

Calculate the amount of the claim that will be admitted by the insurance company.

(8 + 8 =16 Marks)

7. Answer any **four** of the following:

(a) M accepted the following bills drawn by S:

On 8th March, 2013, Rs. 4,000 for 4 months.

On 16th March, 2013, Rs. 5,000 for 3 months.

On 7th April, 2013, Rs. 6,000 for 5 months.

On 17th May, 2013, Rs. 5,000 for 3 months.

He wants to pay all the bills on a single day. Find out this date.

(b) What are the advantages of outsourcing the accounting functions?

(c) Try Ltd. sold its building to Apex Ltd. for Rs. 60 lakhs on 30.09.2012 and gave possession of the property to Apex Ltd. However, documentation and legal formalities are pending. Due to this, the company has not recorded the sale and has shown the amount received as an advance. The book value of the building is Rs. 25 lakhs as on 31st March, 2013. Do you agree with this treatment? If you do not agree, explain the reasons with reference to the accounting standard.

(d) Sure Ltd. undertook a construction contract for Rs. 50 crores in April, 2012. The cost of construction was initially estimated at Rs. 35 crores. The contract is to be completed in 3 years. While executing the contract, the company estimated the cost of completion of the contract at Rs. 53 crores.

Can the company provide for the expected loss in the book of account for the year ended 31st March, 2013?

(e) What are the issues, with which Accounting Standards deal? *(4 x 4 =16 Marks)*

MOCK TEST PAPER - 1

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

SUGGESTED ANSWERS/HINTS

1. (a) As per para 9.3 of AS 10 'Accounting for Fixed Assets', expenditure incurred on start-up and commissioning of the project, including the expenditure incurred on test runs and experimental production, is usually capitalized as an indirect element of the construction cost. However, the expenditure incurred after the plant has begun commercial production *i.e.,* production intended for sale or captive consumption, is not capitalized and is treated as revenue expenditure even though the contract may stipulate that the plant will not be finally taken over until after the satisfactory completion of the guarantee period. In the present case, the company did not stop production even if the output was not of the desired quality, and continued the sub-standard production due to huge investment involved in the project. Capitalization should cease at the end of the trial run, since the cut-off date would be the date when the trial run was completed.

(b) **In the books of M/s Kumar**

Investment Account

for the period from 1st December 2012 to 1st March, 2013

(Scrip: 12% Debentures of Royal Ltd.)

Date	*Particulars*	*Nominal Value (Rs.)*	*Interest*	*Cost (Rs.)*	*Date*	*Particulars*	*Nominal Value (Rs.)*	*Interest*	*Cost (Rs.)*
1.12.2012	To Bank A/c (W.N.1)	10,00,000	20,000	10,00,100	1.03.2013	By Bank A/c (W.N.2)	10,00,000	50,000	9,99,400
1.3.2013	To Profit & loss A/c	-	30,000		1.3.2013	By Profit & loss A/c			700
		10,00,000	50,000	10,00,100			10,00,000	50,000	10,00,100

Working Notes:

(i) Cost of 12% debentures purchased on 1.12.2012 Rs.

Cost Value (10,000 × Rs. 101)	=	10,10,000
Add: Brokerage (1% of Rs. 10,10,000)	=	10,100
Less: Cum Interest (10,000 x 100 x12% x 2/12)	=	(20,000)
Total	=	10,00,100

(ii) Sale proceeds of 12% debentures sold on 1st March, 2013

		Rs.
Sales Price (10,000 $\times$ Rs. 106)	=	10,60,000
Less: Brokerage (1% of Rs. 10,60,000)	=	(10,600)
Less: Cum Interest (10,000 x 100 x12% x 5/12)	=	(50,000)
Total	=	9,99,400

(c) As per para 15 of AS 6, 'Depreciation Accounting', when the method of depreciation is changed, depreciation is recalculated in accordance with the new method from the date of the assets coming into use. The deficiency or surplus arising from retrospective re-computation of depreciation in accordance with the new method is adjusted in the statement of profit & loss in the year in which the method of depreciation is changed.

Calculation of Surplus/Deficiency due to change in method of depreciation

	Rs.
Purchase price of plant as on 01-04-2011	2,00,000
Less: Depreciation as per SLM, for the year 2011-12 (Rs. 2,00,000 $\div$ 7 years)	(28,571)
Balance as on 31-3-12	1,71,429
Less: Depreciation for the year 2012-13 (Rs. 2,00,000 $\div$ 7 years)	(28,571)
Balance as on 31-3-2013	1,42,858
Book value as per WDV method	1,44,500
Book value as per SLM	1,42,858
Deficiency	1,642

Deficiency of Rs. 1,642 should be charged to Profit & Loss account.

Therefore, the accounting treatment done by the enterprises is wrong i.e. book value of Rs. 1,44,500 will not be written off over the remaining useful life of machinery i.e. 5 years.

Note: It is assumed that when the company changed the method of depreciation from WDV to SLM, it re-calculated the depreciation amount on the basis of useful life and has not continued with WDV rate of depreciation.

(d) **Ratio of interest and amount due** = $\frac{\text{Rate of interest}}{100+\text{Rate of interest}} = \frac{10}{110} = \frac{1}{11}$

There is no interest element in the down payment as it is paid on the date of the transaction. Instalments paid after certain period includes interest portion also.

Therefore, to ascertain cash price, interest will be calculated from last instalment to first instalment as follows:

Calculation of Interest and Cash Price

No. of instalments	*Amount due at the time of instalment*	*Interest*	*Cumulative Cash price*
[1]	*[2]*	*[3]*	*(2-3) = [4]*
3rd	2,20,000	1/11 of Rs. 2,20,000 = Rs. 20,000	2,00,000
2nd	4,20,000 [W.N.1]	1/11 of Rs. 4,20,000 = Rs. 38,182	3,81,818
1st	6,01,818 [W.N.2]	1/11of Rs. 6,01,818 = Rs. 54,711	5,47,107

Total cash price = Rs. 5,47,107+ 2,40,000 (down payment) =Rs. 7,87,107.

Working Notes:

1. Rs. 2,00,000+ 2nd instalment of Rs. 2,20,000= Rs. 4,20,000.
2. Rs. 3,81,818+ 1st instalment of Rs. 2,20,000= Rs. 6,01,818.

2. **Balance Sheet of C Ltd.**

as at 1st April, 2012

Particulars	*Note No.*	*(Rs. in lakhs)*
I. **Equity and Liabilities**		
(1) **Shareholder's Funds**		
(a) Share Capital	1	1,200
(b) Reserves and Surplus	2	1,750
(2) **Non-Current Liabilities**		
Long-term borrowings	3	60
(3) **Current Liabilities**		
Trade payables	4	610
Total		3,620
II. **Assets**		
(1) **Non-current assets**		
(a) Fixed assets		
i. Tangible assets	5	1,550

ii. Intangible assets	6	20
(b) Non-current investments	7	200
(c) Other non-current assets	8	100
(2) **Current assets**		
(a) Inventories		600
(b) Trade receivables	9	650
(c) Cash and cash equivalents		500
Total		3,620

Notes to Accounts

		(Rs. in lakhs)	(Rs. in lakhs)
1.	Share Capital		
	Equity share capital		
	70 Lakhs Equity shares of Rs. 10 each	700	
	5 Lakhs Preference shares of Rs. 100 each	500	
	(all the above shares are allotted as fully paid-up pursuant to contracts without payment being received in cash)		1,200
2.	Reserves and surplus		
	Securities Premium Account		
	On equity shares - 70 lakh shares x Rs. 20 = 1,400		
	On preference shares - 5 lakh shares x Rs. 50 = 250	1,650	
	Investment Allowance Reserve	100	1,750
3.	Long-term borrowings		
	15% Debentures		60
4.	Trade payables		
	Sundry creditors	390	
	Bills Payables	220	610
5.	Tangible assets		
	Land and Building	950	
	Plant and Machinery	600	1,550
6.	Intangible assets		
	Goodwill [W.N. 2] (110-90)		20

7.	Non-current Investments		
	Investments		200
8.	Other non-current assets		
	Amalgamation Adjustment Account		100
9.	Trade receivables		
	Sundry Debtors	550	
	Bills receivable	100	650

Working Notes:

		(Rs. in lakhs)	
		K Ltd.	*L Ltd.*
(1)	Computation of Purchase consideration		
	(a) Preference shareholders:		
	$\left(\frac{3,00,00,000}{100}\right)$ i.e. 3,00,000 shares $\times$ Rs. 150 each	450	
	$\left(\frac{2,00,00,000}{100}\right)$ i.e. 2,00,000 shares $\times$ Rs. 150 each		300
	(b) Equity shareholders:		
	$\left(\frac{8,00,00,000 \times 5}{100}\right)$ i.e. 40,00,000 shares $\times$ Rs. 30 each	1,200	
	$\left(\frac{7,50,00,000 \times 4}{100}\right)$ i.e. 30,00,000 shares $\times$ Rs. 30 each		900
	Amount of Purchase Consideration	1,650	1,200
(2)	Net Assets Taken Over		
	Assets taken over:		
	Land and Building	550	400
	Plant and Machinery	350	250
	Investments	150	50
	Inventories	350	250
	Sundry Debtors	250	300
	Bills receivable	50	50

	Cash and bank		300		200
			2,000		1,500
	Less: Liabilities taken over:				
	Debentures	40		20	
	Sundry Creditors	270		120	
	Bills payable	150		70	
			(460)		(210)
	Net assets taken over		1,540		1,290
	Purchase consideration		1,650		1,200
	Goodwill		110		-
	Capital reserve				90

3. **Statement showing calculation of profits for pre and post incorporation periods for the year ended 31.3.2014**

Particulars	*Pre-incorporation period Rs.*	*Post- incorporation period Rs.*
Gross profit (1:3)	80,000	2,40,000
Less: Salaries (1:2)	16,000	32,000
Stationery (1:2)	1,600	3,200
Advertisement (1:3)	4,000	12,000
Travelling expenses (W.N.3)	4,000	8,000
Sales promotion expenses (W.N.3)	1,200	3,600
Misc. trade expenses (1:2)	12,600	25,200
Rent (office building) (W.N.2)	8,000	18,400
Electricity charges (1:2)	1,400	2,800
Director's fee	-	11,200
Bad debts (1:3)	800	2,400
Selling agents commission (1:3)	4,000	12,000
Audit fee (1:3)	1,500	4,500
Debenture interest	-	3,000
Interest paid to vendor (2:1) (W.N.4)	2,800	1,400
Selling expenses (1:3)	6,300	18,900
Depreciation on fixed assets (W.N.5)	3,000	6,600
Capital reserve (Bal.Fig.)	12,800	-
Net profit (Bal.Fig.)	-	74,800

Working Notes:

1. Time Ratio

Pre incorporation period = 1st April, 2013 to 31st July, 2013

i.e. 4 months

Post incorporation period is 8 months

Time ratio is 1: 2.

2. Sales ratio

Let the monthly sales for first 6 months (i.e. from 1.4.2013 to 30.09.13) be = x

Then, sales for 6 months = 6x

Monthly sales for next 6 months (i.e. from 1.10.13 to 31.3.2014) = $x + \frac{2}{3}x = \frac{5}{3}x$

Then, sales for next 6 months = $\frac{5}{3}x \times 6 = 10x$

Total sales for the year = 6x + 10x = 16x

Monthly sales in the pre incorporation period = Rs. 19,20,000/16 = Rs. 1,20,000

Total sales for pre-incorporation period = Rs. 1,20,000 x 4 = Rs. 4,80,000

Total sales for post incorporation period = Rs. 19,20,000 – Rs. 4,80,000 = Rs. 14,40,000

Sales Ratio = 4,80,000 : 14,40,000 = 1 : 3

3. Rent

		Rs.
Rent for pre-incorporation period (Rs. 2,000 x 4)		8,000 (pre)
Rent for post incorporation period		
August,2013 & September, 2013 (Rs. 2,000 x 2)	4,000	
October,2013 to March,2014 (Rs. 2,400 x 6)	14,400	18,400 (post)

4. Travelling expenses and sales promotion expenses

	Pre *Rs.*	*Post* *Rs.*
Traveling expenses Rs. 12,000 (i.e. Rs. 16,800- Rs. 4,800) distributed in 1:2 ratio	4,000	8,000
Sales promotion expenses Rs. 4,800 distributed in 1:3 ratio	1,200	3,600

5. **Interest paid to vendor till 30th September, 2013**

	Pre *Rs.*	*Post* *Rs.*
Interest for pre-incorporation period $\left(\frac{₹\ 4,200}{6} \times 4\right)$	2,800	
Interest for post incorporation period i.e. for August, 2013 & September, 2013 = $\left(\frac{₹\ 4,200}{6} \times 2\right)$		1,400

6. **Depreciation**

		Pre *Rs.*	*Post* *Rs.*
Total depreciation	9,600		
Less: Depreciation exclusively for post incorporation period	600		600
	9,000		
Depreciation for pre-incorporation period $\left[9,000 \times \frac{4}{12}\right]$		3,000	
Depreciation for post incorporation period $\left[9,000 \times \frac{8}{12}\right]$		–	6,000
		3,000	6,600

4. **Revaluation Account**

Particulars	Rs.	Particulars	Rs.
To Provision for doubtful debts	600	By Unexpired insurance	2,000
To Machinery	2,400	By Land and building	10,000
To Outstanding repairs	3,000		
To Profit t/f to:			
A's capital A/c	3,000		
B's capital A/c	2,000		
C's capital A/c	1,000		
	12,000		12,000

Capital Accounts of Partners

Particulars	A	B	C	Particulars	A	B	C

	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
To B's capital A/c (for goodwill) (W. N 2)	9,000	-	3,000	By Balance b/d	72,000	48,000	24,000
				By Revaluation A/c	3,000	2,000	1,000
To Bank A/c	-	6,000	-	By A's capital A/c (for goodwill) (W .N. 2)	-	9,000	-
To B's loan A/c	-	68,000	-	By C's capital A/c (for goodwill) (W .N 2)	-	3,000	-
To Balance c/d	90,000	-	30,000	By Contingency Reserve	15,000	10,000	5,000
				By Work Compensation Reserve	3,000	2,000	1,000
				By Bank A/c (Bal. fig)	6,000	-	2,000
	99,000	74,000	33,000		99,000	74,000	33,000

Balance Sheet of A and C at 31st December 2013

Liabilities	Rs.	Assets	Rs.	Rs.
Creditors	20,000	Cash at bank (W .N 1)		18,000
Employees' Provident Fund	1,600	Debtors	20,000	
Liability for repairs	3,000	*Less*: Provision	(1,000)	19,000
B's loan A/c	68,000	Stock		18,000
A's capital A/c	90,000	Machinery (48,000 - 2,400)		45,600
C's capital A/c	30,000	Land & building (1,00,000+10,000)		1,10,000
		Unexpired insurance		2,000
	2,12,600			2,12,600

Working Notes:

1. Bank Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	16,000	By B's capital A/c	6,000
To A's capital A/c	6,000	By Balance c/d	18,000
To C's capital A/c	2,000		
	24,000		24,000

2. Adjustment of goodwill

	New ratio	Old ratio	Gaining ratio
A	3/4	3/6	$\frac{18-12}{24}=\frac{6}{24}$
C	1/4	1/6	$\frac{6-4}{24}=\frac{2}{24}$

Therefore, gaining ratio of A & C = 3:1

B's share of goodwill of Rs. 12,000 will be shared by A & C in 3:1 = Rs.9,000: Rs. 3,000

5. Perfect Society

Income and Expenditure Account
for the year ended 31st March, 2013

Dr.					*Cr.*
Expenditure	*Rs.*	*Rs.*	*Income*		*Rs.*
To Electric charges		7,200	By Entrance fee (25% of Rs. 30,000)		7,500
To Postage and stationary		5,000			
To Telephone charges		5,000	By Membership subscription	2,00,000	
To Rent	88,000		*Less*: Received in advance	10,000	1,90,000
Add: Outstanding	4,000	92,000			
To Salaries	66,000		By Sale proceeds of old papers		1,500
Add: Outstanding	3,000	69,000			
To Depreciation (W.N.1)			By Hire of lecture hall		20,000
Electrical fittings	15,000		By Interest on securities (W.N.2)	8,000	
Furniture	5,000				
Books	46,000	66,000	*Add*: Receivable	500	8,500
			By Deficit- excess of expenditure over income		16,700
		2,44,200			2,44,200

Balance Sheet of Perfect Society
as on 31st March, 2013

Liabilities	*Rs.*	*Rs.*	*Asset*	*Rs.*	*Rs.*
Capital fund	7,93,000		Electrical fittings	1,50,000	
Add: Entrance fees	22,500		*Less*: Depreciation	(15,000)	1,35,000
	8,15,500		Furniture	50,000	
Less: Excess of expenditure over income	(16,700)	7,98,800	*Less*: Depreciation	(5,000)	45,000
			Books	4,60,000	
Outstanding expenses:			*Less* Depreciation	(46,000)	4,14,000
Rent	4,000		Investment:		
Salaries	3,000	7,000	Securities	1,90,000	
Membership subscription in advance		10,000	Accrued interest	500	1,90,500
			Cash at bank		20,000
			Cash in hand		11,300
		8,15,800			8,15,800

Working Notes:

1. Depreciation

	Rs.
Electrical fittings 10% of Rs. 1,50,000	15,000
Furniture 10% of Rs. 50,000	5,000
Books 10% of Rs. 4,60,000	46,000

2. Interest on Securities

Interest @ 5% p.a. on Rs. 1,50,000 for full year	7,500	
Interest @ 5% p.a. on Rs. 40,000 for half year	1,000	8,500
Less: Received		(8,000)
Receivable		500

6. (a) **General Ledger Adjustment Account in Debtors' Ledger**

			Rs.				Rs.
1.4.2012	To Balance b/d		480	1.4.2012	By Balance b/d		94,400
	To Debtor's ledger adjustment account:				By Debtors ledger adjustment account:		
	Bank	1,16,400			Sales (on credit)	2,24,000	
	Discount	1,600			Bills receivable dishonoured	3,000	
	Returns	5,200			Endorsed bills receivable dishonoured	2,000	2,29,000
	Bills receivable	40,200					
	Bad debts Written off (4,400 + 600)	5,000	1,68,400	31.3.2013	By Balance c/d		760
	To Debtors ledger adjustment account:						
	Transfer from debtors ledger to creditor's ledger	2,200					
	Transfer from creditor's ledger to debtor's ledger	3,800	6,000				
31.3.2013	To Balance c/d (balancing figure)		1,49,280				
			3,24,160				3,24,160

Notes: No entries will be made for the following transactions in respect to debtors as they do not affect general ledger adjustment accounts in Debtor's Ledger:

(i) Cash sales

(ii) Bills receivable discounted

(iii) Bad debts recovered and Provision for doubtful debts.

(b) Memorandum Trading Account for the period 1st April, 2012 to 29th August 2012

		Rs.		Rs.
To Opening Stock		7,90,100	By Sales	45,36,000
To Purchases	33,10,700		By Closing stock (Bal. fig.)	8,82,600
Less: Advertisement	(41,000)			
Drawings	(2,000)	32,67,700		
To Gross Profit [30% of Sales - Refer Working Note]		13,60,800		
		54,18,600		54,18,600

Statement of Insurance Claim

	Rs.
Value of stock destroyed by fire	8,82,600
Less: Salvaged Stock	(1,08,000)
Add: Fire Fighting Expenses	4,700
Insurance Claim	7,79,300

Note: Since policy amount is more than claim amount, average clause will not apply. Therefore, claim amount of Rs.7,79,300 will be admitted by the Insurance Company.

Working Note:

Trading Account for the year ended 31st March, 2012

	Rs.		Rs.
To Opening Stock	7,10,500	By Sales	80,00,000
To Purchases	56,79,600	By Closing stock	7,90,100
To Gross Profit	24,00,000		
	87,90,100		87,90,100

Rate of Gross Profit in 2011-12

$$\frac{\text{Gross Profit}}{\text{Sales}} \times 100 = \frac{24,00,000}{80,00,000} \times 100 = 30\%$$

7. (a) Calculation of number of days from base date

Transaction date	*Due date*	*Amount Rs.*	*No. of days from Base date (Base date 19.6.2013)*	*Product*
8.3.2013	11.7.2013	4,000	22	88,000
16.3.2013	19.6.2013	5,000	0	0

7.4.2013	10.9.2013	6,000	83	4,98,000
17.5.2013	20.8.2013	5,000	62	3,10,000
		20,000		8,96,000

Average due date $= \text{Base date} + \dfrac{\text{Total of Product}}{\text{Total of Amount}}$

= 19.6.2013 + Rs. 8,96,000 / Rs. 20,000

= 19.6.2013 + 45 days = 3.8.2013

(b) Following are the advantages of outsourcing the accounting functions:

(i) **Saving of Time:** The organisation that outsources its accounting function is able to save time to concentrate on the core area of business activity.

(ii) **Expertise of the third party**: The organisation is able to utilise the expertise of the third party in undertaking the accounting work.

(iii) **Maintenance of data:** Storage and maintenance of the data is in the hand of professional people.

(iv) **Economical:** The organisation is not bothered about people leaving the organisation in key accounting positions. The proposition often proves to be economically more sensible.

(c) As per para 16 & 17 of AS 1, "Disclosure of Accounting Policies", the main consideration in selection of accounting policy is the presentation of a true and fair picture of the state of affairs & performance of the enterprise. To ensure true and fair consideration, principles of prudence, substance over form and materiality should be looked into.

In this case, the economic reality and substance of the transaction is that the rights and beneficial interest in the property has been transferred although legal title has not been transferred. Hence, Try Ltd. in its financial statements for the year ended 31.3.2013, should record the sale and recognize the profit of Rs. 35 lakhs in its Profit & Loss Account and building should be removed from the balance sheet of Try Ltd. Therefore, the treatment given by the company is not correct.

(d) As per para 35 of AS 7 "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as an expense immediately. Therefore, The foreseeable loss of Rs. 3 crores (Rs. 53 crores less Rs. 50 crores) should be recognised as an expense immediately in the year ended 31st March, 2013. The amount of loss is determined irrespective of

(i) Whether or not work has commenced on the contract;

(ii) Stage of completion of contract activity; or

(iii) The amount of profits expected to arise on other contracts which are not treated as a single construction contract in accordance with para 8 of AS 7.

(e) Accounting Standards deal with the issues of

(i) Recognition of events and transactions in the financial statements,

(ii) Measurement of these transactions and events,

(iii) Presentation of these transactions and events in the financial statements in a manner that is meaningful and understandable to the reader, and

(iv) Disclosure requirements which should be there to enable the public at large and the stakeholders and the potential investors in particular, to get an insight into what these financial statements are trying to reflect and thereby facilitating them to take prudent and informed business decisions.

Test Series: September, 2014

Mock Test Paper – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 2: BUSINESS LAWS, ETHICS AND COMMUNICATION

*Question No.**1** is compulsory.*

*Attempt any **five** questions from the remaining **six** questions.*

Time Allowed – 3 Hours **Maximum Marks – 100**

1. (a) Mr. X decided to wear his marriage coat in family function. He gave the coat to the laundry for the dryclean. Launderer gives X a receipt for the received clothe with the printed condition on the back side that only 10% of the amount will be paid in case of the damage of the clothes. X, without reading the terms keeps the receipt in the pocket. After taking the delivery, X finds the coat to be damaged. Examine the position of X in the light of the Indian Contract Act,1872? *(5 Marks)*

(b) Explain the power of the company to close the register of members or debenture holders or other security holders as per the Companies Act, 2013. State the manner in which the corresponding provision given under the Companies Act, 1956 differs from the law given under new Act. *(5 Marks)*

(c) State with reasons as to nature of ethics, whether the following statements are correct or incorrect:

(i) Ethics is following the law.

(ii) Ethics is not science. *(5 Marks)*

(d) What are the different ways of non-verbal communication? *(5 Marks)*

2. (a) (i) A company employed 20 full–time and 5 part-time employees who were drawing salary of less than Rs. 10,000 per month. After completing service of 28 days, in an accounting year, 10 full-time employees submitted their resignations and left the service of the company. The Board of directors of this company decided not to give the bonus to the employees, who resigned the services.

Decide, stating the provisions of the Payment of Bonus Act, 1965, whether the employees, who resigned, will get relief. *(4 Marks)*

(ii) Mr. K, an employee in a coal mine with five days working in a week. K was not in continuous service during the financial year 2012-2013. He worked only for 150 days and due to arising out of an accident during working in a mine, he was on leave with full pay for 45 days. Referring to the provisions of the Payment of Gratuity Act, 1972 decide, whether K is entitled to gratuity payable under the Act? *(4 Marks)*

(b) What is the concept behind emphasizing the ecological ethics. *(4 Marks)*

(c) Explain how 'interpersonal communication is inescapable and irreversible'. *(4 Marks)*

3. (a) (i) Discuss with reasons, in the following given conditions, whether X can be called as a 'holder' under the Negotiable Instruments Act, 1881:

(I) X who obtains a cheque drawn by Y by way of gift.

(II) X, the payee of the cheque, who is prohibited by a court order from receiving the amount of the cheque.

(III) X, finds a cheque payable to bearer, on the road and retains it.

(IV) X, the agent of Y, is entrusted with an instrument without endorsement by Y, who is the payee.

(V) X, steals a blank cheque of Y and forges Y's signature. *(5 Marks)*

(ii) Referring to the provision of the Negotiable Instruments Act, 1881, examine the validity of the following:

'A Bill of Exchange originally drawn by M for a sum of Rs. 10,000, but accepted by R only for Rs. 7,000.' *(3 Marks)*

(b) Explain "communications is another area in which ethical concern may arise".

(4 Marks)

(c) How negotiations can be approached? *(4 Marks)*

4. (a) An allottee of shares in a Company brought action against a Director in respect of false statements in prospectus. The director contended that the statements were prepared by the promoters and he has relied on them. Is the Director liable under the circumstances? Decide referring to the provisions of the Companies Act, 2013.

(8 Marks)

(b) What are the common CSR policies ?. *(4 Marks)*

(c) Draft the performa of affidavit for not obtaining Marriage certificate. *(4 Marks)*

5. (a) A, the bailor, pledges a cinema projector and other accessories with Cine Association Co-operative Bank Limited, the bailee, for a loan. A requests the bank to allow the pledged goods to remain in his possession and promises to hold the same in trust for the bailee and also further promises to handover the possession of the same to the bank whenever demanded. Examining the provisions of the Indian Contract Act, 1872 decide, whether a valid contract of pledge has been made between A, the bailor and Bank, the bailee? *(8 Marks)*

(b) Write a note on the powers of the Central Government with respect to the Companies Act, 1956 in regard to conversion of debentures and loans into shares of the company under the following heads:

(i) When terms of issue of such debenture or terms of loan do not include term providing for an option of conversion;

(ii) Matters considered in determining the terms and conditions of such conversion. *(4 Marks)*

(c) State with reason whether the following statement is correct or incorrect: *(4 Marks)*

(i) A good environmental practice improves corporate performance'

(ii) Business and industry are closely linked with environment and resource utilization'.

6. (a) State the procedure for passing a resolution by Postal Ballot as per the Companies Act, 1956. *(8 Marks)*

(b) Draft a letter informing the customer that his cheque has been dishonoured. *(4 Marks)*

(c) State whether the following statements are correct or incorrect: *(4 Marks)*

(i) A proposal may be revoked by the proposer before the posting of the letter of acceptance by the acceptor.

(ii) 'An agreement with an alien friend is valid but an agreement with an alien enemy is void'.

(iii) Term "Significant influence" used in the definition of Associate company under the Companies Act, 2013 means control of at least 2% of total share capital, or of business decisions under an agreement.

(iv) As per the Companies Act, 2013 , Cash flow statement is the compulsory part of the financial statement of one person company, small company and dormant company.

7. Answer any FOUR of the following: *(4 x 4=16 Marks)*

(a) Examine the law relating to review of order regarding determination of applicability of the EPF & MP Act, 1952 and the money due. *(4 Marks)*

(b) M/s X Ltd. was incorporated on 1.4.2013. No General Meeting of the company has been held so far. Explain the provisions of the Companies Act, 1956 regarding the time limit for holding the first annual general meeting of the Company and the power of the Registrar to grant extension of time for the First Annual General Meeting. *(4 Marks)*

(c) State the purposes for which the Securities Premium Account can be used under the provisions of the Companies Act, 1956. *(4 Marks)*

(d) Explain the pragmatic reasons for maintaining ethical behaviour in marketing through marketing executives. *(4 Marks)*

(e) ABC Ltd. proposes to convene an EGM for changing the name of the company to BCD Ltd. Draft the notice for calling the EGM of the members.

(4 Marks)

Test Series: September, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 2 : BUSINESS LAWS, ETHICS AND COMMUNICATION

SUGGESTED ANSWERS/HINTS

1. **(a)** According to the Indian Contract Act, 1872, sometimes there are situation where there are contracts with special conditions. These special conditions are conveyed tacitly and the acceptance of these conditions are also conveyed by the offeree again tacitly or without him even realizing it.

   Where a launderer gives his customer a receipt for clothe received for drycleaning. The receipt carries special conditions and are to be treated as having been duly communicated to the customer and therein a tacit acceptance of these conditions is implied by the customer's acceptance of the receipt *[Lily White vs. R. Muthuswami [1966] A. Mad. 13].*

   Thus in the given problem, X cannot claim the full cost of the marriage coat and has right to get only 10% of the cost of the clothe.

   (b) **Power to close register of members or debenture holders or other security holders-** Section 91 of the Companies Act, 2013 deals with the closing of the register of members. The provision says that-

   (i) **Closing of register of members, debenture holders or other security holder by giving previous notice-** A company may close the register of members or the register of debenture-holders or the register of other security holders for any period or periods not exceeding in the aggregate forty-five days in each year, but not exceeding thirty days at any one time, subject to giving of previous notice of at least seven days or such lesser period as may be specified by Securities and Exchange Board for listed companies or the companies which intend to get their securities listed, in such manner as may be prescribed.

   (ii) **If the register of members or of debenture-holders or of other security holders is closed without giving the notice or after giving shorter notice** than that so provided, or for a continuous or an aggregate period in excess of the limits specified above, the company and every officer of the company who is in default shall be liable to a penalty of 5,000/- for every day subject to a maximum of one lakh rupees during which the register is kept closed.

   Point of comparison with respect to the Companies Act, 1956-

   - This section of 2013 Act replaces section 154(Power to close register of members or debenture holders) of the 1956 Act.

- The new Act of 2013 introduces the closure of the Registers of other security holders in the provision.
- Listed companies or the companies which intend to get their securities listed(i.e., the unlisted companies) close the register of members/ register of debenture-holders / the register of other security holders by giving a previous notice of at least 7 days/ such lesser period as may be specified by Securities and Exchange Board. This law pertaining to listed companies is lacking in the 1956 Act.
- In case of default with respect to the closure of register of member / register of debenture-holders / the register of other security holders, there the company and every officer of the company who is in default shall be liable to a penalty of five thousand rupees for every day during which register is closed but not exceeding one lakh rupees. This limit of penalty is lacking in 1956 Act.

(c) **(1)** **Incorrect:** A good system of law does incorporate many ethical standards, but Law can deviate from what is ethical. Law can become ethically corrupt, as some totalitarian regimes have made it. Law can be made to be a function of power alone and designed to serve the interests of narrow groups. Law may have a difficult time designing or enforcing standards in some important areas, and may be slow to address new problems.

Hence, Ethics is not following the law.

(2) **Correct:** Social and natural science can provide important data to help us make better ethical choices. But science alone does not tell us what we ought to do. Science may provide an explanation for what humans are like. But ethics provides reasons for how humans ought to act. And just because something is scientifically or technologically possible, it may not be ethical to do it.

Hence, Ethics is not science.

(d) **One may continue to communicate non-verbally through:**

Kinesics or Body language: All our bodily movements, gestures, postures etc., are guided by our feelings and thought processes. The nodding of our head, blinking of our eyes, waving of our hands, shrugging of our shoulders etc., are expressions of our thought and feelings. All these movements are the signals that our body sends out to communicate.

Paralanguage: The term paralanguage is used to describe a wide range of vocal characteristics like tone, pitch, and speed etc – vocal cues that accompany spoken language which help to express and reflect the speaker's attitude.Speaker uses a vast range of vocal cues like:

(a) Pitch Variation

(b) Speaking

(c) Pause

(d) Volume variation

(e) Non – fluencies

(f) Word Stress

Artificial Communication : It is well known that we react to people on the basis of their appearance. The use of personal adornment like clothing , accessories, makeup, hairstyle etc. provides important non verbal cues about one's age, social and economic status, educational level, personality etc.

Proxemics : refers to the space that exists between us when we talk or relate to each other as well the way we organize space around us. We can also call it 'space language".

Chronemics or Time language: is the study of how we use time to communicate. Punctuality is an important factor in time communication. Misunderstandings or disagreements involving time can create communication and relationship problems.

Haptics : is communication through touch .How we use touch sends important messages about us. It reveals our perceptions of status, our attitudes and even our needs.

Silence: The absence of paralinguistic and verbal cues also serves important communicative functions.

2. (a) (i) In accordance with the provisions of Section 2(13) of the Payment of Bonus Act, 1965 any person other than an apprentice employed on a salary or wage not exceeding Rs. 10,000 per month in any industry to do any skilled or unskilled, manual, supervisory, managerial, administrative, technical or clerical work for hire or reward whether the terms of employment be express or implied is eligible for bonus. Further, in accordance with the provisions of Section 8 of the Payment of Bonus Act, 1965 every employee of an establishment covered under the Act is entitled to bonus from his employer in an accounting year provided he has worked in that establishment for not less than thirty working days in the year on a salary less than Rs. 10,000 per month.

The problem as asked is based on the above provisions of the Act. According to it, the employees who have resigned are not entitled to bonus because they have given their services only for 28 days in an accounting year although they are drawing salary less than Rs. 10,000 per mensem.

(ii) As per Section 2 A of the Payment of Gratuity Act, 1972 an employee shall be said to be in continuous service for a period if he has, for that period, been in uninterrupted service, including service which may be interrupted on account of sickness, accident, leave, lay-off, strike or a lockout or cessation of work not due to any fault of an employee.

Where any employee (not being an employee employed in a seasonal establishment) is not in continuous service for any period of one year he shall be deemed to be in continuous service under the employer for the said period of one year, if the employee during the period of twelve calendar months preceding the date with reference to which calculation is to be made, has actually worked under the employer for not less than (i) one hundred and ninety days, in the case of any employee employed below the ground in a mine or in an establishment which works for less than six days in a week, and (ii) two hundred and forty days, in any other case.

For the purposes of calculating the number of days on which an employee has actually worked under an employer shall include the days on which the person was absent due to temporary disablement caused by accident arising out and in the course of his employment.

Thus, as per the above provisions, K is entitled for gratuity because he was in continuous service (150+45 days) more than 190 days in 2012-2013 and was working in a mine with 5 days in a week(less than six days in a week).

(b) Ecological ethics is based on the concept that the environment should be protected not only for the sake of human beings but also for its own sake. The issue of environmental ethics goes beyond the problems relating to protection of environment or nature in terms of pollution, resource utilization or waste disposal. It is the issues of exploitive human nature and attitudes that should be addressed in a rational way. Problems like Global warming, Ozone depletion and disposal of hazardous wastes that concern the entire world. They require International cooperation and have to be tackled at the global level.

Unless businesses recognize the interrelationships and interdependencies of the ecological systems within which they operate and unless they ensure that their activities will not seriously injure these systems one cannot hope to deal with the problem of pollution.

(c) The following principles are key to interpersonal communication:

Interpersonal communication is inescapable: We cannot keep ourselves away from communication. The very attempt not to communicate, communicates something. Not only through words but also through the tone of voice and gestures, postures, facial expressions etc, we constantly communicate to others.

Interpersonal communication is irreversible: A Russian proverb says, "Once a word goes out of your mouth, you can never swallow it again." You cannot really take back something once it has been said. The effect will inevitably remain.

3. (i) Person to be called as a holder: As per section 8 of the Negotiable Instruments Act, 1881 ‘holder’ of a Negotiable Instrument means any person entitled in his own name to the possession of it and to receive or recover the amount due thereon from the parties thereto.

On applying the above provision in the given cases-

(I) Yes, X can be termed as a holder because he has a right to possession and to receive the amount due in his own name.

(II) No, X is not a 'holder' because to be called as a 'holder' he must be entitled not only to the possession of the instrument but also to receive the amount mentioned therein.

(III) No, X is not a holder of the Instrument though he is in possession of the cheque, so is not entitled to the possession of it in his own name.

(IV) No, X is not a holder. While the agent may receive payment of the amount mentioned in the cheque, yet he cannot be called the holder thereof because he has no right to sue on the instrument in his own name.

(V) No, X is not a holder because he is in wrongful possession of the instrument

(ii) As per the provisions of the Negotiable Instruments Act 1881, acceptance may be either general or qualified. It is qualified when the drawee does not accept the bill according to the apparent tenor of the bill but attaches some condition or qualification which have the effect of either reducing his (acceptor's) liability or acceptance of this liability is subject to certain condition. The holder of the bill is entitled to require an absolute and unconditional acceptance, otherwise he will treat it as dishonoured however, he may agree to qualified acceptance but he does so at his own peril, since he discharges all parties prior to himself, unless he has obtained their consent.

Thus in this given case in accordance with the Explanation to Section 86 of the Act, when the drawee undertakes the payment of part only of the sum ordered to be paid, it is a qualified acceptance and the drawer may treat it as dishonoured unless agreed by him. If the Drawer (M) agrees to acceptance, the drawee (R) is responsible for a sum of Rs. 7000 only.

(b) Communications is another area in which ethical concerns may arise. False and misleading advertising, as well as deceptive personal-selling tactics, anger consumers and can lead to the failure of a business. Truthfulness about product safety and quality are also important to consumers. The Food and Drug Regulatory authorities need to ensure that customers are told the truth about product safety, quality, and effectiveness claims. Some manufacturers fail to provide enough information to consumers about differences or similarities between products.

For *example*, a lawsuit filed by consumers against Johnson claimed that the company's Acuvue and 1-Day Acuvue contact lenses were actually the same product. Consumers were directed by the company to dispose of the 1-Day Acuvue lenses after one day's use. The suit claims that because the two products were identical, the lenses could have been worn up to two weeks. It is estimated that six million people who used contact lenses spent $1.1 billion on unnecessary replacements because of the company's misleading advertising. Johnson & Johnson agreed to pay up to $860 million to settle the complaints. Another important aspect of communications that may raise ethical concerns relates to product labelling. It is mandatory for cigarette manufacturers to indicate clearly on cigarette packing that smoking cigarettes is harmful to the smoker's health.

(c) *Negotiati*on occurs when two or more parties-either individuals or groups discuss specific proposals in order to find a mutually acceptable agreement.

Negotiations can be approached in four ways. Each of these approaches produces a different outcome.

Win-Lose Orientation : This is the approach taken by competitive communicators. The win-lose orientation is based on the assumption that only one side can reach its goals and that any victory by that party will be matched by the other's loss. Despite the fact that it produces losers as well as winners, a win-lose orientation can sometimes be the best approach to negotiating.

Lose-Lose Orientation: With a lose-lose orientation, a conflict plays out in a way that damages both parties to such a degree that everyone feels like a loser. Nobody starts out seeking a lose-lose outcome, of course; but sometimes when people feel that a negotiating partner is blocking them, they wind up seeking revenge.

Compromise: Sometimes it seems better to compromise than to fight battles in a competitive manner and risk a lose-lose outcome. There are cases in which compromise is the best obtainable outcome-usually when disputed resources are limited or scarce.

Win-Win Orientatio: A win-win approach differs significantly from the preceding negotiating styles. It is a collaborative approach to negotiation and assumes that solutions can be reached that satisfy the needs of all parties .

4. (a) Yes, the Director shall be held liable. A director can escape liability for mis-statements in a prospectus only on the grounds specified under Section 34 and 35 of the Companies Act, 2013. Relying on statements prepared by promoters is not a ground included there under. Accordingly, no defence shall be available to the Director.

A Director shall not be liable if he puts up the following defences:

(i) Such statement or omission in the prospectus was immaterial, or

(ii) Director had reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was necessary(Section 34, the Companies Act, 2013)

(iii) Where a person having consented to become a director of the company, withdrew his consent before the issue of the prospectus, and that it was issued without his authority or consent; or where the prospectus was issued without the knowledge or consent of a person, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent (Section 35, the Companies Act, 2013).

(b) CSR Policies : Corporate Social Responsibility (CSR) refers to operating a business in a manner that accounts for the social and environmental impact created by the business. CSR means a commitment to developing policies that integrate responsible practices into daily business operations, and to reporting on progress made toward implementing these practices.

Common CSR policies include:

- Adoption of internal controls reform in the wake of Enron and other accounting scandals;
- Commitment to diversity in hiring employees and barring discrimination;
- Management teams that view employees as assets rather than costs;
- High performance workplaces that integrate the views of line employees into decision-making processes;
- Adoption of operating policies that exceed compliance with social and environmental laws;
- Advanced resource productivity, focused on the use of natural resources in a more productive, efficient and profitable fashion (such as recycled content and product recycling); and
- Taking responsibility for conditions under which goods are produced directly or by contract employees domestically or abroad.

(c) Affidavit

I, ...S/o............R/o.............................do hereby solemnly affirm and declare an oath as under:

"That the marriage between......(name of spouses with details) solemnized with the Hindu rituals on.......... at.......(Name of place) .That due to inadvertence, I did not register my marriage with the concerned department.

Date:………………….. Signature

Place:…………………. Deponent

5. (a) Delivery to pawnee under Indian Contract Act, 1872: The problem as asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in Section 149 (delivery to bailee and pledgee). The Section provides that the delivery of the goods to the bailee may be made by actual or constructive delivery or delivery by attornment to the bank. In such a case there is change in the legal character of the possession of goods though not in the actual or physical custody. Though the bailor continues to be in possession of the goods, it is the possession of the bailee.

In the given problem the delivery of the goods is constructive i.e. delivery by attornment to the bailee (pawnee) and the possession of the goods by A, the bailor is construed as possession by bailee/pawnee, the Bank. A constructive pledge comes into existence as soon as the pawnor, without actually delivering the goods, promises to deliver them on demand. The transaction was, therefore, a valid pledge. On this point, the decision given by the Andhra Pradesh High Court in *Bank of Chittur Ltd. vs. Narasimhulu AIR 1966 AP 163* is relevant.

(b) **(i)** Under Section 81 of the Companies Act, 1956 where any debentures have been issued to or loans have been obtained from the Government by a company, whether such debentures have been issued or loans have obtained before or after the commencement of Companies Amendment Act, 1963 (w.e.f. 1.1.1964), the Central Government may, if in its opinion it is necessary in the public interest so to do, by order direct that such debentures or loans or any part thereof shall be converted into shares in the company on such terms and conditions as appear to that Government to be reasonable in the circumstances of the case, even if the terms of issue of such debentures or the terms of such loans do not include term providing for an option for such conversion.

(ii) In determining the terms and conditions of such conversion, the Central Government shall have due regard to the following circumstances:

(1) The financial position of the company;

(2) The terms of issue of the debentures or the terms of the loans, as the case may be;

(3) The rate of interest payable on the debentures or the loans;

(4) The capital of the company, its loan liability, its reserves, its profits during the preceding five years; and

(5) The current market price of the shares in the company.

A copy of every order proposed to be issued by the Central Government shall be laid in draft before each House of Parliament.

(c) **(i)** **Correct:** Environmental consideration have become a part of corporate strategy, which means incorporating environmental issues in the process of developing a product, in new investments and in the organisational set up. A good environmental practice improves corporate performance. In many industries it has been found that environmental friendly practices have resulted in more saving; for example the process of recycling the waste. Thus environmental considerations play a key role in corporate strategy. Markets of new millennium will be able to create wealth if they respond to the challenges of sustainable development, as unsustainable products will become obsolete.

(ii) **Correct:** Business and industry are closely linked with environment and resource utilization. Production process and strategy for eco-friendly technologies throughout the product life cycle and minimization of waste play a major role in the protection of the environment and conservation of resources. Business, industry and multinational corporations have to recognize environmental management as the priority area and a key determinant to sustainable development.

6. **(a)** A listed public company and in case of resolutions relating to such business as the Central Government may, by notification, declare to be conducted only by postal ballot, shall get any resolution passed by means of a postal ballot, instead of transacting the business in general meeting of the company. The term 'Postal Ballot' includes voting by electronic mode.

The procedure laid down in Section 192A of the Companies Act, 1956 is as under:

(i) **Notice to shareholders** : Where a company decides to pass any resolution by resorting to postal ballot, it shall send a notice to all the shareholders, along with a draft resolution explaining the reasons therefore and requesting them to send their assent within a period of 30 days from the date of posting of the letter;

(ii) **Notice shall be sent by registered post acknowledgement:** The notice shall be sent by registered post acknowledgement due or by any other method as may be prescribed by the Central Government in this behalf, and shall be annexed with the notice a postage pre-paid envelope for facilitating the communication of the assent or dissent of the shareholder to the resolution within the said period;

(iii) **Appointment of scrutinizer:** The board of directors shall appoint one scrutinizer, who is not in employment of the company, may be a retired judge or any person of repute, who, in the opinion of the board can conduct the postal ballot voting process in a fair and transparent manner;

(iv) **Submission of report by the scrutinizer:** The scrutinizer will be in position for 35 days (excluding holidays) from the date of issue of notice for annual general meeting. He is required to submit his final report on or before the said period.

(v) **Resolution assented by majority:** If a resolution is assented to by a requisite majority of the shareholders by means of postal ballot, it shall be deemed to have been passed at a general meeting convened in that behalf.

For this purpose the scrutinizer willing to be appointed is available at the registered office of the company for ascertaining the requisite majority.

(vi) **Fraudulent defence or destroy of postal ballot:** If a shareholder sends his assent or dissent in writing on a postal ballot and thereafter any person fraudulently defences or destroys the ballot paper or declaration of the identity of shareholder, such person shall be punishable with imprisonment for a term which may extend to six months or with fine or both;

(vii) **Maintenance of register by scrutinizer:** The scrutinizer shall maintain a register to record the consent received, including electronic media, mentioning the particulars of name, address, folio number, number of shares, nominal value of shares, whether the shares have voting, differential voting or non-rights and the scrutinizer shall also maintain record for postal ballot which are received in defaced or mutilated form. The postal ballot and all other papers relating to postal ballot will be under the safe custody of the scrutinizer till the Chairman considers, approves and signs the minutes of the meeting. Thereafter, the scrutinizer shall return the ballot papers and other related papers/register to the company so as to preserve such ballot papers and other related papers/registers safely till the resolution is given effect to.

(b)

-----------Bank Ltd

----------Branch,
New Delhi

To,

Date…………

Regarding: Dishonour of cheque no.-------drawn on ----------, dated--------

Dear Sir,

We inform you that your above cheque due to insufficient fund in your account was not clear and was received back by us. The cheque has been sent to you by registered post dated --------- at your residential address.

Sd/-

Manager of the Bank

(c) (i) Correct

(ii) Correct

(iii) Incorrect

(iv) Incorrect

7. (a) Any person aggrieved by order under Section 7A(1) can make application for review of the order in following cases – (a) if new and important evidence is discovered which could not be produced earlier as it was not within his knowledge even after due diligence (b) there is some mistake or error apparent on the records or (c) any other sufficient reason. No application for review can be made if appeal was filed.

The officer can himself review the order on his own motion. [Section 7B(1)]. The officer can either reject the application for review if there are not sufficient grounds for review, or he can grant the review. [Section 7B(4)]. Appeal cannot be filed against order rejecting the application for review. However, if fresh order is passed after the review, appeal can be filed against such order [Section 7B(5)].Application for review should be made within such form and manner and in time as may be specified in the Scheme.

In *Balu Fire Clay Niwas v. U.O.I., 2003 LLR 578 (Jhar HC)*, it was held that when statute provides for review, it cannot be contended that petitioner should have filed appeal against the order. It was also held that review petition should be disposed of by a speaking order.

(b) According to Section 166 of the Companies Act, 1956, every company shall hold its first annual general meeting within a period of 18 months from the date of incorporation. Since M/s X Ltd was incorporated on 1.4.2013, the first annual general meeting of the company should be held on or before 30th September, 2014. Even though the Registrar of Companies is empowered to grant extension of time for a period not exceeding 3 months for holding the annual general meeting, such a power is not available to the Registrar in the case of the first annual general meeting. Thus, the company and its directors will be liable for the default if the annual general meeting is held after 30th September. 2014.

(c) **Issue of securities at premium (Section 78 of the Companies Act, 1956):** If the market exists, a company may issue its securities at premium i.e. the price higher than their nominal value. There is no restriction contained in the Companies Act, 1956 on the sale of shares at a premium. But SEBI guidelines have to be observed as they indicate when an issue has to be at par and when premium is chargeable. Premium may be received in cash or kind. Where the value of assets received by a company as a consideration for allotment is greater than the nominal value of shares, it is in essence an allotment at a premium. An amount equal to extra value of the assets would have to be carried to the securities premium account. The amount to the credit of share premium account has to be maintained with the same sanctity as share capital and can be reduced only in the manner of share capital.

The Act does regulate the disbursement of the amount collected as premium. Such account be used in the following ways be the company.

(I) it may be applied to issue to the members as fully paid by way of bonus the unissued shares of the company.

(II) it may be used to write off preliminary expenses.

(III) it may be used to write off the expenses of commission paid or discount allowed.

(IV) it may be spent in providing for the premium payable on the redemption of any redeemable preference shares or debentures of the company.

(d) Pragmatic reasons for maintaining ethical behaviour: Marketing executives should practice ethical bahaviour because it is morally correct. To maintain ethical behaviour in marketing, the following positive reasons may be useful to the marketing executives:

1. **To reverse declining public confidence in marketing:** Sometime misleading package labels, false claim in advertisement, phony list prices, infringement of trademarks pervert the market trends and such behaviour damages the marketers' reputation. To reverse this situation, business leaders must demonstrate convincingly that they are aware of their ethical responsibility and will fulfill it. Companies must set high ethical standards and enforce them. Moreover, it is in management's interest to be concerned with the well being of consumers, since they are the lifeblood of a business.

2. **To avoid increase in government regulation:** Business apathy, resistance, or token responses to unethical behaviour increase the probability of more governmental regulation. The governmental limitations may also result from management's failure to live up to its ethical responsibilities. Moreover, once the government control is introduced, it is rarely removed.

3. **To retain power granted by society:** Marketing executives wield a great deal of social power as they influence markets and speak out on economic issues. However, there is a responsibility tied to that power. If marketers do not use their power in a socially acceptable manner, that power will be lost in the long run.

4. **To protect the image of the organisation:** Buyers often form an impression of an entire organisation based on their contact with one person. That person represents the marketing function. Some times a single sales clerk may pervert the market opinion in relation to that company which he represents.

   Therefore, the ethical behaviour in marketing may be strengthened only through the behaviour of the marketing executives.

(e) Notice for Extraordinary General Meeting of the Members

Notice is hereby given that extraordinary General Meeting of the members of ABC Limited will be held on Monday, the ……day of 2014, at the registered office of the company at…….Mumbai at……..P.M. to transact the following business.

Special Business

To consider and if thought fit, to pass with or without modification the following resolution as special resolution.

"Resolved that, subject to the approval of the Central Government under section 21 of the Companies Act,1956, the name of the company be and is changed from ABC to BCD Limited and that consequent to this change clause I of the Memorandum and Articles of Association of the company be altered accordingly.

By order of the Board of Directors of ABC Limited.

Secretary…………………………….

Place:…………………………………

Date:………………………………….

Test Series: September, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – I : COST ACCOUNTING

*Question No. **1** is compulsory.*

*Attempt any **five** questions from the remaining **six** questions.*

Working notes should form part of the answer.

Time Allowed – 1 ½ Hours **Maximum Marks – 50**

1. Answer the followings:

(a) The Profit as per cost accounts of Venkatesh Pvt. Ltd., for the quarter ended 30th June, 2014 is Rs. 3,65,200. The following information is extracted from the books of Venkatesh Pvt. Ltd., for the quarter ended 30th June, 2014:

(i)

Stocks	As per Cost Accounts (Rs.)	As per Financial Accounts (Rs.)
Opening stocks:		
- Raw Material	52,800	55,600
- Work in Progress	21,200	22,300
Closing stocks:		
- Raw Material	56,000	54,200
- Work in Progress	18,600	17,500
- Finished Goods	18,000	16,000

(ii) Directors' fees Rs. 52,000, Interest expenses Rs. 9,600, Provision for doubtful debts Rs. 1,300 and dividend received Rs. 3,800 have been considered in the financial accounts only.

(iii) Notional rent of Rs. 7,200 was charged only in the cost accounts.

(iv) Research expenses written-off of Rs. 13,600 has not been charged in the cost accounts.

(v) Other overheads for the quarter as per the financial accounts were Rs. 1,28,000 and as per the cost accounts, it was Rs. 1,30,400.

You are required to prepare, a statement showing profit/ loss as per financial accounts.

(b) Kevin Ltd. produces a product 'C123', the cost structure of product C123 is as follows:

	Amount per unit (Rs.)
Direct Material	1,650
Direct Labour	925
Variable overheads	315
Total Variable cost	2,890

Selling price of C123 is Rs. 3,400 per unit and quantity of sales is 55,000 units per annum. Total fixed cost per annum is Rs. 1,80,00,000.

You are required to calculate:

(i) Break-even sales in units.

(ii) Margin of safety in units

(iii) If the total variable cost increased by 10% and fixed cost increased by Rs. 20,00,000, how many additional units of C123 should be sold in order to obtain the present profit while selling price per unit remains unchanged.

(2 x 5 Marks = 10 Marks)

2. From the following information for the month of July, 2014, prepare Process-III cost accounts.

Opening WIP in Process-III	1,600 units at Rs. 24,000
Transfer from Process-II	55,400 units at Rs. 6,23,250
Transferred to warehouse	52,200 units
Closing WIP of Process-III	4,200 units
Units Scrapped	600 units
Direct material added in Process-III	Rs. 2,12,400
Direct wages	Rs. 96,420
Production overheads	Rs. 56,400

Degree of completion:

	Opening Stock	Closing Stock	Scrap
Material	80%	70%	100%
Labour	60%	50%	70%
Overheads	60%	50%	70%

The normal loss in the process was 5% of the production and scrap was sold @ Rs. 5 per unit.

(Students may treat material transferred from Process – II as Material – A and fresh material used in Process – III as Material B) *(8 Marks)*

3. Swift Cabs Pvt. Ltd. is a New Delhi based cab renting company, provides cab facility on rent for cities Delhi, Agra and Jaipur to the tourists. To attract more tourists it has launched a new three days tour package for Delhi-Jaipur-Agra-Delhi. Following are the relevant information regarding the package:

Distance between Delhi to Jaipur (Km.)	274
Distance between Delhi to Agra (Km.)	242
Distance between Agra to Jaipur (Km.)	238
Price of diesel in Delhi	Rs. 54 per litre
Price of diesel in Jaipur	Rs. 56 per litre
Price of diesel in Agra	Rs. 58 per litre
Mileage of cab per litre of diesel (Km.)	16
Chauffeur's salary	Rs. 12,000 per month
Cost of the cab	Rs. 12,00,000
Expected life of the cab	24,00,000 kms.
Servicing cost	Rs. 30,000 after every 50,000 kilometres run.
Chauffeur's meal allowance	Rs. 50 for every 200 kilometres of completed journey
Other set up and office cost	Rs. 2,400 per month.

Swift Cabs has made tie-up with fuel service centres at Agra, Jaipur and Delhi to fill diesel to its cabs on production of fuel passbook to the fuel centre. Company has a policy to get fuel filled up sufficient to reach next destination only.

You are required to calculate the price inclusive of service tax @ 12.36% to be quoted for the package if company wants to earn profit of 25% on its net takings i.e. excluding service tax. *(8 Marks)*

4. August Furniture makes different varieties of office furniture. It makes 7 revolving chairs per hour by employing 5 skilled, 10 semiskilled and 20 unskilled workers. The standard wage rate is Rs. 24 per labour hour. During the last week workers worked for 56 hours and made 400 revolving chairs. 2% of the time paid was lost due to the abnormal reasons. The actual hourly rate paid to skilled, semiskilled and unskilled workers were Rs.30, Rs.24 and Rs.18 respectively.

You are required to calculate

(i) Labour Cost Variance

(ii) Labour Rate Variance

(iii) Labour Efficiency Variance and

(iv) Idle Time Variance. *(8 Marks)*

5. (a) (i) Discuss accounting treatment of idle capacity costs in cost accounting.

   (ii) List any four functional budgets prepared by a business organization.

   (b) Distinguish between job costing and process costing *(4 x 2 = 8 Marks)*

6. Panchal Group undertook a contract for Rs. 5,00,000 on 1st April 2013. On 31st March 2014 when the accounts were closed, the following details about the contract were gathered:

	Rs.
Materials purchased	1,25,000
Wages paid	45,000
General expenses	12,000
Plant purchased	1,25,000
Material in hand 31.3.2014	25,000
Wages accrued 31.3.2014	15,000
Work certified	2,50,000
Cash received	2,00,000
Work uncertified	15,000
Depreciation of plant	12,500

The contract contained an escalation clause, which read as follows:

"In the event of increase(s) of prices of materials and rates of wages by more than 5%, the contract price would be increased accordingly by 25% of the rise of the cost of materials and wages beyond 5% in each case."

It was found that since the date of signing the agreement, the prices of materials and wage rates increased by 25%. The value of the work certified does not take into account the effect of the above clause.

Prepare the contract account. The workings should form part of your answer. *(8 Marks)*

7. (a) Explain the treatment of over and under absorption of overheads in cost accounting.

   (b) Distinguish between fixed and flexible budget. *(4 x 2 =8 Marks)*

Test Series: September, 2014

MOCK TEST - I

INTERMEDIATE (IPC) – Group I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – II : FINANCIAL MANAGEMENT

All questions are compulsory.

Working notes should form part of the answer.

Time Allowed – 1 ½ Hours **Maximum Marks – 50**

1. Answer the following questions, supporting the same with reasoning/working notes:

   (a) Mr. X wants to buy an ordinary annuity that will pay him Rs. 4,000 a year for the next 20 years. He expects annual interest rates will be 8 per cent over that time period. Calculate the maximum price he would be willing to pay for the annuity.

   (b) EOQ is the order quantity that minimizes total carrying costs over our planning horizon. Is the statement true or false?

   (c) If two projects are completely independent (or unrelated), what is the measure of correlation between them?

   (d) A firm's degree of operating leverage (DOL) depends primarily upon its sales variability. Is the statement true or false? *(4 × 2 = 8 Marks)*

2. (a) The following data applies to Alpha Limited (Rs. in crores):

	Rs.
Cash and marketable securities	10.00
Fixed Assets	28.35
Sales	100.00
Net income	5.00
Current liabilities	10.55
Current ratio	3.0 ×
DSO*	40.55 days
ROE	12%

*Calculation is based on a 365 days year.

The company has no preference shares – only equity shares, current liabilities, and long-term debt.

You are to calculate Alpha Limited's (i) Accounts receivable (A/R), (ii) Current assets, (iii) Total assets, (iv) ROA, (v) Common equity, and (vi) Long-term debt.

If Alpha Limited's accounts receivable (A/R) = Rs. 11.10 crores. If the company could reduce its DSO from 40.55 days to 30.4 days while holding other things constant, how much cash would it generate? If this cash were used to buy back equity shares (at book value), thus reducing the amount of equity, how would this affect (i) the ROE, (ii) the ROA, and (iii) the total debt/total assets ratio?

(b) You are a financial analyst for Beta Limited. The director of finance has asked you to analyse two proposed capital investments, Projects X and Y. Each project has a cost of Rs. 10,000, and the cost of capital for each project is 12 per cent. The project's expected net cash flows are as follows:

Year	*Expected net cash flows*	
	Project X	*Project Y*
	Rs.	*Rs.*
0	(10,000)	(10,000)
1	6,500	3,500
2	3,000	3,500
3	3,000	3,500
4	1,000	3,500

(i) Calculate each project's payback period, net present value (NPV), internal rate of return (IRR), and modified internal rate of return (MIRR).

(ii) Which project or projects should be accepted if they are independent?

(iii) Which project should be accepted if they are mutually exclusive?

(12 + 8= 20 Marks)

3. (a) There are two companies, Company A and B having Net Operating Income of Rs. 15,00,000 each. Company B is a levered company whereas company A is all equity company. Debt employed by Company B is of Rs. 7,00,000 @ 11%. The tax rate applicable to both the companies is 25%. Calculate:

(i) Earnings available for equity and debt for both the companies.

(ii) Present value of tax shield.

(b) A proforma cost sheet of a Company provides the following particulars:

	Amount per unit (Rs.)
Raw materials cost	100
Direct labour cost	37.50
Overheads cost	75
Total cost	212.50
Profit	37.50
Selling Price	250

The Company keeps raw material in stock, on an average for one month; work-in-progress, on an average for one week; and finished goods in stock, on an average for two weeks.

The credit allowed by suppliers is three weeks and company allows four weeks credit to its debtors. The lag in payment of wages is one week and lag in payment of overhead expenses is two weeks.

The Company sells one-fifth of the output against cash and maintains cash-in-hand and at bank put together at Rs.37,500.

You are required to prepare a statement showing estimate of Working Capital needed to finance an activity level of 1,30,000 units of production. Assume that production is carried on evenly throughout the year, and wages and overheads accrue similarly. Work-in-progress stock is 80% complete in all respects. (For calculation purposes, four weeks has been considered equivalent to 1 month and 1 year is = 52 weeks)

(6 + 8 = 14 Marks)

4. Answer the following:

(a) Differentiate between the following:

(i) Deep Discount Bonds and Zero Coupon Bonds

(ii) Investment Decision and Financing Decision

(b) Write a short note on Seed Capital Assistance. *(6 + 2 = 8 Marks)*

Test Series: October, 2014

MOCK TEST PAPER – 2

INTERMEDIATE (IPC): GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – I : COST ACCOUNTING

Suggested Answers/ Hints

1. (a) Calculation of effective wages rate and weekly earnings of the workers A, B and C

Workers	A	B	C
Standard Output	96 units (8 hrs. × 2 units × 6 days)	96 units (8 hrs. × 2 units × 6 days)	96 units (8 hrs. × 2 units × 6 days)
Actual Output	132 units	108 units	96 units
Efficiency (%)	$\frac{132\text{units}}{96\text{units}} \times 100 = 137.5$	$\frac{108\text{units}}{96\text{units}} \times 100 = 112.5$	$\frac{96\text{units}}{96\text{units}} \times 100 = 100$
Daily wages Rate	₹ 360	₹ 360	₹ 360
Incentive system	Emerson's Efficiency System	Merrick differential piece rate system	Taylor's differential piece work system
Rate of Bonus	57.5% of time rate (20% + 37.5%)	20% of ordinary piece rate	25% of ordinary piece rate
Effective Wage Rate	**₹ 70.875 per hour** $\left(\frac{₹\ 360}{8\text{hours}} \times 157.5\%\right)$	**₹ 27 per piece** $\left(\frac{₹\ 360}{16\text{units}} \times 120\%\right)$	**₹ 28.125 per piece** $\left(\frac{₹\ 360}{16\text{units}} \times 125\%\right)$
Total weekly earnings	**₹ 3,402** (8 hours × 6 days × ₹ 70.875)	**₹ 2,916** (108 units × ₹ 27)	**₹ 2,700** (96 units × ₹ 28.125)

(b) Budgeted Production 30,000 hours ÷ 6 hours per unit = 5,000 units

Budgeted Fixed Overhead Rate = ₹ 4,50,000 ÷ 5,000 units = ₹ 90 per unit Or

= ₹ 4,50,000 ÷ 30,000 hours = ₹ 15 per hour.

(i) Material Cost Variance = (Std. Qty. × Std. Price) – (Actual Qty. × Actual Price)

= (4,800 units × 10 kg. × ₹10) - ₹ 5,25,000

= ₹ 4.80,000 – ₹ 5,25,000

= ₹ 45,000 (A)

(ii) Labour Cost Variance = (Std. Hours × Std. Rate) – (Actual Hours × Actual rate)

= (4,800 units × 6 hours × ₹ 5.50) – ₹1,55,000

= ₹ 1,58,400 – ₹ 1,55,000

= ₹ 3,400 (F)

(iii) Fixed Overhead Cost Variance = (Budgeted Rate × Actual Qty) – Actual Overhead

= (₹ 90 x 4,800 units) – ₹ 4,70,000

= ₹ 38,000 (A)

OR = (Budgeted Rate × Std. Hours) – Actual Overhead

= (₹ 15 x 4,800 units × 6 hours) – ₹ 4,70,000

= ₹ 38,000 (A)

(iv) Variable Overhead Cost Variance= (Std. Rate × Std. Hours) – Actual Overhead

= (4,800 units × 6 hours × ₹ 10) - ₹ 2,93,000

= ₹ 2,88,000 - ₹ 2,93,000

= ₹ 5,000 (A)

2. (a) Production Budget (in units)

	Product- K_{596} (units)	**Product- H_{852} (units)**
Expected sales	8,000	4,200
Add: Closing stock	1,000	2,100
Less: Opening stock	(800)	(1,600)
Units to be produced	8,200	4,700

(b) Material Purchase Budget

	Material-X (kg.)	**Material-Y (kg.)**	**Material-Z (ltr.)**
Materials required:			
- Product-K_{596}	98,400 (8,200 units × 12 kg.)	1,23,000 (8,200 units × 15 kg.)	65,600 (8,200 units × 8 ltr.)
- Product- H_{852}	70,500 (4,700 units × 15 kg.)	28,200 (4,700 units × 6 kg.)	65,800 (4,700 units × 14ltr.)
Total	1,68,900	1,51,200	1,31,400

Add: Closing stock	30,000	18,000	7,500
Less: Opening stock	(25,000)	(30,000)	(14,000)
Quantity to be purchased	1,73,900	1,39,200	1,24,900
Rate	₹15 per kg.	₹16 per kg.	₹5 per ltr.
Purchase cost	₹ 26,08,500	₹ 22,27,200	₹ 6,24,500

(c) Direct Labour Budget

	Unskilled (hours)	**Skilled (hours)**
For Product K_{596}	98,400 (8,200 units × 12 hours)	65,600 (8,200 units × 8 hours)
For Product H_{852}	47,000 (4,700 units × 10 hours)	23,500 (4,700 units × 5 hours)
Labour hours required	1,45,400	89,100
Rate	₹ 40 per hour	₹ 75 per hour
Wages to be paid	₹ 58,16,000	₹ 66,82,500

3. (i) Amount of under/ over absorption of production overheads during the year 2013-14

		(₹)
Total production overheads actually incurred during the year 2013-14		7,20,000
Less: 'Written off' obsolete stores	₹ 15,000	
Wages paid for strike period	₹ 12,000	(27,000)
Net production overheads actually incurred: (A)		6,93,000
Production overheads absorbed by 52,000 machines hours @ ₹15 per hour: (B)		7,80,000
Amount of over-absorption of production overheads: [(B)–(A)]		87,000

(ii) Accounting treatment of over absorption of production overheads: It is given in the statement of the question that 25,000 units were completely finished and 6,000 units were 50% complete, one third of the over-absorbed overheads were due to faulty production planning and the rest were attributable to normal increase/ decrease in costs.

	(₹)
1. (33-1/3% of ₹87,000) i.e. ₹29,000 of over – absorbed overheads were due to faulty production planning. This being abnormal, should be credited to the Profit and Loss A/c	29,000
2 Balance (66-2/3% of ₹87,000) i.e. ₹58,000 of over – absorbed overheads should be distributed over work-in-progress, finished goods and cost of sales by using supplementary rate	58,000
Total over-absorbed overheads	87,000

Apportionment of over-absorbed overhead of ₹58,000 over work-in-progress, finished goods and cost of sales.

	Equivalent Completed units	(₹)
Work-in-progress (3,000 units × ₹2.0714) (Refer to Working Note)	3,000	6,215
Finished goods (5,000 units × ₹2.0714)	5,000	10,357
Cost of sales (20,000 units × ₹2.0714)	20,000	41,428
	28,000	58,000

Accounting treatment:

	Dr. (₹)	Cr. (₹)
Overhead control A/c .... Dr.	87,000	
To Work-in-progress A/c		6,215
To Finished goods control A/c		10,357
To Cost of sales A/c		41428
To Cost Profit & Loss A/c		29,000

Working Note:

Supplementary overhead absorption rate $= \dfrac{₹\,58{,}000}{28{,}000 \text{ units}} =$ ₹2.0714per unit

4. Working notes

1. Annual demand (30,000 units per quarter × 4 quarters) = 1,20,000 units

2. Raw material required for 1,20,000 units (1,20,000 units × 1.5 kg.) = 1,80,000 kg.

3. EOQ $= \sqrt{\dfrac{2 \times 1{,}80{,}000 \text{ kgs.} \times ₹\ 1{,}000}{₹\ 2}} = 13{,}416$ kgs.(appx)

4.Total cost of procurement and storage when the order size is equal to EOQ or 13,416 kg.

No. of orders (1,80,000 kg. ÷ 13,416 kg.) = 13.42 times or 14 times

Ordering cost (14 orders × ₹1,000) = ₹ 14,000

Carrying cost (½ × 13,416 kg. × ₹ 2) = ₹ 13,416

Total cost = ₹ 27,416

(i) **Re-order point** = Safety stock + Lead time consumption

$$= 8{,}000 \text{ kg.} + \frac{1{,}80{,}000 \text{ kg.}}{360 \text{ days}} \times 24 \text{ days}$$

= 8,000 kg. + 12,000 kg. = 20,000 kg.

(ii) **Statement showing the total cost of procurement and storage of raw materials** (after considering the discount)

Order size	No. of orders	Total cost of procurement	Average stock	Total cost of storage of raw materials	Discount	Total cost
Kg.		(₹)	Kg.	(₹)	(₹)	(₹)
(1)	(2)	(3)=(2)×₹1,000	(4)=½×(1)	(5)=(4)×₹2	(6)	(7)=[(3)+(5)– (6)]
1,80,000	1	1,000	90,000	1,80,000	32,000	1,49,000
90,000	2	2,000	45,000	90,000	20,000	72,000
45,000	4	4,000	22,500	45,000	-	49,000
30,000	6	6,000	15,000	30,000	-	36,000

(iii) Number of orders which the company should place to minimize the costs after taking EOQ also into consideration is 14 orders. Total cost of procurement and storage in this case comes to ₹ 27,416 (please refer working note-4 above), which is minimum.

5. **(a)** In some process industries the output of one process is transferred to the next process not at cost but at market value or cost plus a percentage of profit. *The difference between cost and the transfer price is known as inter-process profits.*

The advantages and disadvantages of using inter-process profit, in the case of process type industries are as follows:

Advantages:

1. Comparison between the cost of output and its market price at the stage of completion is facilitated.
2. Each process is made to stand by itself as to the profitability.

Disadvantages:

1. The use of inter-process profits involves complication.

2. The system shows profits which are not realised because of stock not sold out

(b) Practical applications of Marginal costing:

(i) Pricing Policy: Since marginal cost per unit is constant from period to period, firm decisions on pricing policy can be taken particularly in short term.

(ii) Decision Making: Marginal costing helps the management in taking a number of business decisions like make or buy, discontinuance of a particular product, replacement of machines, etc.

(iii) Ascertaining Realistic Profit: Under the marginal costing technique, the stock of finished goods and work-in-progress are carried on marginal cost basis and the fixed expenses are written off to profit and loss account as period cost. This shows the true profit of the period.

(iv) Determination of production level: Marginal costing helps in the preparation of break-even analysis which shows the effect of increasing or decreasing production activity on the profitability of the company.

6. (i) Statement showing allocation of Joint Cost

Particulars	R_1	L_1
No. of units Produced	2,000	3,000
Selling Price Per unit (₹)	60	70
Sales Value (₹)	1,20,000	2,10,000
Less: Estimated Profit (R_1 -25% & L_1 -30%)	(30,000)	(63,000)
Cost of Sales	90,000	1,47,000
Less: Estimated Selling Expenses (R_1 -10% & L_1 -15%)	(12,000)	(31,500)
Cost of Production	78,000	1,15,500
Less: Cost after separation	(38,000)	(26,000)
Joint Cost allocated	40,000	89,500

(ii) Statement of Profitability

Particulars	G_1 (₹)	R_1 (₹)	L_1 (₹)
Sales Value (A)	6,00,000 (4,000 × ₹150)	1,20,000	2,10,000
Less: - Joint Cost	2,98,500	40,000	89,500

	(4,28,000 -40,000 - 89,500)		
- Cost after separation	-	38,000	26,000
- Selling Expenses (G1- 20%, R1-10% & L1-15%)	1,20,000	12,000	31,500
(B)	4,18,500	90,000	1,47,000
Profit (A –B)	1,81,500	30,000	63,000
Overall Profit = ₹1,81,500 + ₹30,000 + ₹63,000 = ₹ 2,74,500			

7. **(a)** ***Time and motions study:*** It is the study of time taken and motions (movements) performed by workers while performing their jobs at the place of their work. Time and motion study has played a significant role in controlling and reducing labour cost.

Time Study is concerned with the determination of standard time required by a person of average ability to perform a job. Motion study, on the other hand, is concerned with determining the proper method of performing a job so that there are no wasteful movements, hiring the worker unnecessarily. However, both the studies are conducted simultaneously. Since materials, tools, equipment and general arrangement of work, all have vital bearing on the method and time required for its completion. Therefore, their study would be incomplete and would not yield its full benefit without a proper consideration of these factors.

Time and motion study is important to management because of the following features*:*

1. Improved methods, layout, and design of work ensure effective use of men, material and resources.
2. Unnecessary and wasteful methods are pin-pointed with a view to either improving them or eliminating them altogether. This leads to reduction in the work content of an operation, economy in human efforts and reduction of fatigue.
3. Highest possible level of efficiency is achieved in all respect.
4. Provides information for setting labour standards - a step towards labour cost control and cost reduction.
5. Useful for fixing wage rates and introducing effective incentive scheme.

(b) *Explicit costs:* These costs are also known as out of pocket costs. They refer to those costs which involves immediate payment of cash. Salaries, wages, postage and telegram, interest on loan etc. are some examples of explicit costs because they involve immediate cash payment. These payments are recorded in the books of account and can be easily measured.

Main points of difference: The following are the main points of difference between Explicit and Implicit costs.

(i) Implicit costs do not involve any immediate cash payment. As such they are also known as imputed costs or economic costs.

(ii) Implicit costs are not recorded in the books of account but yet, they are important for certain types of managerial decisions such as equipment replacement and relative profitability of two alternative courses of action.

Test Series: October, 2014

MOCK TEST – 2

INTERMEDIATE (IPC) – GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – II : FINANCIAL MANAGEMENT

SUGGESTED ANSWERS/HINTS

1. (a) (i) **Computation of Internal Rate of Return**

$995 \times (1+i)^5 = 1,200.$

$$(1+i)^5 = \frac{1,200}{995}$$

Taking 5th root of both sides:

$(1+i) = 1.0382$

Internal rate of return i.e. i = 0.0382 = 3.82%

In order to make a choice, you need to know what interest rate is being offered by the local bank.

(ii) **Advice**: If the bank is paying 3.5%, Mr. Raman should choose the bond because it is earning a higher rate of return i.e. 3.82%.

(iii) **Advice**: If the bank is paying 5% per year, Mr. Raman should deposit his money in the bank. He would earn a higher rate of return.

If the price of the bond was Rs. 900, its IRR would be as following:

$900 \times (1+i)^5 = 1,200.$

$$(1+i)^5 = \frac{1,200}{900}$$

Internal rate of return i.e. i =5.92%

Since the internal rate of return i.e. 5.92% is higher than the bank rate i.e. 5%; hence, Mr. Raman should choose to buy the bond.

(b) Present Value of Investment

$$PV = \frac{\text{Rs. } 50,00,000}{0.10} = \text{Rs. } 5,00,00,000$$

Highest price you would be willing to pay = Rs. 5,00,00,000.

2. (a)

Particulars	Par	Premium	Discount
Gross Proceeds	10,000×100 =10,00,000	10,000×110 =11,00,000	10,000×90 = 9,00,000
Less : Cost of Issue	25,000	25,000	25,000
Net Proceeds	**9,75,000**	**10,75,000**	**8,75,000**
Interest at 10%	1,00,000	1,00,000	1,00,000
Less : Tax at 35%	35,000	35,000	35,000
Net Outflow	**65,000**	**65,000**	**65,000**
Kd=Interest (after tax)/Net Proceeds	**6.67%**	**6.05%**	**7.43%**

(b)

Firm		A	B	C	D
	EBIT	2,00,000	3,00,000	5,00,000	6,00,000
Less:	Interest	20,000	60,000	2,00,000	2,40,000
	EBT = Net Income	**1,80,000**	**2,40,000**	**3,00,000**	**3,60,000**
K e	(given)	12%	16%	15%	18%
Value of Equity (E)=Net Income ÷Ke		15,00,000	15,00,000	20,00,000	20,00,000
Value of Debt (D)=Interest ÷ Kd of 10%		2,00,000	6,00,000	20,00,000	24,00,000
Value of Firm (V) = (E+D)		17,00,000	21,00,000	40,00,000	44,00,000
K_0	= WACC = EBIT÷V	**11.76%**	**14.29%**	**12.5%**	**13.64%**

3. (a) (A) **Schedule of Changes in Working Capital**

Particulars	*31.3.2013*	*31.3.2014*	*Effect on Working Capital*	
			Increase	*Decrease*
	Rs.	*Rs.*	*Rs.*	*Rs.*
Current Assets:				
Stock	3,60,000	3,50,000	-	10,000
Debtors	3,00,000	3,90,000	90,000	-
Cash and Bank	1,00,000	95,000	-	5,000
Prepaid Expenses	15,000	20,000	5,000	-
Total (A)	7,75,000	8,55,000		

Current Liabilities:				
Creditors	2,05,000	3,00,000	-	95,000
Bills Payable	45,000	81,000	-	36,000
Total (B)	2,50,000	3,81,000		
Net Working Capital (A-B)	5,25,000	4,74,000	-	
Net Decrease in Working Capital	-	51,000	51,000	-
	5,25,000	5,25,000	1,46,000	1,46,000

(B) Funds Flow Statement for the year ended 31st March, 2014

	Rs.
Sources of Fund	
Funds from Operation	7,49,000
Issue of 9% Preference Shares	5,00,000
Sales of Plant & Machinery	32,000
Refund of Income Tax	4,000
Financial Resources Provided (A)	12,85,000
Applications of Fund	
Purchase of Land and Building	1,50,000
Purchase of Plant and Machinery	3,60,000
Redemption of Debentures	2,06,000
Redemption of Preference Shares	3,15,000
Payment of Tax	1,05,000
Payment of Interim Dividend	50,000
Payment of Dividend (2012-13)	1,50,000
Financial Resources Applied (B)	13,36,000
Net Decrease in Working Capital (A - B)	51,000

Working Notes:

Estimation of Funds from Operation		*Rs.*
Profit and Loss A/c Balance on 31.3.2014		3,00,000
Add: Depreciation on Land and Building	50,000	
Depreciation on Plant and Machinery	1,20,000	
Loss on Sale of Plant and Machinery (40,000 – 32,000)	8,000	

Preliminary Expenses written off	(40,000 – 35,000)	5,000	
Transfer to General Reserve		50,000	
Proposed Dividend		2,60,000	
Provision for Taxation		1,06,000	
Interim Dividend paid		50,000	
			6,49,000
			9,49,000
Less: Profit and Loss A/c balance on 31.3.13			2,00,000
Funds from Operation			7,49,000

Plant & Machinery A/c

	Rs.		*Rs.*
To Balance b/d	9,00,000	By Depreciation	1,20,000
To Bank [Purchase (Bal. Fig.)]	3,60,000	By Bank (Sale)	32,000
		By P/L A/c (Loss on Sale)	8,000
		By Balance c/d	11,00,000
	12,60,000		12,60,000

Provision for Taxation A/c

	Rs.		*Rs.*
To Advance tax payment A/c	76,000	By Balance b/d	70,000
To Balance c/d	1,00,000	By P/L A/c (additional provision for 2012-13)	6,000
		By P/L A/c (Provision for 13-14)	1,00,000
	1,76,000		1,76,000

Advance Tax Payment A/c

	Rs.		*Rs.*
To Balance b/d	80,000	By Provision for taxation A/c	76,000
To Bank (paid for 13-14)	1,05,000	By Bank (Refund of tax)	4,000
		By Balance c/d	1,05,000
	1,85000		1,85,000

8% Debentures A/c

	Rs.		Rs.
To Bank (2,00,000 x 103%) (redemption)	2,06,000	By Balance b/d	3,00,000
		By Premium on redemption	
To Balance c/d	1,00,000	of Debentures A/c	6,000
	3,06,000		3,06,000

9% Preference Share Capital A/c

	Rs.		Rs.
To Bank A/c (3,00,000 x 105%) (redemption)	3,15,000	By Balance b/d	3,00,000
		By Premium on redemption	
To Balance c/d	5,00,000	of Preference shares A/c	15,000
		By Bank (Issue)	5,00,000
	8,15,000		8,15,000

Securities Premium A/c

	Rs.		Rs.
To Premium on redemption of debentures A/c	6,000	By Balance b/d	25,000
To Premium on redemption of preference shares A/c	15,000		
To Balance c/d	4,000		
	25,000		25,000

General Reserve A/c

	Rs.		Rs.
To Bonus to Shareholders A/c	2,00,000	By Balance b/d	3,50,000
To Balance c/d	2,00,000	By P/L A/c (transfer) b/f	50,000
	4,00,000		4,00,000

Land and Building A/c

	Rs.		Rs.
To Balance b/d	6,00,000	By Depreciation	50,000
To Bank (Purchase) (Bal. Fig.)	1,50,000	By Balance c/d	7,00,000
	7,50,000		7,50,000

(b) **Activity level: 1,30,000 units**

Statement showing Estimate of Working Capital Needs

A.	Investment in Inventory:		
	Raw material inventory: 1 month		
	$\left(1{,}30{,}000 \times \frac{4}{52} \times ₹\ 100\right)^{*}$		10,00,000
	WIP Inventory : 1 week $\left(1{,}30{,}000 \times \frac{1}{52} \times 0.80 \times 212.50\right)$		4,25,000
	Finished goods inventory: 2 weeks		
	$\left(1{,}30{,}000 \times \frac{2}{52} \times 212.50\right)$		10,62,500
B.	Investment in Debtors: 4 weeks at cost		
	$\left(1{,}30{,}000 \times \frac{4}{5} \times \frac{4}{52} \times 212.50\right)$		17,00,000
C.	Cash balance		37,500
D.	Investment in Current Assets (A + B + C)		42,25,000
E.	Current Liabilities:		
	Creditors : 3 weeks		
	$\left(1{,}30{,}000 \times \frac{3}{52} \times 100\right)$	7,50,000	
	Deferred wages : 1 week		
	$\left(1{,}30{,}000 \times \frac{1}{52} \times 37.50\right)$	93,750	
	Deferred overheads : 2 weeks		
	$\left(1{,}30{,}000 \times \frac{2}{52} \times 75\right)$	3,75,000	12,18,750
	Net Working Capital Needs		30,06,250

4. (a) Calculation of Debt Service Coverage Ratio (DSCR) and its Significance

The debt service coverage ratio can be calculated as under:

$$\text{Debt Service Coverage Ratio} = \frac{\text{Earnings available for debt service}}{\text{Interest} + \text{Installments}}$$

Debt service coverage ratio indicates the capacity of a firm to service a particular level of debt. High credit rating firms target DSCR to be greater than 2 in its entire loan life. High DSCR facilitates the firm to borrow at the most competitive rates.

(b) Conflict in Profit versus Wealth Maximization Objective

The company may pursue profit maximisation goal but that may not result into creation of shareholder value. However, profit maximisation cannot be the sole objective of a company. It is at best a limited objective. If profit is given undue importance, a number of problems can arise like the term profit is vague, profit maximisation has to be attempted with a realisation of risks involved, it does not take into account the time pattern of returns and as an objective it is too narrow.

Whereas, on the other hand, wealth maximisation, as an objective, means that the company is using its resources in a good manner. If the share value is to stay high, the company has to reduce its costs and use the resources properly. If the company follows the goal of wealth maximisation, it means that the company will promote only those policies that will lead to an efficient allocation of resources.

Test Series: September, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 4: TAXATION

Time Allowed – 3 Hours **Maximum Marks – 100**

1. (a) Compute the taxable income and tax liability of Mrs. Sudha Sharma for the A.Y. 2014-15 from the following detail:

   (i) Smt. Sudha Sharma was born on 01.07.1950. She is a Deputy Manager in a Company in Mumbai. She is getting a monthly salary and D.A. of Rs.45,000 and Rs. 12,000 respectively. 50% of DA forms part of pay. She also gets a House Rent Allowance of Rs. 6,000 per month. She is a member of Recognised P.F. wherein she contributes 15% of her salary of Rs. 51,000 p.m. (45,000 + 6,000, being 50% of DA). Her employer also contributes an equal amount.

   (ii) She is living in the house of her minor son in Mumbai.

   (iii) During the previous year 2013-14, her minor son has earned an income of Rs. 30,000 (computed) as rent from a House Property, which had been transferred to him by Smt. Sudha Sharma without consideration a few years back.

   (iv) During the previous year 2013-14, she sold Government of India Capital Indexed Bonds for Rs. 1,50,000 on 30.09.2013, which she purchased on 01.07.2001 for Rs. 80,000 (Cost inflation index – F.Y. 2001-2002: 426 and for the F.Y. 2013-14: 939).

   (v) Her employer gave her an interest free loan of Rs. 1,50,000 on 01.10.2013 to one of her son's wife for the purchase of an Alto Maruti Car. Nothing has been repaid to the company towards the loan. The lending rate on SBI for a similar loan is 8% p.a as on 01.04.2013.

   (vi) During the previous year 2013-14 she paid Rs. 15,000 by cheque to GIC towards Medical Insurance Premium of her dependent mother. *(10 Marks)*

   (b) Star Professionals Ltd. is engaged in providing services which became taxable with effect from August 01, 2013. Compute the service tax payable by Star Professionals Ltd. on the following amounts (inclusive of service tax wherever applicable) received in the month of March, 2014:-

Particulars	**Amount (Rs.)**
Services performed in July, 2013 (Amount received from the client is full and final)	5,00,000

Services by way of renting of residential dwelling for use as residence	1,75,000
Free services rendered to the friends (Value of similar services is Rs. 60,000)	
Services rendered to its associated enterprise in UK for which no invoice has been issued	5,00,000
Other receipts	7,00,000

(10 Marks)

2. (a) Mr. Mahesh purchased a house property on 14th April, 1979 for Rs. 1,05,000. He entered into an agreement with Mr. Sonu for the sale of house on 15th September, 1982 and received an advance of Rs. 25,000. However, since Mr. Sonu did not remit the balance amount, Mr. Mahesh forfeited the advance.

Later on, he gifted the house property to his friend Mr. Suresh on 15th June, 1986.

Following renovations were carried out by Mr. Mahesh and Mr. Suresh to the house property:

	Rs.
By Mr. Mahesh during F.Y. 1979-80	10,000
By Mr. Mahesh during F.Y. 1983-84	50,000
By Mr. Suresh during F.Y. 1993-94	1,90,000

The fair market value of the property as on 1.4.1981 is Rs. 1,50,000.

Mr. Suresh entered into an agreement with Mr. Pintu for sale of the house on 1st June, 1995 and received an advance of Rs. 80,000. The said amount was forfeited by Mr. Suresh, since Mr. Pintu could not fulfil the terms of the agreement.

Finally, the house was sold by Mr. Suresh to Mr. Rajeev on 2nd January, 2014 for a consideration of Rs. 12,00,000.

Compute the capital gains chargeable to tax in the hands of Mr. Suresh for the assessment year 2014-15. Cost inflation indices are as under:

Financial Year	**Cost inflation index**
1981-82	100
1983-84	116
1986-87	140
1993-94	244
2013-14	939

(8 Marks)

(b) Determine net VAT liability of Mr. Mehta for the month of January, 2014 using invoice method of computation from the following data:

Purchase price of goods acquired from local market (including VAT)	Rs. 52 lakhs
VAT rate on input	4%
Transportation, insurance, warehousing and handling cost incurred by X	Rs. 30,000
Goods sold at a profit margin (% of cost of production)	15%
VAT rate on sales	12.50%

(4 Marks)

(c) Mr. Sumit Arora is a service tax assessee. His service tax liability for the quarter April - June was Rs. 35,000. However, on account of a clerical error, he paid Rs. 3,50,000 as service tax for the said quarter. Now Mr. Sumit Arora wants to adjust the excess payment of Rs. 3,15,000 against his service tax liability for the succeeding quarter. Can he do so? What is the condition to be satisfied for it?

(4 Marks)

3. (a) Mr. Bhimsen is engaged in composite business of growing and curing (further processing) coffee in Munnar, Kerala. The whole of coffee grown in his plantation is cured. Relevant information pertaining to the year ended 31.3.2014 are given below:

Particulars	Rs.
WDV of car as on 1.4.2013	4,50,000
WDV of machinery as on 1.4.2013 (15% rate)	17,50,000
Expenses incurred for growing coffee	4,20,000
Expenditure for curing coffee	3,10,000
Sale value of cured coffee	29,00,000

Besides being used for agricultural operations, the car is also used for personal use; disallowance for personal use may be taken at 25%. The expenses incurred for car running and maintenance are Rs. 60,000. The machines were used in coffee curing business operations.

Compute the income arising from the above activities for the assessment year 2014-15. Show the WDV of the assets as on 31.3.2014. *(8 Marks)*

(b) Mr. X is an air travel agent, who discharges his service tax liability at special rates provided under the Service Tax Rules, 1994. Compute his service tax liability for the quarter October – December, 2013 with the help of following particulars furnished by him:

Particulars	Basic fare as per rule 6(7) of Service Tax Rules, 1994 (Rs.)	Other charges and fee (Rs.)	Taxes (Rs.)	Total
Domestic Bookings	1,00,900	8,420	3,960	1,13,280
International Bookings	3,16,880	22,110	13,890	3,52,880

Mr. X wants to pay service tax at the general rate of 12% in respect of bookings done by him during the quarter January – March, 2014. Can he do so? Explain.

(8 Marks)

4. (a) Gayatri holding 32% of equity shares in a company, took a loan of Rs. 6,00,000 from the same company. On the date of granting the loan, the company had accumulated profit of Rs. 4,50,000. The company is engaged in some manufacturing activity.

(i) Is the amount of loan taxable as deemed dividend in the hands of Gayatri, if the company is a company in which the public are substantially interested?

(ii) What would be your answer, if the lending company is a private limited company (i.e. a company in which the public are not substantially interested)?

(4 Marks)

(b) M/s. Cool and Calm, a sole proprietary concern, was converted into a company on 21.8.2013. Before the conversion, the sole proprietary concern had a Block of Plant and Machinery (Rate of depreciation 15%), whose WDV as on 1.4.2013 was Rs. 5,00,000. On 1st April itself, a new plant of the same block was purchased for Rs. 1,50,000. After the conversion, the company has purchased the same type of Plant on 30.12.2013 for Rs. 1,80,000.

Compute the depreciation that would be allocated between the sole proprietary concern and the successor company. *(4 Marks)*

(c) Golden Export House exported some goods to Newyork. Compute the export duty payable by it from the following information available:

(i) Assessable value Rs. 60,00,000.

(ii) Shipping bill presented electronically on 18.02.2014.

(iii) Proper officer passed order permitting clearance and loading of goods for export on 10.03.2014.

(iv) Rate of export duty are as under:

	Rate of export duty
On 18.02.2014	10%
On 10.03.2014	8%

(4 Marks)

(d) Compute the CENVAT credit available in respect of the following services billed to Shri Brijmohan Services Ltd. in the month of February, 2014:-

S.No.	Services billed	Service tax paid* [Rs.]
(i)	Accounting and auditing services	12,00,000
(ii)	Legal services	4,00,000
(iii)	Security services	40,000
(iv)	Hiring of motor vehicles (Such motor vehicles are not eligible as capital goods for the purposes of claiming CENVAT credit)	2,00,000

*including EC and SHEC *(4 Marks)*

5. (a) Mr. Dhruv and his wife Mrs. Diya furnish the following information:

Sl. No.	Particulars	Rs.
(i)	Salary income (computed) of Mrs. Diya	4,60,000
(ii)	Income of minor son 'B' who suffers from disability specified in Section 80U	1,08,000
(iii)	Income of minor daughter 'C' from singing	86,000
(iv)	Income from profession of Mr. Dhruv	7,50,000
(v)	Cash gift received by 'C' on 2.10.2013 from friend of Mrs. Diya on winning of singing competition	48,000
(vi)	Income of minor married daughter 'A' from company deposit	30,000

Compute the total income of Mr. Dhruv and Mrs. Diya for the Assessment Year 2014-15. *(5 Marks)*

(b) Cheeku is in possession of agricultural land situated within urban limits, which is used for agricultural purposes during the preceeding 3 years by his father. On 1.5.2013, this land is compulsorily acquired by the Central Government of India on a compensation fixed and paid by it for Rs. 25 lakhs. Advise Cheeku as to the tax consequences, assuming that the entire amount is invested in purchase of shares.

(3 Marks)

(c) Rahman Services Ltd. started providing services with effect from 01.04.2013. It rendered services to ABC Ltd. on 16.10.2013 for which payment was received on 21.10.2013. With effect from 02.11.2013, the said services became taxable. On 13.11.2013, Rahman Services Ltd. raised the invoice on ABC Ltd. You are required to examine whether service tax is payable on the said services.

Will your answer be different if Rahman Services Ltd. raised the invoice on ABC Ltd. on 16.11.2013? *(5 Marks)*

(d) A manufacturer cleared some goods by charging excise duty. The invoice provided the following details:

	Rs.
Price	20,000
Excise duty @ 10.30%	2,060
Total	22,060

However, he came to know later that actual rate of excise duty is 12.36%. How much differential duty is payable by him, if he is not able to recover any extra amount from the customer? *(3 Marks)*

6. (a) Mr. Ram Bharose, a resident individual aged 64, is a partner in Musical Ears & Co., a partnership firm. He also runs a wholesale business in medical products. The following details are made available for the year ended 31.3.2014:

Sl. No.	**Particulars**	**Rs.**	**Rs.**
(i)	Interest on capital received from Musicals Ears & Co., at 18%		1,80,000
(ii)	Interest from bank on fixed deposit (Net of TDS Rs. 2,500)		22,500
(iii)	Income-tax refund received relating to assessment year 2012-13 including interest of Rs. 2,450		36,500
(iv)	Net profit from wholesale business		7,20,000
	Amounts debited include the following:		
	Depreciation as per books	45,000	
	Motor car expenses	55,000	
	Municipal taxes for the shop (For two half years; payment for one half year made on 12.4.2014 and for the other on 20.11.2014)	8,500	
	Salary to manager by way of a single cash payment	32,000	

(v)	The WDV of the assets (as on 1.4.2013) used in above wholesale business is as under:		
	- Computers	2,10,000	
	- Motor car (20% used for personal use)	3,80,000	
(vi)	LIP paid for major son	75,000	
	PPF of his wife	85,000	
	Interest on loan taken for higher education of daughter	55,000	

Compute the total income of the assessee for the assessment year 2014-15. The computation should show the proper heads of income. Also compute the WDV of the different blocks of assets as on 31.3.2014. *(8 Marks)*

(b) Shubh Ltd. exported some goods to Riddhi Inc. of USA. It received US $ 8,000 as consideration for the same and sold the foreign currency @ Rs. 62 per US dollar. Compute the value of taxable service under rule 2B of the Service Tax (Determination of Value) Rules, 2006 in the following cases:-

(i) RBI reference rate for US dollar at that time is Rs. 63 per US dollar.

(ii) RBI reference rate for US dollars is not available.

What would be the value of taxable service if US $ 8,000 are converted into UK £ 4,000. RBI reference rate at that time for US $ is Rs. 64 per US dollar and for UK £ is Rs. 102 per UK Pound. *(8 Marks)*

7. (a) Will a charitable trust be forfeited of tax exemption granted to it, if it holds shares in Public Sector Company? Will a charitable trust having business receipt and income of Rs. 20,00,000 and Rs. 2,00,000, respectively, be denied the tax exemption?

(4 Marks)

(b) Miss Vinita paid a sum of 8,500 USD to Mr. Shekhar, a management consultant practising in Macau, specializing in project financing. The payment was made in Macau. Mr. Shekhar is a non-resident. The consultancy is related to a project in India with possible Korean collaboration. Is this payment chargeable to tax in India in the hands of Mr. Shekhar, since the services were used in India? *(4 Marks)*

(c) Examine whether following amount to inter-State sales:-

(i) P of Chandigarh sends goods by air to his branch office at Australia. Subsequently, he transfers the documents of title of such goods to a buyer at Scotland after said goods have crossed the customs frontiers of India.

(ii) A London based entrepreneur enters into a contract of sale of goods with Manoj of Rajasthan and sends the goods to India. *(4 Marks)*

(d) Y is a consulting engineer. He has obtained service tax registration on May 4, 2013. Y has entered into a contract with Z for provision of consulting services on May 5, 2013. Y provides the services on May 15, 2013 but Z has communicated that he will be able to pay the consideration only after three months owing to his poor financial condition.

Y has not issued any invoice or bill for the said service as he is not sure of the requirements of an invoice issued by a registered service tax provider. You are required to guide Y with regard to content and time of issuance of an invoice. *(4 Marks)*

MOCK TEST – 2

INTERMEDIATE (IPC) – GROUP – I

PAPER – 4: TAXATION

SUGGESTED ANSWERS/HINTS

1. (a) **Computation of total income of Mr. Mahendra for the A. Y. 2014-15**

Particulars	Rs.	Rs.
Income from business of plying goods vehicle (Refer Note 1)		4,50,000
Less: Brought forward business loss of financial year 2012-13 (Refer Note 2 & 3)		1,00,000
Gross Total Income		**3,50,000**
Less: **Deduction under Chapter VI-A**		
Section 80C:-		
Life insurance premium paid for insurance of married daughter (Refer Note 5)	20,000	
Section 80D:-		
Medical insurance premium paid for insurance of parents (Refer Note 6)	20,000	
Section 80E:-		
Interest paid towards education loan taken for studies of his daughter (Refer Note 7)	15,000	55,000
Total Income		**2,95,000**

Working Notes:

(1) Computation of income from business of plying goods vehicles under section 44AE.

Particulars	Rs.
6 heavy goods vehicle held throughout the year (Rs. 5,000×6×12)	3,60,000
2 heavy goods vehicle – held for 9 months (Rs. 5,000×2×9)	90,000
Income under section 44AE	4,50,000

(2) As per section 44AE, any deduction allowable under the provisions of sections 30 to 38 shall be deemed to have been already allowed. Therefore, the unabsorbed depreciation of Rs. 70,000 shall not be allowed as a deduction since it is covered by section 32.

(3) Brought forward business loss of Rs. 1,00,000 shall be allowed as deduction, by virtue of section 72, as it is allowed to be carried forward for 8 assessment years following the assessment year to which it relates, since the return for A.Y. 2013-14 was filed before the due date specified under section 139(1).

(4) Fixed deposit in the name of married son does not qualify for deduction under section 80C.

(5) Premium paid for insurance on the life of any child of the individual, whether married or not, qualifies for deduction under section 80C. In respect of policies issued on or after 1.04.2012, only premium paid to the extent of 10% of "minimum capital sum assured" qualifies for deduction under section 80C. Therefore, out of the life insurance premium of Rs. 25,000 paid for insurance policy of married daughter, only Rs. 20,000 (being 10% of Rs. 2,00,000) is allowed as deduction under section 80C.

(6) Deduction is allowed under section 80D for payment made for medical insurance of parents. Medical insurance premium paid for insuring the health of a person who is a senior citizen i.e. of age 60 years or more, qualifies for deduction under section 80D, subject to a maximum of Rs. 20,000. Hence, deduction of Rs. 20,000 is provided to Mr. Mahendra, as his parents are senior citizens.

(7) It is only the payment of interest on education loan which qualifies for deduction under section 80E. Deduction under section 80E is allowed in respect of interest on loan taken for education of children of the individual even if they are not dependent. Principal repayment of the education loan is not eligible for deduction under section 80E.

(b) Computation of value of taxable service and service tax liability of Amiro Bank Ltd.

Particulars	**Amount (Rs.)**
Interest on overdraft (Note-1)	Nil
Interest on loans with a collateral security (Note-1)	Nil
Interest on corporate deposits (Note-1)	Nil
Administrative charges (over and above interest) on loans, advances and deposits (Note-2)	6,00,000
Sale of foreign exchange to general public (Note-3)	15,00,000
Service charges relating to issuance of CD (Note-4)	20,00,000
Value of taxable service	41,00,000
Service tax @ 12% [Rs. 41,00,000×12%]	4,92,000
Education cess @ 2% [Rs. 4,92,000×2%]	9,840

Secondary and higher education cess @ 1% [Rs. 4,92,000×1%]	4,920
Service tax liability	5,06,760

Notes:

1. Following services provided are included in the negative list so far as the consideration is represented by way of interest and hence are not taxable:-
   - Overdraft facility.
   - Loans with a collateral security.
   - Corporate deposits.
2. Administrative charges or amounts collected over and above the interest or discount amounts would not be part of the negative list and thus would represent taxable consideration.
3. Services by way of sale of foreign exchange between banks or by banks to authorized dealers of foreign exchange is included in the negative list. However, services provided by banks by way of sale of foreign exchange to general public is not so covered and hence taxable.
4. Since CDs are in the nature of promissory notes, transactions in CDs shall be considered as transaction in money. However, a related activity, for which a separate consideration is charged would not be treated as a transaction of money and would be taxable. Hence, service charges relating to issuance of CDs shall be chargeable to service tax.

2. (a) Computation of total income of Mr. Arun, Mrs. Arun and their minor son for the A.Y. 2014-15

Particulars	Mr. Arun (Rs.)		Mrs. Arun (Rs.)	Minor Son (Rs.)
Salary income (of Mrs. Arun)		-	2,40,000	-
Pension income (of Mr. Arun) (Rs. 10,000×12)		1,20,000		
Income from House Property ***[See Note (3) below)***		52,000	-	-
Income from other sources				
Interest on Mr. Arun's fixed deposit with Bank of India (Rs. 5,00,000×9%) ***[See Note (1) below]***	45,000		-	-
Commission received by Mrs. Arun from a partnership firm, in which Mr. Arun has substantial interest ***[See Note (2) below]***	25,000	70,000	-	-

Income before including income of minor son under section 64(1A)		**2,42,000**	**2,40,000**	**-**
Income of the minor son from the investment made in the business out of the amount gifted by Mr. Arun ***[See Note (4) below]***		18,500	-	-
Income of the minor son through a business activity involving application of his skill and talent ***[See Note (5) below]***		-	-	20,000
Total Income		**2,60,500**	**2,40,000**	**20,000**

Notes:

(1) As per section 60, in case there is a transfer of income without transfer of asset from which such income is derived, such income shall be treated as income of the transferor. Therefore, the fixed deposit interest of Rs. 45,000 transferred by Mr. Arun to Mr. Bhola shall be included in the total income of Mr. Arun.

(2) As per section 64(1)(ii), in case the spouse of the individual receives any amount by way of income from any concern in which the individual has substantial interest (i.e. holding shares carrying at least 20% voting power or entitled to at least 20% of the profits of the concern), then, such income shall be included in the total income of the individual. The only exception is in a case where the spouse possesses any technical or professional qualifications and the income earned is solely attributable to the application of her technical or professional knowledge and experience, in which case, the clubbing provisions would not apply.

In this case, the commission income of Rs. 25,000 received by Mrs. Arun from the partnership firm has to be included in the total income of Mr. Arun, as Mrs. Arun does not possess any technical or professional qualification for earning such commission and Mr. Arun has substantial interest in the partnership firm as he holds 75% share in the firm.

(3) According to section 27(i), an individual who transfers any house property to his or her spouse otherwise than for adequate consideration or in connection with an agreement to live apart, shall be deemed to be the owner of the house property so transferred. Hence, Mr. Arun shall be deemed to be the owner of the flat gifted to Mrs. Arun and hence, the income arising from the same shall be computed in the hands of Mr. Arun.

Note:

(i) It has been assumed that the net income from the flat i.e., Rs. 52,000 given in the question is the net income computed under the head "Income from house property".

Note: Alternatively, the net income from the flat i.e., Rs. 52,000 given in the question may be taken as the net income before providing for deduction @ 30% under section 24(a) and accordingly, the solution can be worked out on this basis.

(ii) The provisions of section 56(2)(vii) would not be attracted in the hands of Mrs. Arun, since she has received immovable property without consideration from a relative i.e., her husband.

(4) As per section 64(1A), the income of the minor child is to be included in the total income of the parent whose total income (excluding the income of minor child to be so clubbed) is greater. Further, as per section 10(32), income of a minor child which is includible in the income of the parent shall be exempt to the extent of Rs. 1,500 per child.

Therefore, the income of Rs. 20,000 received by minor son from the investment made out of the sum gifted by Mr. Arun shall, after providing for exemption of Rs. 1,500 under section 10(32), be included in the income of Mr. Arun, since Mr. Arun's income of Rs. 2,42,000 (before including the income of the minor child) is greater than Mrs. Arun's income of Rs. 2,40,000. Therefore, Rs. 18,500 (i.e., Rs. 20,000 – Rs. 1,500) shall be included in Mr. Arun's income. It is assumed that this is the first year in which clubbing provisions are attracted.

Note *– The provisions of section 56(2)(vii) would not be attracted in the hands of the minor son, since he has received a sum of money exceeding Rs. 50,000 without consideration from a relative i.e., his father.*

(5) In case the income earned by the minor child is on account of any activity involving application of any skill or talent, then, such income of the minor child shall not be included in the income of the parent, but shall be taxable in the hands of the minor child.

Therefore, the income of Rs. 20,000 derived by Mr. Arun's minor son through a business activity involving application of his skill and talent shall not be clubbed in the hands of the parent. Such income shall be taxable in the hands of the minor son.

(b) Computation of Net VAT payable by M/s. AB Ltd. for the month of July, 2014

	Particulars	Rs.
(A)	**Output VAT payable**	
	(i) On sale of finished goods produced from Goods 'X'	62,500

	within Mumbai (Rs. 5,00,000 × 12.5%)	
	(ii) On sale of finished goods produced from Goods 'Z' within Mumbai (Rs. 40,00,000 × 4 %)	1,60,000
	Total (A)	2,22,500
(B)	**Input tax credit available**	
	(i) Goods 'X' (Exempt)	Nil
	(ii) Goods 'Y' (Note-2)	Nil
	(iii) Goods 'Z' transferred to branch (Rs. 5,00,000×10.5%) (Note-3)	52,500
	(iv) Remaining Goods 'Z' after transfer to the branch [Rs. (35,00,000- 5,00,000)×12.5%]	3,75,000
	Total (B)	4,27,500
	Net VAT payable = (A)-(B)	(2,05,000)
	CST payable (Rs. 6,00,000 × 2% = Rs. 12,000) on inter-state sale of goods produced from Goods 'X' adjusted (Note-4)	12,000
	Excess input tax credit carried forward to next month	**1,93,000**

Notes:

1. It is assumed that there is no opening and closing inventory. Hence, entire purchases of the raw materials have been used to manufacture the respective finished goods.
2. Goods utilized in the manufacture of exempted goods are not eligible for input tax credit. Hence, no input tax credit is available in respect of VAT paid on purchase of Goods 'Y' as they have been used to produce goods which are exempt from VAT.
3. In case of stock transfer, input tax paid in excess of 2% can be claimed as input tax credit.
4. Input tax credit can be used to set off the central sales tax payable on the inter-state sales.

3. (a) Computation of total income of Smita for the A.Y. 2014-15

Particulars	Rs.	Rs.
Profit of business of consumer and house-hold products	50,000	
Less: Loss of business of readymade garments for the year adjusted under section 70(1)	10,000	
	40,000	
Less: Brought forward loss of catering business closed in A.Y. 2013- 14 set off against business income for the		

current year as per section 72(1)	15,000	25,000
Profit of speculative transaction		12,500
Total Income		**37,500**

Notes:

1. Loss of speculative transaction of A.Y. 2009-10 is not allowed to be set off against the profit of speculative transaction of the A.Y.2014-15, since, as per the provisions of section 73(4), such loss can be carried forward for set-off for a maximum period of 4 years only i.e. up to A.Y.2013-14.
2. Short term capital loss of Rs. 15,000 on sale of securities and shares has to be carried forward as per section 74 since there is no income under the head Capital Gains for the A.Y.2014-15. The loss is to be carried forward for set off in future years against income chargeable under the head Capital Gains. Such loss can be carried forward for a maximum period of 8 assessment years.

(b) **(i)** Since the rent paid for hire of machinery by Bridgestone. Ltd. to Mr. Raghav exceeds Rs. 1,80,000, the provisions of section 194-I for deduction of tax at source are attracted.

The rate applicable for deduction of tax at source under section 194-I on rent paid for hire of plant and machinery is 2% assuming that Mr. Raghav had furnished his permanent account number to Bridgestone Ltd.

Therefore, the amount of tax to be deducted at source:

= Rs. 2,10,000 x 2% = Rs. 4200.

Note: In case Mr. Raghav does not furnish his permanent account number to Bridgestone Ltd., tax shall be deducted @ 20% on Rs. 2,10,000, by virtue of provisions of section 206AA.

(ii) As per the provisions of section 194J, a Hindu Undivided Family is required to deduct tax at source on fees paid for professional services only if it is subject to tax audit under section 44AB in the financial year preceding the current financial year.

However, if such payment made for professional services is exclusively for the personal purpose of any member of Hindu Undivided Family, then, the liability to deduct tax is not attracted.

Therefore, in the given case, even if Sharma (HUF) is liable to tax audit in the immediately preceding financial year, the liability to deduct tax at source is not attracted in this case since, the fees for professional service to Dr. K.P. Singh is paid for a personal purpose i.e. the surgery of a member of the family.

(c) **(i)** In case of renting of motor vehicles, abatement of 60% from gross amount charged is available if CENVAT credit on inputs, capital goods and input services is not availed. Therefore, since in the given case, Mr. Y avails CENVAT credit on inputs, capital goods and input services, it cannot pay service tax on abated value.

In case of taxable services provided by way of renting of a motor vehicle designed to carry passengers on **non abated** value to any person who is not engaged in the similar line of business by any individual/HUF/partnership firm (whether registered or not) including association of persons, located in the taxable territory to a business entity registered as body corporate, located in the taxable territory, both service provider and service receiver are liable to pay service tax. 60% of tax is to be paid by service provider and 40% by service receiver.

Since in the given case, service by way of renting of motor vehicle is provided by an individual (Mr. Y) to another individual (Mr. X) and not to any body corporate, reverse charge provisions will not apply and entire service tax will be payable by service provider (Mr. Y). Thus, service tax of Rs. 309 (12.36% of Rs. 2,500) is liable to be paid by Mr. Y.

However, when motor vehicle is taken on rent by ABC Ltd. (a company), reverse charge provisions will apply and 60% of tax will be paid by Mr. Y (service provider) and 40% by ABC Ltd. (service receiver). Thus, Mr. Y will pay Rs. 185 and ABC Ltd. will pay Rs. 124.

(ii) In case of renting of motor vehicles, abatement of 60% is available from gross amount charged on fulfillment of certain conditions. In other words, effective rate of service tax in case of renting of motor vehicles provided on abated value is 4.944% [12.36% of 40]. Thus, in the given case, service tax is payable on abated value [(Rs. 123.60 / Rs. 2500) x 100 = 4.944%].

In case of taxable services provided by way of renting of a motor vehicle designed to carry passengers on **abated** value to any person who is not engaged in the similar line of business by any individual/HUF/partnership firm (whether registered or not) including association of persons, located in the taxable territory to a business entity registered as body corporate, located in the taxable territory, entire service tax is liable to be paid by service receiver.

Since in the given case, renting of motor vehicle service is provided to a company (LMN Ltd.), reverse charge provisions will apply and entire service tax will be payable by service receiver (LMN Ltd.). Thus, service tax of Rs. 123.60 (4.944% of Rs. 2,500) is liable to be paid by LMN Ltd.

4. (a) (i) As per *Explanation 3* to section 40(b), "book profit" shall mean the net profit as per the profit and loss account for the relevant previous year computed in the manner laid down in Chapter IV-D as increased by the aggregate amount of the remuneration paid or payable to the partners of the firm if the same has been already deducted while computing the net profit.

In the present case, the net profit given is before deduction of depreciation on plant and machinery, interest on capital of partners and salary to the working partners. Therefore, the book profit shall be as follows:

Computation of Book Profit of the firm under section 40(b)

Particulars	**Rs.**	**Rs.**
Net Profit (before deduction of depreciation, salary and interest)		7,00,000
Less: Depreciation under section 32	1,50,000	
Interest @ 12% p.a. [being the maximum allowable as per section 40(b)] (5,00,000 × 12%)	60,000	2,10,000
Book Profit		**4,90,000**

(ii) Salary actually paid to working partners = Rs. 20,000 × 2 × 12 = Rs. 4,80,000.

As per the provisions of section 40(b)(v), the salary paid to the working partners is allowed subject to the following limits -

On the first Rs. 3,00,000 of book profit or in case of loss	Rs. 1,50,000 or 90% of book profit, whichever is more
On the balance of book profit	60% of the balance book profit

Therefore, the maximum allowable working partners' salary for the A.Y. 2014-15 in this case would be:

Particulars	**Rs.**
On the first Rs. 3,00,000 of book profit [(Rs. 1,50,000 or 90% of Rs. 3,00,000) whichever is more]	2,70,000
On the balance of book profit [60% of (Rs. 4,90,000 - Rs. 3,00,000)]	1,14,000
Maximum allowable partners' salary	3,84,000

Hence, allowable working partners' salary for the A.Y. 2014-15 as per the provisions of section 40(b)(v) is Rs. 3,84,000.

(b) Perquisite value for housing loan

The value of the benefit to the assessee resulting from the provision of interest-free or concessional loan made available to the employee or any member of his household during the relevant previous year by the employer or any person on his behalf shall be determined as the sum equal to the interest computed at the rate charged per annum by the State Bank of India (SBI) as on the 1st day of the relevant previous year in respect of loans for the same purpose advanced by it. This rate should be applied on the maximum outstanding monthly balance and the resulting amount should be reduced by the interest, if any, actually paid by him.

"Maximum outstanding monthly balance" means the aggregate outstanding balance for loan as on the last day of each month.

The perquisite value for computation is 10% - 6% = 4%

Month	**Maximum outstanding balance as on last date of month (Rs.)**	**Perquisite value at 4% for the month (Rs.)**
April, 2013	5,88,000	1,960
May, 2013	5,76,000	1,920
June, 2013	5,64,000	1,880
July, 2013	5,52,000	1,840
August, 2013	5,40,000	1,800
September, 2013	5,28,000	1,760
October, 2013	5,16,000	1,720
November, 2013	5,04,000	1,680
December, 2013	4,92,000	1,640
January, 2014	4,80,000	1,600
February, 2014	4,68,000	1,560
March, 2014	4,56,000	1,520
	Total value of this perquisite	**20,880**

Perquisite Value of Air Conditioners

Particulars	**Rs.**
Original cost	2,00,000
Depreciation on SLM basis for 4 years @10% i.e. Rs. 2,00,000 x10% x 4	80,000
Written down value	**1,20,000**
Amount recovered from the employee	90,000
Perquisite value	**30,000**

Chargeable perquisite in the hands of Mr. Sharad for the assessment year 2014-15

Particulars	**Rs.**
Housing loan	20,880

Air Conditioner	30,000
Total	**50,880**

(c) No, PQR Manufacturers Ltd. is not liable to pay duty in the given case. If any goods are pilfered after the unloading thereof but before the proper officer has made an order for clearance for home consumption, the importer shall not be liable to pay duty on such goods.

However, where such goods are restored to the importer after the pilferage, the importer becomes liable to pay duty. Thus, PQR Manufacturers Ltd. will be liable to pay duty if goods are restored to it.

(d) Computation of CENVAT credit available:

Particulars	**Amount (Rs.)**
Dumper [Note-1] =50% of Rs.1,00,000	50,000
Refrigerator fitted in office [Note-2]	Nil
Diesel for use in dumper [Note-3]	Nil
Car for use of employees for coming to site and going back [Note-2]	Nil
CENVAT credit available to contractor	50,000

Notes:

1. As per the definition of the capital goods read along with rule 4 of the CENVAT Credit Rules, 2004, CENVAT credit of 50% of the duty paid on the dumpers is available in current financial year and balance 50% in the succeeding financial year.
2. The definition of capital goods excludes
   (i) the motor vehicles designed to carry passengers and
   (ii) office equipment.
   Hence, the CENVAT credit of the above goods is not available.
3. The definition of the inputs specifically excludes diesel oil. Hence, the CENVAT credit of the same is not available.

5. (a) Computation of taxable income of Mrs. Ragini from gifts for A.Y.2014-15

Sl. No.	**Particulars**	**Taxable amount (Rs.)**	**Reason for taxability or otherwise of each gift**
1.	Relatives and friends	Nil	Gifts received on the occasion of marriage are not taxable.

2.	Cousin of Mrs. Ragini's mother	18,000	Cousin of Mrs. Ragini's mother is not a relative. Hence, the cash gift is taxable.
3.	Friend	Nil	Cell phone is not included in the definition of property as per *Explanation* to section 56(2)(vii). Hence, it is not taxable.
4.	Elder brother of husband's grandfather	25,000	Brother of husband's grandfather is not a relative. Hence, the cash gift is taxable.
5.	Friend	12,000	Cash gift from friend is taxable.
Aggregate value of gifts		**55,000**	

Since the sum of money received by Mrs. Ragini without consideration during the previous year 2013-14 exceeds Rs. 50,000, the whole of the amount is chargeable to tax under section 56(2)(vii) of the Income-tax Act, 1961.

(b) Under section 6(1), an individual is said to be resident in India in any previous year if he satisfies any one of the following conditions -

(i) He has been in India during the previous year for a total period of 182 days or more, or

(ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

In the case of Indian citizens leaving India for employment, the period of stay during the previous year must be 182 days instead of 60 days given in (ii) above.

During the previous year 2013-14, Mr. Rajan, an Indian citizen, was in India for 175 days only (i.e 30+31+30+31+31+22 days). Thereafter, he left India for employment purposes.

Since he does not satisfy the minimum criteria of 182 days, he is a non-resident for the A.Y. 2014-15.

(c) As per rule 5 of the Point of Taxation Rules, where a service is taxed for the first time, then,—

(a) no tax shall be payable to the extent the invoice has been issued and the payment received against such invoice before such service became taxable;

(b) no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within 14 days of the date when the service is taxed for the first time.

The facts given in the question do not fall under any of the above two clauses. Hence, service tax is payable on the same.

(d) Section 68 of Finance Act, 1994 casts the liability to pay service tax upon the service provider. This liability is not contingent upon the service provider realizing or charging service tax at the prevailing rate. Statutory liability does not get extinguished if service provider fails to realize or charge service tax from service receiver.

Therefore, action taken by tour operator is not correct in law. He will have to deposit service tax even if he has not collected the same from his client.

6. (a) Computation of total income of Mr. Yogesh for A.Y. 2014-15

Particulars	Rs.	Rs.	Rs.
Capital Gains			
Short term capital gains (on sale of flat)			
(i) Sale consideration	3,60,000		
(ii) Stamp duty valuation	3,70,000		
Consideration for the purpose of capital gains as per section 50C (stamp duty value, since it is higher than sale consideration)		3,70,000	
Less: Cost of acquisition [As per section 49(4), cost to be taken into consideration for 56(2)(vii) will be the cost of acquisition]		3,40,000	30,000
Long term capital loss on sale of equity shares of ABC Pvt. Ltd			
Sale consideration		2,80,000	
Less: Indexed cost of acquisition(Rs. 3,50,000 × 939/519)		6,33,237	
Long term capital loss to be carried forward		**3,53,237**	
(See Note 1 below)			
Income from other sources:			
Gift from friends by way of immovable property on 30.11.2013 [See Note 3 below].			3,40,000
Gift received from a close friend (unrelated person) [See Note 2 below]			75,000
Total income			**4,45,000**

Notes:

1. In the given problem, shares have been held for more than 12 months and hence, constitute a long term capital asset. The loss arising from sale of such

shares is, therefore, a long-term capital loss. As per section 70(3), long term capital loss can be set-off only against long-term capital gains. Therefore, long-term capital loss cannot be set-off against short-term capital gains. However, such long-term capital loss can be carried forward to the next year for set-off against long-term capital gains arising in that year.

2. Any sum received from an unrelated person will be deemed as income and taxed as income from other sources if the aggregate sum received exceeds Rs. 50,000 in a year [Section 56(2)(vii)].

3. Receipt of immovable property without consideration would attract the provisions of section 56(2)(vii).

(b) Services provided by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, excluding services provided by such artist as a brand ambassador are exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012.*

Since Ms. Namrita Kapoor is the brand ambassador of 'Sweet 16' soap manufactured by MNO Pvt. Ltd., the services rendered by her by way of a classical dance performance in the concert organized by MNO Pvt. Ltd. to promote its brand will not be eligible for the above-mentioned exemption and thus, be liable to service tax. The fact that the proceeds of the concert will be donated to a charitable organization will not have any bearing on the eligibility or otherwise to the above-mentioned exemption.

(c) As per section 65B(44) of Finance Act, 1994, a service is an activity carried out by one person for another person in lieu of a consideration. Further, Explanation 3 to section 65B(44) provides *inter alia* that an establishment of a person located in taxable territory and another establishment of such person located in non-taxable territory are treated as establishments of distinct persons. Also, as per explanation 4 to the said section, a person carrying on a business through a branch in any territory is treated as having an establishment in that territory.

Therefore, services provided by Mumbai branch to Head Office at New Delhi will not be 'service' in terms of section 65B(44) since both the establishments namely, Branch office and Head office are located in the taxable territory and are thus, one and the same person. However, when services are provided by Head Office at New Delhi to Singapore branch (located in non-taxable territory), the two establishments are treated as establishments of distinct persons and thus, the services provided in this case will constitute 'service' under service tax law.

7. (a) **Computation of business income of All India Aviation Ltd.**

Particulars	**Rs. (in lacs)**
Total profit derived from Units A & B (Rs. 13 lacs + Rs. 4 lacs)	17
Less: Exemption under section 10AA [**See Working Note below**]	12
	5
Less: Brought forward business loss	2
	3

Working Note:

Computation of exemption under section 10AA in respect of Unit A located in a SEZ

Particulars	**Rs. (in lacs)**
Domestic turnover of Unit A	10
Export turnover of Unit A	120
Total turnover of Unit A	**130**
Profit derived from Unit A	13
Exemption under section 10AA	
Profit of Unit A x $\frac{\text{Export turnover of unit A}}{\text{Total turnover of Unit A}}$ = 13 x $\frac{120}{130}$ =	12

(b) **(i)** As per section 139(4C), a research association referred to in section 10(21) must file its return of income within the due date under section 139(1) if its total income, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to income-tax.

Since the total income of the research association exceeds the basic exemption limit of Rs. 2,00,000, it has to file its return of income for the A.Y.2014-15.

(ii) As per section 139(4C), a registered trade union referred to in section 10(24) must file its return of income if the total income exceeds the basic exemption limit without giving effect to the provisions of section 10.

Since the total income of the trade union is less than the basic exemption limit of Rs. 2,00,000, it need not file its return of income for the A.Y. 2014-15.

(iii) As per section 139(4A), a charitable trust registered under section 12AA must file its return of income, if its total income computed as per the provisions of the Income-tax Act, 1961, without giving effect to the provisions of sections 11 and 12, exceeds the maximum amount which is not chargeable to income-tax.

Since the total income of the charitable trust exceeds Rs. 2,00,000, it has to file its return of income for the A.Y. 2014-15.

(iv) As per third proviso to section 139(1), every company or firm shall furnish on or before the due date the return in respect of its income or loss in every previous year. Since LLP is included in the definition of "firm" under the Income-tax Act, 1961, it has to file its return mandatorily, even though it has incurred a loss.

(c) If a tax has been levied on sale or purchase of any declared goods inside a State and the same goods are subsequently sold in the course of inter-state trade or commerce and is subjected to tax under the CST Act, sales tax paid has to be reimbursed to the dealer. However, sales tax paid within the state can be reimbursed only when the CST has been paid ***subsequently*** and not otherwise.

Hence, in this case, Mr. T can claim refund of tax paid within the State after payment of central sales tax in respect of such declared goods.

(d) Since the articles are not covered under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), excise duty will be payable on the basis of assessable value under section 4 of Central Excise Act (transaction value). Thus, value for purpose of excise duty will be Rs. 1,300 i.e., the price at which the articles are sold to wholesalers.

Particulars	**Rs.**
Transaction value [price at which Alpha Engineers sells articles to their wholesalers]	1,300
Excise duty @ 12% [12% of Rs. 1,300]	156
Education cess @ 2% [2% of Rs. 156]	3.12
Secondary and Higher Education Cess @ 1% [1% of Rs. 156]	1.56
Total excise duty payable (rounded off)	**161**