PAPER – 1: ACCOUNTING

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR MAY, 2017 EXAMINATION

A. Applicable for May, 2017 examination

I. Companies Act, 2013

Relevant Sections of the Companies Act, 2013 notified up to 31st October, 2016 will be applicable for May, 2017 Examination.

II. Amendments made by MCA in the Companies (Accounting Standards) Rules, 2006

Amendments made by MCA on 30.3.2016 in the Companies (Accounting Standards) Rules, 2006 have been made applicable for May, 2017examination.

MCA has issued Companies (Accounting Standards) Amendment Rules, 2016 to amend Companies (Accounting Standards) Rules, 2006 by incorporating the references of the Companies Act, 2013, wherever applicable. Also, the Accounting Standard (AS) 2, AS 4, AS 10, AS 13, AS 14, AS 21 and AS 29 as specified in these Rules will substitute the corresponding Accounting Standards with the same number as specified in Companies (Accounting Standards) Rules, 2006.

Following table summarises the changes made by the Companies (Accounting Standards) Amendment Rules, 2016 vis a vis the Companies (Accounting Standards) Rules, 2006 in the Accounting Standards relevant for Paper 1:

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
AS 2	4 (an extract)	Inventories do not include machinery spares which can be used only in connection with an item of fixed asset and whose use is expected to be irregular; such machinery spares are	Inventories do not include spare parts, servicing equipment and standby equipment which meet the definition of property, plant and equipment as per AS 10, Property, Plant	Now, inventories also do not include servicing equipment and standby equipment other than spare parts if they meet the definition of property, plant and equipment as per AS 10,

		accounted for in accordance with Accounting Standard (AS) 10, Accounting for Fixed Assets.	and Equipment. Such items are accounted for in accordance with Accounting Standard (AS) 10, Property, Plant and Equipment.	Property, Plant and Equipment.
	27	Common classifications of inventories are raw materials and components, work in progress, finished goods, stores and spares, and loose tools.	Common classifications of inventories are: (a) Raw materials and components (b) Work-in-progress (c) Finished goods (d) Stock-in-trade (in respect of goods acquired for trading) (e) Stores and spares (f) Loose tools (g) Others (specify nature)".	Para 27 of AS 2 requires disclosure of inventories under different classifications. One residual category has been added to the said paragraph i.e. 'Others'.
AS 10	All	Fixed Assets	Property, Plant and Equipment	Entire standard has been revised with the title AS 10: 'Property, Plant and Equipment' by

				replacing the existing AS 6 and AS 10. The students are advised to refer the explanation of AS 10 Property, Plant and equipment (2016) given in the Annexure. The Annexure is given at the end of Accounting Part II Suggested Answers
AS 13	20	The cost of any shares in a co-operative society or a company, the holding of which is directly related to the right to hold the investment property, is added to the carrying amount of the investment property.	An investment property is accounted for in accordance with cost model as prescribed in Accounting Standard (AS) 10, Property, Plant and Equipment. The cost of any shares in a co-operative society or a company, the holding of which is directly related to the right to hold the investment property, is added to the carrying amount of the investment property.	Accounting of investment property was not stated in this para but now incorporated i.e. at cost model.

	30	An enterprise holding investment properties should account for them as long term investments.	An enterprise holding investment properties should account for them in accordance with cost model as prescribed in AS 10, Property, Plant and Equipment.	Accounting of investment property shall now be in accordance with AS 10 i.e. at cost model
AS 14	3(a)	Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 1956 or any other statute which may be applicable to companies.	Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 2013 or any other statute which may be applicable to companies and includes 'merger'.	Definition of Amalgamation has been made broader by specifically including 'merger'.
	18 and 39	In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Account') which is disclosed as a part of 'miscellaneous expenditure' or	In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Reserve') which is presented as a separate line item. When the identity of the statutory reserves	Corresponding debit on account of statutory reserve in case of amalgamation in the nature of purchase is termed as 'Amalgamation Adjustment Reserve' and is now to be presented as a separate line item since there is not sub-heading like 'miscellaneous

		other similar category in the balance sheet. When the identity of the statutory reserves is no longer required to be maintained, both the reserves and the aforesaid account are reversed.	is no longer required to be maintained, both the reserves and the aforesaid account are reversed.	expenditure' in Schedule III to the Companies Act, 2013

B. <u>Not applicable for May, 2017 examination</u>

Non-Applicability of Ind ASs for May, 2017 Examination

The Ministry of Corporate Affairs has notified Companies (Indian Accounting Standards) Rules, 2015 on 16th February, 2015, for compliance by certain class of companies. These Ind AS have not been made applicable for May, 2017 Examination.

PART – II: QUESTIONS AND ANSWERS

QUESTIONS

Financial Statements of Companies

1. Garg Ltd. has the Authorised Capital of ₹ 10,00,000 consisting of 4,000 6% Preference shares of ₹ 100 each and 60,000 equity Shares of ₹10 each. The following was the Trial Balance of the Company as on 31st March , 2016

Particulars	Dr.	Cr.
Investment in Shares at cost	1,00,000	
Purchases	9,81,000	
Selling Expenses	1,58,200	
Inventory as at the beginning of the year	2,90,400	
Salaries and Wages	1,04,000	
Cash on Hand	24,000	
Interim Preference dividend for the half year to 30th September	12,000	
Bills Receivable	83,000	

Interest on Bank overdraft	19,600	
Interest on Debentures upto 30th Sep (1st half year)	7,500	
Trade receivables and trade payables	1,00,200	1,75,700
Freehold property at cost	7,00,000	
Furniture at cost less depreciation of ₹ 30,000	70,000	
6% Preference share capital		4,00,000
Equity share capital fully paid up		4,00,000
5% mortgage debentures secured on freehold properties		3,00,000
Income tax paid in advance for the current year	20,000	
Dividends		8,500
Profit and Loss A/c (opening balance)		57,000
Sales (Net)		13,40,700
Bank overdraft secured by hypothecation of stocks and receivables		3,00,000
Technical knowhow fees at cost paid during the year	3,00,000	
Audit fees	12,000	
Total	**29,81,900**	**29,81,900**

You are required to prepare the Profit and Loss Statement for the year ended 31st March, 2016 and the Balance Sheet as on 31st March, 2016 as per Schedule III of the Companies Act, 2013 after taking into account the following –

1. Closing Stock was valued at ₹ 2,85,000.
2. Purchases include ₹ 10,000 worth of goods and articles distributed among valued customers.
3. Salaries and Wages include ₹ 4,000 being Wages incurred for installation of Electrical Fittings which were recorded under "Furniture".
4. Bills Receivable include ₹ 3,000 being dishonoured bills. 50% of which had been considered irrecoverable.
5. Bills Receivable of ₹ 4,000 maturing after 31st March were discounted.
6. Depreciation on Furniture to be charged at 10% on Written Down Value.
7. Investment in shares is to be treated as non-current investments.
8. Interest on Debentures for the half year ending on 31st March was due on that date.
9. Provide Provision for taxation ₹ 8,000.
10. Technical Knowhow Fees is to be written off over a period of 10 years.

11. Salaries and Wages include ₹ 20,000 being Director's Remuneration.
12. Trade receivables include ₹ 12,000 due for more than six months.

Cash flow statement

2. From the following information, prepare a Cash Flow Statement for the year ended 31st March, 2016.

Balance Sheets as on.........

	Particulars	Note	31.03.2016 (₹)	31.03.2015 (₹)
I	EQUITY AND LIABILITES			
	(1) Shareholder's Funds			
	(a) Share Capital	1	3,50,000	3,00,000
	(b) Reserves and Surplus	2	82,000	38,000
	(2) Non-Current Liabilities			
	(3) Current Liabilities			
	Trade Payables		65,000	44,000
	Other Current Liabilities	3	37,000	27,000
	Short term Provisions (provision for tax)		32,000	28,000
	Total		5,66,000	4,37,000
II	ASSETS			
	(1) Non current Assets			
	Tangible Fixed Assets	4	2,66,000	1,90,000
	Intangible Assets (Goodwill)		47,000	60,000
	Non-Current Investments		35,000	10,000
	(2) Current Assets			
	Inventories		78,000	85,000
	Trade Receivables		1,08,000	75,000
	Cash & Cash Equivalents		32,000	17,000
	Total		5,66,000	4,37,000

Note 1: Share Capital

Particulars	31.03.2016 (₹)	31.03.2015 (₹)
Equity Share Capital	2,50,000	1,50,000

8% Preference Share Capital	1,00,000	1,50,000
Total	3,50,000	3,00,000

Note 2: Reserves and Surplus

Particulars	31.03.2016 (₹)	31.03.2015 (₹)
General Reserve	30,000	20,000
Profit and Loss A/c	27,000	18,000
Capital Reserve	25,000	______
Total	82,000	38,000

Note 3: Current Liabilities

Particulars	31.03.2016 (₹)	31.03.2015 (₹)
Dividend declared	37,000	27,000

Note 4: Tangible Fixed Assets

Particulars	31.03.2016 (₹)	31.03.2015 (₹)
Land & Building	75,000	1,00,000
Machinery	1,91,000	90,000
Total	2,66,000	1,90,000

Additional Information:

(i) ₹ 18,000 depreciation for the year has been written off on Plant and Machinery and no depreciation has been charged on land and building.

(ii) A piece of land has been sold out for ₹ 50,000 and the balance has been revalued, profit on such sale and revaluation being transferred to capital reserve. There is no other entry in Capital Reserve Account.

(iii) A plant was sold for ₹ 12,000 (WDV being ₹ 15,000).

(iv) Dividend received amounted to ₹ 2,100 which included pre acquisition dividend of ₹ 600.

(v) An interim dividend of ₹ 10,000 has been paid.

(vi) Non-current investments given in the balance sheet represents investment in shares of other companies.

Profit/Loss prior to Incorporation

3. The partners of Ojasvi Enterprises decided to convert the partnership firm into a Private Limited Company Tejasvi (P) Ltd. with effect from 1st January, 2015. However, company could be incorporated only on 1st June, 2015. The business was continued on behalf of the company and the consideration of ₹ 6,00,000 was settled on that day along with interest @ 12% per annum. The company availed loan of ₹ 9,00,000 @ 10% per annum on 1st June, 2015 to pay purchase consideration and for working capital. The company closed its accounts for the first time on 31st March, 2016 and presents you the following summarized profit and loss account:

	₹	₹
Sales		19,80,000
Cost of goods sold	11,88,000	
Discount to dealers	46,200	
Directors' remuneration	60,000	
Salaries	90,000	
Rent	1,35,000	
Interest	1,05,000	
Depreciation	30,000	
Office expenses	1,05,000	
Preliminary expenses (to be written off in first year itself)	15,000	17,74,200
Profit		2,05,800

Sales from June, 2015 to December, 2015 were 2½ times of the average sales, which further increased to 3½ times in January to March quarter, 2016. The company recruited additional work force to expand the business. The salaries from July, 2015 doubled. The company also acquired additional showroom at monthly rent of ₹ 10,000 from July, 2015.

You are required to prepare a statement showing apportionment of cost and revenue between pre-incorporation and post-incorporation periods. Also suggest the purposes for which Pre-incorporation Profit & Pre-incorporation Losses can be used for.

Accounting for Bonus Issue

4. Following is the extract of the Balance Sheet of Xeta Ltd. as at 31st March, 2017

	₹
Authorised capital:	
50,000 12% Preference shares of ₹ 10 each	5,00,000
4,00,000 Equity shares of ₹ 10 each	40,00,000
	45,00,000

Issued and Subscribed capital:	
24,000 12% Preference shares of ₹ 10 each fully paid	2,40,000
2,70,000 Equity shares of ₹ 10 each, ₹ 8 paid up	21,60,000
Reserves and surplus:	
General Reserve	3,60,000
Securities premium	1,00,000
Profit and Loss Account	6,00,000

On 1st April, 2017, the Company has made final call @ ₹ 2 each on 2,70,000 equity shares. The call money was received by 20th April, 2017. Thereafter, the company decided to capitalize its reserves by way of bonus at the rate of one share for every four shares held.

Show necessary journal entries in the books of the company and prepare the extract of the balance sheet as on 30th April, 2017 after bonus issue.

Internal Reconstruction of a Company

5. Kishor Limited decided to reconstruct its business as it has accumulated huge losses. The following is the Balance Sheet of the company as on 31.03.2016 before reconstruction:

Balance Sheet as on 31.03.2016

Particulars	₹	Particulars	₹
6,00,000 Equity shares of ₹ 10		Goodwill	10,40,000
each fully paid up	60,00,000	Patents	3,00,000
3,20,000, 6% Preference shares		Land & building	34,00,000
of ₹ 10 each fully paid up	32,00,000	Plant & machinery	4,00,000
6% Debentures (secured against		Investments (at cost)	4,40,000
land & building)	30,00,000	Trade receivables	34,80,000
Bank overdraft	11,60,000	Inventory	34,00,000
Trade payables	24,00,000	Profit & loss A/c	37,00,000
Provision for income tax	4,00,000		
	1,61,60,000		1,61,60,000

Following scheme of reconstruction is approved by all interested parties and the Court:

(1) All equity shares are reduced to ₹ 3 each and preference shares to ₹ 7 each.

(2) Debentureholders agreed to take over a part of land and building, book value of which is ₹ 14,00,000, towards their 50% claim. Rate of interest of balance 50% debentures will be increased to 9%.

(3) Goodwill and Patent will be written off.

(4) 10% of Trade receivables to be provided for bad debts.

(5) Inventory to be written off by ₹ 5,20,000.

(6) 50% of balance Land & Building sold for ₹ 12,00,000 and remaining Land & Building valued at ₹ 12,00,000.

(7) Investments to be sold for ₹ 4,00,000.

(8) The income tax liability of the company is settled at ₹ 4,50,000. Provision for income tax will be raised accordingly.

(9) 1/3 of trade payables decided to forgo their claim.

(10) After making all the above adjustments, balance amount available through scheme, will be utilized to write off the value of plant & machinery to that extent.

You are required to pass the necessary Journal Entries.

Amalgamation of Companies

6. H Ltd. and N Ltd. are to be amalgamated into HN Ltd. The new company is to take over all the assets and liabilities of the amalgamating companies.

Assets and Liabilities of H Ltd. are to be taken over at book values in exchange of shares in HN Ltd. Three shares in the new company are to be issued at a premium of 20% for every two shares of ₹ 10 each in H Ltd.

The approved scheme for N Ltd. is as follows:

1. 10% Preference shareholders are to be allowed two 15% Preference shares of ₹ 100 each in HN Ltd. for three Preference shares held in N Ltd.
2. The Debentures of N Ltd. are to be paid off at 5% discount by the issue of debentures of HN Ltd. at par.
3. The Equity shareholders of N Ltd. are to be allowed as many shares at par in HN Ltd. as will cover the balance on their account and for this purpose, plant and machinery is to be valued less by 15% and obsolete stock worth ₹ 7,500 (included in the value of stock) is to be treated as worthless.

The summarized Balance Sheets of the two companies prior to amalgamation are as follows:

Liabilities	H Ltd.	N Ltd.	Assets	H Ltd.	N Ltd.
	₹	₹		₹	₹
Equity Shares of ₹ 10 each	3,20,000	6,25,000	Plant and Machinery	6,40,000	10,00,000
10% Preference Shares of ₹ 100 each	-	3,75,000	Trade receivables	76,000	62,500

General Reserves	4,40,000	-	Inventory	50,000	75,000
Secured Debentures	-	2,50,000	Cash and Bank Balance	54,000	50,000
Trade payables	60,000	1,12,500	Profit and Loss Account	-	1,75,000
	8,20,000	13,62,500		8,20,000	13,62,500

You are required to show the Journal Entries and the Balance Sheet of the amalgamated company immediately after amalgamation.

Average Due Date

7. Kiran had accepted bills payable to Heena, falling due on different dates. The details of bills are as follows:

Date of bill	Amount	Usance of bill
9th April 2016	₹ 3,000	for 4 months
18th April 2016	₹ 5,500	for 3 months
25th May 2016	₹ 3,000	for 6 months
5th June 2016	₹ 6,000	for 3 months

On 1st July, it was agreed that these bills should be withdrawn and that Kiran should accept on that day two bills, one for ₹ 10,000 due in 4 months and the other for the balance with interest, due in 6 months. Calculate the amount of the second bill taking interest @ 10% p.a. Take 365 days in year 2016-2017.

Account Current

8. From the following transactions in the books of Mr. Perfact, prepare an Account Current, by means of product to be sent by him to Mr. Smart for the quarter ending 31st March, 2016. Interest is to be charged and/or allowed @ 12% p.a.

2016		₹
January 1	Balance in Smart's Account (Credit)	3,500
January 12	Sold goods to Smart (due 1st February)	30,000
January 31	Sold goods to Smart (due 15th February)	27,500
February 15	Cash received	40,000
February 20	Cash received	7,500
March 10	Goods returned by Smart	7,000
March 25	Cash received	6,500

Self – Balancing Ledgers

9. How will you show the following items in General Ledger Adjustment Account in Debtors Ledger and General Ledger Adjustment Account in Creditors Ledger:

	₹
Transfer from Debtors' Ledger-to Creditors' Ledger	2,200
Bill receivable endorsed to Creditors	8,000
Endorsed Bills dishonoured	2,000
Bad Debts written off (after deducting bad debts recovered ₹ 600)	4,400
Provision for Doubtful Debts	1,100
Provision for Discount on Debtors	2,000
Reserve for Discount on Creditors	4,000
Cash Sales	6,000
Cash Purchases	8,000
Bill Receivable Collected on maturity	10,000
Bills Receivable discounted	12,000
Bills Payable matured	14,000
Discount allowed	3,000
Discount received	1,200
Allowances from Creditors	6,400

Financial Statements of Not-For-Profit Organizations

10. You are provided the following information related to Krishna sports club:

	31st Dec. 2015	*31st Dec. 2016*
Building (subject to 10% depreciation for the current year)	60,000	?
Furniture (subject to 10% depreciation for the current year)	-	20,000
Stock of Sports Materials	5,000	2,000
Prepaid Insurance	3,000	6,000
Outstanding Subscription	12,000	8,000
Advance Subscription	6,000	4,000
Outstanding Locker Rent		6,000
Advance Locker Rent received	-	2,000
Outstanding Rent for Godown	6,000	3,000

12% General Fund Investments	2,00,000	?
Accrued Interest on above (for 2 months)	-	4,000
Cash Balance	1,000	64,000
Bank Balance	2,000	-
Bank Overdraft		2,000

Entrance Fees received ₹ 20,000, Life Membership Fees received ₹ 20,000, surplus from Income & expenditure Account ₹ 60,000. It is the policy of the club to treat 60% of entrance fees and 40% of Life Membership Fees as of revenue nature. The furniture was purchased on 1.01.2016

You are required to prepare the opening and closing balance sheets of Krishna sports club as on 1st January, 2016 and 31st December, 2016.

Accounts from Incomplete Records

11. From the following information in respect of Mr. Preet, prepare Trading and Profit and Loss Account for the year ended 31st March, 2016 and a Balance Sheet as at that date:

		31-03-2015	31-03-2016
(1)	Liabilities and Assets	₹	₹
	Stock in trade	1,60,000	1,40,000
	Debtors for sales	3,20,000	?
	Bills receivable	-	?
	Creditors for purchases	2,20,000	3,00,000
	Furniture at written down value	1,20,000	1,27,000
	Expenses outstanding	40,000	36,000
	Prepaid expenses	12,000	14,000
	Cash on hand	4,000	3,000
	Bank Balance	20,000	1,500
(2)	Receipts and Payments during 2015-2016:		
	Collections from Debtors		
	(after allowing 2-1/2% discount)		11,70,000
	Payments to Creditors		
	(after receiving 2% discount)		7,84,000
	Proceeds of Bills receivable discounted at 2%)		1,22,500
	Proprietor's drawings		1,40,000

	Purchase of furniture on 30.09.2015		20,000
	12% Government securities purchased on 1-10-2015		2,00,000
	Expenses		3,50,000
	Miscellaneous Income		10,000
(3)	Sales are effected so as to realize a gross profit of 50% on the cost.		
(4)	Capital introduced during the year by the proprietor by cheques was omitted to be recorded in the Cash Book, though the bank balance of 9,500 on 31st March, 2016 (as shown above), is after taking the same into account.		
(5)	Purchases and Sales are made only on credit.		
(6)	During the year, Bills Receivable of ₹ 2,00,000 were drawn on debtors. out of these, Bills amount to ₹ 40,000 were endorsed in favour of creditors. Out of this latter amount, a Bill for ₹ 8,000 was dishonoured by the debtor.		

Hire Purchase Transactions

12. The following particulars relate to hire purchase transactions:

    (a) X purchased three cars from Y on hire purchase basis, the cash price of each car being ₹ 2,00,000.

    (b) The hire purchaser charged depreciation @ 20% on diminishing balance method.

    (c) Two cars were seized by on hire vendor when second installment was not paid at the end of the second year. The hire vendor valued the two cars at cash price less 30% depreciation charged under it diminishing balance method.

    (d) The hire vendor spent ₹ 10,000 on repairs of the cars and then sold them for a total amount of ₹ 1,70,000.

    You are required to compute:

    (i) Agreed value of two cars taken back by the hire vendor.

    (ii) Book value of car left with the hire purchaser.

    (iii) Profit or loss to hire purchaser on two cars taken back by their hire vendor.

    (iv) Profit or loss of cars repossessed, when sold by the hire vendor.

Investment Accounts

13. Muskaan purchased 5,000, 13.5% Debentures of Face Value of ₹ 100 each of Shorya Ltd. on 1st May 2016 @ ₹ 105 on cum interest basis. The interest on these debentures is payable on 31st & 30th of March & September respectively. On August 1st 201,6 she again purchased 2,500 of such debentures @ ₹ 102.50 each on cum interest basis. On October 1st, 2016 she sold 2,000 Debentures @ ₹ 103 each. The market value of the debentures

as at the close of the year was ₹ 106. Prepare the Debenture Investment Account in the books of Muskaan for the year ended 31st Dec. 2016 on Average Cost Basis.

Insurance Claim

14. A fire engulfed the premises of a business of M/s K on the morning of 1st July 2016. The building, equipment and stock were destroyed and the salvage recorded the following:

Building – ₹ 4,000; Equipment – ₹ 2,500; Stock – ₹ 20,000. The following other information was obtained from the records saved for the period from 1st January to 30th June 2016:

	₹
Sales	11,10,000
Purchases	9,37,500
Cartage inward	17,500
Wages	7,500
Stock in hand on 31st December, 2015	1,50,000
Building (value on 31st December, 2015)	3,75,000
Equipment (value on 31st December, 2015)	75,000
Depreciation provision till 31st December, 2015 on:	
Building	1,25,000
Equipment	22,500

No depreciation has been provided since December 31st 2015. The latest rate of depreciation is 5% p.a. on building and 15% p.a. on equipment by straight line method.

Normally business makes a profit of 25% on sales. You are required to prepare the statement of claim for submission to the Insurance Company.

Issues in Partnership Accounts

15. Neha & Co. is a partnership firm with partners Mr. P, Mr. Q and Mr. R, sharing profits and losses in the ratio of 10:6:4. The balance sheet of the firm as at 31st March, 2016 is as under:

Liabilities		**₹**	**Assets**	**₹**
Capitals:			Land	10,000
Mr. P	80,000		Buildings	2,00,000
Mr. Q	20,000		Plant and machinery	1,30,000
Mr. R	30,000	1,30,000	Furniture	43,000
Reserves			Investments	12,000
(un-appropriated profit)		20,000	Inventories	1,30,000

Long Term Debt		3,00,000	Trade receivables	1,39,000
Bank Overdraft		44,000		
Trade payables		1,70,000		
		6,64,000		6,64,000

It was mutually agreed that Mr. Q will retire from partnership and in his place Mr. T will be admitted as a partner with effect from 1st April, 2016. For this purpose, the following adjustments are to be made:

(a) Goodwill is to be valued at ₹1 lakh but the same will not appear as an asset in the books of the reconstituted firm.

(b) Buildings and plant and machinery are to be depreciated by 5% and 20% respectively. Investments are to be taken over by the retiring partner at ₹15,000. Provision of 20% is to be made on Trade receivables to cover doubtful debts.

(c) In the reconstituted firm, the total capital will be ₹ 2 lakhs which will be contributed by Mr. P, Mr. R and Mr. T in their new profit sharing ratio, which is 2:2:1.

(i) The surplus funds, if any, will be used for repaying bank overdraft.

(ii) The amount due to retiring partner shall be transferred to his loan account.

Required:

Prepare

(a) Revaluation account;

(b) Partners' capital accounts;

(c) Bank account; and

(d) Balance sheet of the reconstituted firm as on 1st April, 2016.

Accounting in Computerised Environment

16. Recently, a growing trend is being developed for outsourcing the accounting function to a third party. What are the benefits of such outsourcing? Also, explain the basis on which choice of such third party being made.

Applicability of AS

17. (a) M/s X& Co. (a partnership firm), had a turnover of ₹ 1.25 crores (excluding other income) and borrowings of ₹ 0.95 crores in the previous year. It wants to avail the exemptions available in application of Accounting Standards to non-corporate entities for the year ended 31.3.2016. Advise the management of M/s X & Co in respect of the exemptions of provisions of ASs, as per the directive issued by the ICAI.

AS 1 Disclosure of Accounting Policies

(b) Mini Ltd. was making provision for non-moving stocks based on no issues for the last 12 months up to 31.3.2016.

The company wants to provide during the year ending 31.3.2016 based on technical evaluation:

Total value of stock	₹ 100 lakhs
Provision required based on 12 months issue	₹ 3.5 lakhs
Provision required based on technical evaluation	₹ 2.5 lakhs

Does this amount to change in Accounting Policy? Can the company change the method of provision?

AS 2 Valuation of Inventories

18. (a) Suraj Stores is a departmental store, which sell goods on retail basis. It makes a gross profit of 20% on net sales. The following figures for the year-end are available:

Opening Inventory ₹ 50,000; Purchases ₹ 3,60,000; Purchase Returns ₹ 10,000; Freight Inwards ₹ 10,000; Gross Sales ₹ 4,50,000; Sales Returns ₹ 11,250; Carriage Outwards ₹ 5,000.

Compute the estimated cost of the inventory on the closing date.

Depreciation Accounting as per AS 10 Property, Plant and Equipment

(b) A property costing ₹ 10,00,000 is bought in 2016. Its estimated total physical life is 50 years. However, the company considers it likely that it will sell the property after 20 years.

The estimated residual value in 20 years' time, based on 2016 prices, is:

Case (a) ₹ 10,00,000

Case (b) ₹ 9,00,000

You are required to compute the amount of depreciation charged for the year 2016.

AS 7 Construction Contracts

19. (a) Mr. 'Mehta' as a contractor has just entered into a contract with a local municipal body for building a flyover. As per the contract terms, Mr. 'Mehta'' will receive an additional ₹ 2 crore if the construction of the flyover were to be finished within a period of two years of the commencement of the contract. Mr. 'Mehta' wants to recognize this revenue since in the past he has been able to meet similar targets very easily.

Is Mr. 'Mehta' correct in his proposal? Discuss.

AS 9 Revenue Recognition

(b) K Ltd. has sold its building for ₹ 50 lakhs to B Ltd. and has also given the possession to B Ltd. The book value of the building is ₹ 30 lakhs. As on 31st March, 2016, the documentation and legal formalities are pending. The company has not recorded the sale and has shown the amount received as advance. Do you agree with this treatment?

AS 10 Property, Plant and Equipment

20. (a) Entity Hello has an existing freehold factory property, which it intends to knock down and redevelop. During the redevelopment period the company will move its production facilities to another (temporary) site.

The following incremental costs will be incurred:

Setup costs of ₹ 5,00,000 to install machinery in the new location.

Rent of ₹ 15,00,000

Removal costs of ₹ 3,00,000 to transport the machinery from the old location to the temporary location.

You are required to advise can these costs be capitalised into the cost of the new building?

AS 13 Accounting for Investments

(b) Z Bank has classified its total investment on 31-3-2016 into three categories (a) held to maturity (b) available for sale (c) held for trading as per the RBI Guidelines.

'Held to maturity' investments are carried at acquisition cost less amortised amount. 'Available for sale' investments are carried at marked to market. 'Held for trading' investments are valued at weekly intervals at market rates. Net depreciation, if any, is charged to revenue and net appreciation, if any, is ignored. Comment whether the policy of the bank is in accordance with AS 13?

SUGGESTED ANSWERS

1. **Statement of Profit and Loss of Garg Ltd. for the year ended 31st March, 2016**

	Particulars	*Note*	*This Year*
I	Revenue from Operations		13,40,700
II	Other income (Divided income)		8,500
III	Total Revenue (I &+ II)		13,49,200
IV	Expenses:		
	(a) Purchases of Inventory (9,81,000 – Advertisement		9,71,000

	Expenses 10,000)		
	(b) Changes in Inventories of finished Goods / Work in progress & inventory (2,90,400 – 2,85,000)		5,400
	(c) Employee Benefits expense	**9**	80,000
	(d) Finance costs	**10**	34,600
	(e) Depreciation & Amortization Expenses [10% of (70,000 + 4,000)]		7,400
	(f) Other Expenses	**11**	2,31,700
	Total Expenses		13,30,100
V	Profit before exceptional, extraordinary items and tax (III-IV)		19,100
VI	Exceptional items		-
VII	Profit before extra ordinary items and tax (V-IV)		19,100
VIII	Extraordinary items		-
IX	Profit before tax (VII-VIII)		19,100
X	Tax expense:		
	Current Tax		8,000
XI	Profit/Loss for the period (after tax)		11,100

Balance sheet of Garg Ltd. as on 31st March, 2016

	Particulars as on 31st March	*Note*	
I			
(1)	**Shareholders' funds:**		
	(a) Share capital	**1**	8,00,000
	(b) Reserves and surplus	**2**	44,100
(2)	**Non current liabilities:**		
	Long term borrowings	**3**	3,00,000
(3)	**Current liabilities:**		
	(a) Short term borrowings	**4**	3,00,000
	(b) Trade payables		1,75,700
	(c) Other current liabilities	**5**	19,500
	Total		**16,39,300**
II	**ASSETS**		
(1)	(a) Non-current Assets		
	Fixed assets (i) Tangible assets	**6**	7,66,600
	(ii) Intangible assets	**7**	2,70,000

	(b) Non current investments (Shares at cost)		1,00,000
	Current Assets:		
	(a) Inventories		2,85,000
	(b) Trade receivables	**8**	1,81,700
	(c) Cash and Cash equivalents – Cash on hand		24,000
	(d) Short term loans and advances –Income tax (paid 20,000-Provision 8000)		12,000
	Total		**16,39,300**

Note: There is a Contingent liability for Bills receivable discounted with Bank ₹ 4000.

Notes to accounts

			(₹)
1.	**Share Capital**		
	Authorized,		
	60,000 Equity Shares of ₹ 10 each.	6,00,000	
	4,000 6% Preference shares of ₹ 100 each	4,00,000	
	Issued, subscribed & called up		
	40,000, Equity Shares of ₹ 10 each	4,00,000	
	4,000 6% Redeemable Preference Shares of 100 each	4,00,000	8,00,000
2.	**Reserves and Surplus**		
	Balance as on 1st April, 2015	57,000	
	Add: Surplus for current year	11,100	68,100
	Less: Preference Dividend		24,000
	Balance as on 31st March, 2016		44,100
3.	**Long Term Borrowings**		
	5% Mortgage Debentures (Secured against Freehold Properties)		3,00,000
4.	**Short Term Borrowings**		
	Secured Borrowings: Loans Repayable on Demand Overdraft from Banks (Secured by Hypothecation of Stocks & Receivables)		3,00,000
5.	**Other Current liabilities**		
	Interest Accrued and due on Borrowings (5% Debentures)	7,500	

	Unpaid Preference Dividends	12,000	19,500
6.	**Tangible Fixed assets**		
	Furniture		
	Furniture at Cost Less depreciation ₹ 30,000 (as given in Trial Balance	70,000	
	Add: Depreciation	30,000	
	Cost of Furniture	1,00,000	
	Add: Installation charge of Electrical Fittings wrongly included under the heading Salaries and Wages	4,000	
	Total Gross block of Furniture A/c	1,04,000	
	Accumulated Depreciation Account: Opening Balance-given in Trial Balance 30,000		
	Depreciation for the year: On Opening WDV at 10% i.e. (10% x 70,000) 7,000		
	On additional purchase during the year at 10% i.e. (10% x 4,000) 400		
	Less: Accumulated Depreciation	37,400	66,600
	Freehold property (at cost)		7,00,000
			7,66,600
7.	**Intangible Fixed Assets**		
	Technical knowhow	3,00,000	
	Less: Written off	30,000	2,70,000
8.	**Trade Receivables**		
	Sundry Debtors (a) Debt outstanding due more than six months	12,000	
	(b) Other Debts (refer Working Note)	89,700	
	Bills Receivable (83,000 -3,000)	80,000	1,81,700
9.	**Employee benefit expenses**		
	Amount as per Trial Balance	1,04,000	
	Less: Wages incurred for installation of electrical fittings to be capitalised	4,000	
	Less: Directors' Remuneration shown separately	20,000	
	Balance amount		80,000

10.	**Finance Costs**		
	Interest on bank overdraft	15,600	
	Interest on debentures	15,000	
	Discount on Issue of Debentures	4,000	34,600
11.	**Other Expenses**		
	Payment to the auditors	12,000	
	Director's remuneration	20,000	
	Selling expenses	1,58,200	
	Technical knowhow written of (3,00,000/10)	30,000	
	Advertisement (Goods and Articles Distributed)	10,000	
	Bad Debts (3,000 x50%)	1,500	2,31,700

Working Note

Calculation of Sundry Debtors-Other Debts

Sundry Debtors as given in Trial Balance	1,00,200
Add Back: Bills Receivables Dishonoured	3,000
	1,03,200
Less: Bad Debts written off – 50% ₹ 3,000	(1,500)
Adjusted Sundry Debtors	1,01,700
Less: Debts due for more than 6 months (as per information given)	(12,000)
Total of other Debtors i.e. Debtors outstanding for less than 6 months	89,700

2. Cash flow Statement for the year ending 31st March, 2016

		Particulars	₹	₹
1		**Cash Flow from Operating Activities**		
	A.	Closing balance as per Profit and Loss Account		27,000
		Less: Opening balance as per Profit and Loss Account		(18,000)
		Add: Dividend declared during the year		37,000
		Add: Interim dividend paid during the year		10,000
		Add: Transfer to reserve		10,000
		Add: Provision for Tax		32,000
	B.	Net profit before taxation, and extra ordinary item		98,000
	C.	*Add:* Items to be added		
		Depreciation	18,000	
		Loss on sale of Plant	3,000	
		Goodwill written off	13,000	34,000

	D.	*Less:* Dividend Income		(1,500)
	E.	Operating profit before working capital changes [B + C - D]		1,30,500
	F.	*Add:* Decrease in Current Assets and Increase in current Liabilities		
		Decrease in Inventories	7,000	
		Increase in Trade Payables	21,000	28,000
	G.	*Less:* Increase in Trade Receivables (Gross)		(33,000)
	H	Cash generated from operations (E+F-G)		1,25,500
	I	Less: Income taxes paid		(28,000)
	J	Net Cash from (used in) operating activities		97,500
II.		**Cash Flows from investing activities:**		
		Purchase of Plant		(1,34,000)
		Sale of Land		50,000
		Sale of plant		12,000
		Purchase of investments		(25,600)
		Dividend Received		2,100
		Net cash used in investing activities		(95,500)
III.		**Cash Flows from Financing Activities:**		
		Proceeds from issuance of share capital		1,00,000
		Redemption of preference shares		(50,000)
		Interim Dividend paid		(10,000)
		Final dividend paid		(27,000)
		Net cash from financing activities		13,000
IV.		**Net increase in cash and cash equivalents (I+II+III)**		15,000
V.		**Cash and cash equivalents at beginning of period**		17,000
VI.		**Cash and cash equivalents at end of period (IV+V)**		32,000

1. Land and Building Account

Particulars	₹	*Particulars*	₹
To Balance b/d	1,00,000	By Bank A/c (Sale)	50,000
To Capital Reserve A/c (Profit on sale/revaluation)	25,000	By Balance c/d	75,000
	1,25,000		1,25,000

2. **Plant and Machinery Account**

Particulars	₹	*Particulars*	₹
To Balance b/d	90,000	By Depreciation A/c	18,000
To Bank A/c (Purchase)	1,34,000	By Bank A/c (sale)	12,000
		By Profit and Loss A/c (Loss on sale)	3,000
		By Balance c/d	1,91,000
	2,24,000		**2,24,000**

3. **Investments Account**

Particulars	₹	*Particulars*	₹
To Balance b/d	10,000	By bank A/c (Div. received)	600
To bank A/c (Purchase	25,600	By Balance c/d	35,000
Total	**35,600**		**35,600**

3. **Tejasvi (P) Limited**

Profit and Loss Account

for 15 months ended 31st March, 2016

	Pre. inc. (5 months) (₹)	***Post inc. (10 months) (₹)***
Sales (W.N.1)	3,00,000	16,80,000
Less: Cost of sales	1,80,000	10,08,000
Discount to dealers	7,000	39,200
Directors' remuneration	-	60,000
Salaries (W.N.2)	18,750	71,250
Rent (W.N.3)	15,000	1,20,000
Interest (W.N.4)	30,000	75,000
Depreciation	10,000	20,000
Office expenses	35,000	70,000
Preliminary expenses		15,000
Net profit	4,250	2,01,550

Purposes for which pre-incorporation profits and losses can be used are as follows:

Pre-incorporation Profits can be used for:	Pre-incorporation Losses can be used for:
• writing off Goodwill on acquisition • writing off Preliminary Expenses • writing down over-valued assets • issuing of bonus shares • paying up partly paid shares.	• setting off against Post-Incorporation Profit • addition to Goodwill on acquisition • writing off Capital Profit

Working Notes:

1. Calculation of sales ratio

Let the average sales per month in pre-incorporation period be x

Average Sales (Pre-incorporation)	= x X 5	=	5x
Sales (Post incorporation) from June to December, 2015	= 2½x X 7	=	17.5x
From January to March, 2016	= 3½x X 3	=	10.5x
Total Sales			28.0x

Sales ratio of pre-incorporation & post incorporation is 5x : 28x

2. Calculation of ratio for salaries

Let the average salary be x

Pre-incorporation salary	=	x X 5	=	5x
Post incorporation salary				
June, 2015	=			x
July to March, 2016	=	x X 9 X 2	=	18x
				19x

Ratio is 5 : 19

3. Calculation of Rent

		₹
Total rent		1,35,000
Less: Additional rent for 9 months @ ₹ 10,000 p.m.		90,000
Rent of old premises apportioned in time ratio		45,000
Apportionment	Pre Inc.	Post Inc.
Old premises rent	15,000	30,000
Additional Rent		90,000
	15,000	1,20,000

4. Calculation of interest

Pre-incorporation period from January, 2015 to May, 2015

$\left(\frac{6,00,000 \times 12 \times 5}{100 \times 12}\right) =$ ₹ 30,000

Post incorporation period from June, 2015 to March, 2016

$\left(\frac{9,00,000 \times 10 \times 10}{100 \times 12}\right) =$ ₹ 75,000

₹ 1,05,000

4. Journal Entries in the books of Xeta Ltd.

			₹	₹
1-4-2017	Equity share final call A/c	Dr.	5,40,000	
	To Equity share capital A/c			5,40,000
	(For final calls of ₹ 2 per share on 2,70,000 equity shares due as per Board's Resolution dated….)			
20-4-2017	Bank A/c	Dr.	5,40,000	
	To Equity share final call A/c			5,40,000
	(For final call money on 2,70,000 equity shares received)			
	Securities Premium A/c	Dr.	1,00,000	
	General Reserve A/c	Dr.	3,60,000	
	Profit and Loss A/c	Dr.	2,15,000	
	To Bonus to shareholders A/c			6,75,000
	(For making provision for bonus issue of one share for every four shares held)			
	Bonus to shareholders A/c	Dr.	6,75,000	
	To Equity share capital A/c			6,75,000
	(For issue of bonus shares)			

Extract of Balance Sheet as at 30th April, 2017 (after bonus issue)

	₹
Authorised Capital	
50,000 12% Preference shares of ₹10 each	5,00,000
4,00,000 Equity shares of ₹10 each	40,00,000
Issued and subscribed capital	
24,000 12% Preference shares of ₹10 each, fully paid	2,40,000
3,37,500 Equity shares of ₹10 each, fully paid	33,75,000
(Out of above, 67,500 equity shares @ ₹10 each were issued by way of bonus)	
Reserves and surplus	
Profit and Loss Account	3,85,000

5. **Journal Entries in the books of Kishor Limited**

			Dr. (₹)	***Cr. (₹)***
1.	Equity share capital A/c (₹ 10)	Dr.	60,00,000	
	To Equity share capital A/c (₹ 3)			18,00,000
	To Capital reduction A/c			42,00,000
	(Reduction of equity share of ₹ 10 each to shares of ₹ 3 each as per the reconstruction scheme)			
2.	6% Preference share capital A/c (₹ 10)	Dr.	32,00,000	
	To 6% Preference share capital A/c (₹ 7)			22,40,000
	To Capital reduction A/c			9,60,000
	(Reduction of preference share of ₹ 10 each to shares of ₹ 7 each as per the reconstruction scheme)			
3.	6 % Debentures A/c	Dr.	30,00,000	
	To Land & building A/c			14,00,000
	To 9% Debentures A/c			15,00,000
	To Capital reduction A/c			1,00,000
	(50% claim of debentureholders discharged by transfer of a part of land & building having book value ₹ 14,00,000 and rate of interest of balance 50% debentures increased to 9% as per the reconstruction scheme).			
4.	Bank A/c	Dr.	12,00,000	
	To Land & building A/c			10,00,000
	To Capital reduction A/c			2,00,000
	(50% of balance land & building having book value ₹ 10,00,000 sold as per the reconstruction scheme)			
5.	Land & building A/c	Dr.	2,00,000	
	To Capital Reduction A/c			2,00,000
	(50% of balance land & building having book value ₹ 10,00,000, valued at ₹ 12,00,000, as per the reconstruction scheme)			
6.	Bank A/c	Dr.	4,00,000	
	Capital reduction A/c	Dr.	40,000	
	To Investment A/c			4,40,000
	(All the investment sold as per the reconstruction scheme)			

7.	Trade payables A/c	Dr.	8,00,000	
	To Capital reduction A/c			8,00,000
	(1/3 of Trade payables decided to forgo their claim as per the reconstruction scheme)			
8.	Capital reduction A/c	Dr.	61,58,000	
	To Goodwill A/c			10,40,000
	To Patents A/c			3,00,000
	To Provision of doubtful debts A/c			3,48,000
	To Inventory A/c			5,20,000
	To Provision for income tax A/c			50,000
	To Profit & loss A/c			37,00,000
	To Plant & machinery A/c (Bal. fig.)			2,00,000
	(Written off goodwill, patent, profit & loss, part value of stock, plant & machinery, penalty paid for cancellation of contracts and provision made for doubtful debts, income tax, as per the reconstruction scheme)			

6. Journal Entries in the books of HN Ltd. (Amalgamated Company)

	Particulars		*Debit*	*Credit*
			₹	₹
1.	Business Purchase A/c	Dr.	12,56,000	
	To Liquidators of H Ltd.			5,76,000
	To Liquidators of N Ltd.			6,80,000
	(Being purchase of business of H Ltd. and N Ltd.- Refer Working Note)			
2.	Plant and Machinery A/c	Dr.	6,40,000	
	Trade receivables A/c	Dr.	76,000	
	Inventory A/c	Dr.	50,000	
	Cash and Bank A/c	Dr.	54,000	
	To Trade payables A/c			60,000
	To General Reserve A/c			1,84,000
	To Business Purchase A/c			5,76,000
	(Being assets and liabilities of H Ltd. taken over)			
3.	Plant and Machinery A/c	Dr.	8,50,000	
	Trade receivables A/c	Dr.	62,500	
	Inventory A/c	Dr.	67,500	
	Cash and Bank A/c	Dr.	50,000	

	To Debentureholders A/c (95% of 2,50,000)		2,37,500
	To Trade payables A/c		1,12,500
	To Business Purchase A/c		6,80,000
	(Being assets and liabilities of N Ltd. taken over)		
4.	Liquidator of H Ltd. A/c Dr.	5,76,000	
	To Equity Share Capital A/c		4,80,000
	To Securities Premium A/c		96,000
	(Being equity shares issued at 20% premium to shareholders of H Ltd.)		
5.	Liquidators of N Ltd. A/c Dr.	6,80,000	
	To Equity Share Capital A/c		4,30,000
	To 15% Preference Share Capital A/c		2,50,000
	(Being issue of shares to discharge purchase consideration)		
6.	Debentureholders of N Ltd. A/c Dr.	2,37,500	
	To Debentures A/c		2,37,500
	(Being own debentures issued against debentures of N Ltd.)		

Balance Sheet of HN Ltd. after amalgamation

Particulars	*Note No.*	₹
I. **Equity and Liabilities**		
(1) **Shareholder's Funds**		
(a) Share Capital	1	11,60,000
(b) Reserves and Surplus	2	2,80,000
(2) **Non-current Liabilities**		
Long-term borrowings	3	2,37,500
(3) **Current Liabilities**		
Trade payables		1,72,500
Total		18,50,000
II. **Assets**		
(1) **Non-current assets**		
Fixed assets		
Tangible assets	4	14,90,000
(2) **Current assets**		
(a) Inventories		1,17,500
(b) Trade receivables		1,38,500
(c) Cash and cash equivalents		1,04,000
Total		18,50,000

Notes to Accounts

		₹
1.	**Share Capital**	
	Equity shares of ₹ 10 each	9,10,000
	Preference shares of ₹ 10 each	2,50,000
		11,60,000
2.	**Reserves and surplus**	
	General Reserve	1,84,000
	Securities Premium	96,000
		2,80,000
3.	**Long-term Borrowings**	
	Secured Debentures	2,37,500
4.	**Tangible Assets**	
	Plant and Machinery	14,90,000

Working Note:

Computation of Purchase Consideration

A. For H Ltd., the Payment Method is applied for determining the Purchase Consideration. Hence, the amalgamation is accounted under Pooling of Interests method.

Number of shares to be issued by HN Ltd. for H Ltd.'s shareholders = 32,000 x 3/2 = 48,000 shares.

Since, the issue price is ₹ 12 per share, the Purchase Consideration is 48,000 x 12 = ₹ 5,76,000.

B. For N Ltd. the Net Assets Method is applied for determining the Purchase Consideration. Since, the assets are not taken over at book value, the amalgamation is accounted under Purchase method.

		₹
Assets taken over:		
Plant and Machinery	(10,00,000 less 15%)	8,50,000
Trade receivables		62,500
Inventory	(75,000 less 7,500)	67,500
Cash and Bank balance		50,000
Total Assets		10,30,000
Less: Liabilities		
Trade payables		(1,12,500)
Secured Debentures		(2,37,500)
Net Purchase Consideration		6,80,000

Discharge:		
Preference Shareholders	(3,75,000 x 2/3)	2,50,000
Equity Shareholders (bal. fig.)	(6,80,000-2,50,000)	4,30,000
		6,80,000

7. **Calculation of Average Due Date**

Taking Base Date 21.07.2016

Date of bill	*Period*	*Due Date*	*Amount*	*Number of Days from Base Date*	*Product*
			₹		₹
9.4.2016	4 months	12.08.2016	3,000	22	66,000
18.4.2016	3 months	21.07.2016	5,500	0	0
25.5.2016	6 months	28.11.2016	3,000	130	3,90,000
5.6.2016	3 months	8.09.2016	6,000	49	2,94,000
			17,500		7,50,000

$$\text{Average Due Date} = \text{21st July} + \frac{7,50,000}{17,500}$$ = 21.7.2016 + 43 days = 2.09.2016.

Since two new bills will be drawn, their due dates will be as follows:

First Bill- 1.7.2016 + 4 months = 4.11.2016;

Second Bill- 1.7.2016+ 6 months = 4.1.2017.

Interest to be charged in respect of the above bills:

1st bill = Interest will be charged on ₹ 10,000 @ 10% p.a. for 63 days (2.09.2016 to 4.11.2016)

= ₹ 10,000 x 10% x 63/365 = ₹ 172.60

2nd bill = Interest will be charged on ₹ 7,500 (₹ 17,500 - 10,000) @ 10% p.a. for 124 days (2.09.2016 to 4.1.2017)

= ₹ 7,500 x 10% x 124/365 = ₹ 254.80.

Therefore, the value of the two bills:

First bill = ₹ 10,000

Second bill = ₹ (7,500+ 172.60+ 254.80) = ₹ 7,927.4

8. **In the books of Mr. Perfact**

Mr. Smart in Account Current with Mr. Perfact

(Interest to 31st March, 2016 @ 12% p.a.)

(By means of product)

Date 2016	Particulars	Due Date	Amount ₹	Days	Product	Date 2016	Particulars	Due Date	Amount ₹	Days	Product
Jan 12	To Sales A/c	Feb. 1	30,000	59	17,70,000	Jan. 1	By Balance b/d	Jan. 1	3,500	91	3,18,500
Jan 31	To Sales A/c	Feb. 15	27,500	45	12,37,500	Feb. 15	By Cash A/c	Feb. 15	40,000	45	18,00,000
Mar. 31	To Interest $\frac{4,03,000}{366} \times \frac{12}{100}$		132			Feb. 20	By Cash A/c	Feb. 20	7,500	40	3,00,000
						Mar. 10	By Sales returns	Mar. 10	7,000	21	1,47,000
						Mar. 25	By Cash A/c	Mar. 25	6,500	6	39,000
Mar. 31	To Balance c/d		6,868			Mar. 31	By Balance of products				4,03,000
			64,500		30,07,500				64,500		30,07,500

9. **In Debtors Ledger**

General Ledger Adjustment Account

Particulars	₹	*Particulars*	₹
To Debtors Ledger Adjustment A/c:		To Debtors Ledger Adjustment A/c:	
Discount Allowed	3,000	Endorsed Bills receivable dishonoured	2,000
Bad Debts (4,400 + 600)	5,000		
Transfer to creditor ledger	2,200		

In Creditors Ledger

General Ledger Adjustment Account

Particulars	₹	*Particulars*	₹
To Creditors Leger Adjustment A/c:		By Creditors Ledger Adjustment A/c	
Endorsed Bills receivable dishonoured	2,000	Transfer from debtor ledger	2,200
		Bill receivable endorsed to creditors	8,000
		Discount received	1,200
		Allowances	6,400

Notes:

(i) The following items do not appear in GLA Account in Debtors Ledger.

1. Cash Sales
2. Provision *for* Doubtful Debts
3. Provision for Discount on Debtors
4. Bad Debts Recovered
5. Bills Receivable matured/collected on maturity
6. Bills Receivable discounted
7. Bills Receivable endorsed

(ii) The following items do not appear in GLA Account in Creditors Ledger

1. Cash Purchases
2. Reserve for Discount on Creditors
3. Bills Payable matured

10. **Balance Sheet of Krishna sports club as on 1st Jan., 2016**

Liabilities	₹	***Assets***	₹
Outstanding Rent for godown	6,000	Building	60,000
Advance Subscription	6,000	Stock of Sports Materials	5,000
Capital Fund *(Balancing Figure)*	2,71,000	Prepaid Insurance	3,000
		Outstanding Subscription	12,000
		12% General Fund Investments	2,00,000
		Cash Balance	1,000
	-	Bank Balance	2,000
	2,83,000		2,83,000

Balance Sheet of Krishna sports club as on 31st Dec. 2016

Liabilities	₹	₹	***Assets***		₹
Outstanding Rent		3,000	Building		
Advance Subscription		4,000	Book Value	60,000	
Advance Locker Rent		2,000	*Less:* Depreciation	6,000	54,000
Bank Overdraft		2,000	Furniture Cost	20,000	
Capital Fund:			*Less:* Depreciation	2,000	18,000
Opening Balance	2,71,000		Stock of Sports Materials		2,000
Add: Entrance Fees [20,000 x 40%]	8,000		Prepaid Insurance		6,000
Add: Life Membership Fees [₹ 20,000 x 60%]	12,000		Outstanding Subscription		8,000
Add: Surplus	60,000	3,51,000	Outstanding Locker Rent		6,000
			12% General Fund Investment		2,00,000
			Accrued interest on 12% General Fund Investments		4,000
			Cash Balance		64,000
		3,62,000			3,62,000

11. **Trading and Profit and Loss Account of Mr. Preet for the year ended 31st March, 2016**

		Amount			Amount
		₹			₹
To	Opening stock	1,60,000	By	Sales	13,98,000
To	Purchases (W.N.5)	9,12,000	By	Closing stock	1,40,000
To	Gross profit c/d (Bal.fig.)	4,66,000			
		15,38,000			15,38,000
To	Expenses (W.N.7)	3,44,000	By	Gross profit b/d	4,66,000
To	Discount allowed (W.N.9)	32,500	By	Discount received (W.N.10)	16,000
To	Depreciation on furniture (W.N.1)	13,000	By	Interest on Govt. Securities (W.N.8)	12,000
To	Net profit	1,14,500	By	Miscellaneous income	10,000
		5,04,000			5,04,000

Balance Sheet of Mr. Preet as on 31st March, 2016

Liabilities		Amount ₹	Assets	Amount ₹
Capital (W.N.6)	3,76,000		Furniture	1,27,000
Add: Additional capital (W.N.2)	1,72,000		12% Government Securities	2,00,000
			Accrued interest on Govt.	
Add: Profit during the year	1,14,500		securities (W.N.8)	12,000
	6,62,500		Debtors (W.N.3)	3,26,000
Less: Drawings	(1,40,000)	5,22,500	Bills Receivable (W.N.4)	35,000
Creditors		3,00,000	Stock	1,40,000
Outstanding expenses		36,000	Prepaid expenses	14,000
			Cash on hand	3,000
			Bank balance	1,500
		8,58,500		8,58,500

Working Notes:

1. **Furniture account**

		₹			₹
To	Balance b/d	1,20,000	By	Depreciation (bal.fig.)	13,000
To	Bank	20,000	By	Balance c/d	1,27,000
		1,40,000			1,40,000

2. **Cash and Bank account**

		₹			₹
To	Balance b/d		By	Creditors	7,84,000
	Cash	4,000	By	Drawings	1,40,000
	Bank	20,000	By	Furniture	20,000
To	Debtors	11,70,000	By	12% Govt. securities	2,00,000
To	Bill Receivable	1,22,500	By	Expenses	3,50,000
To	Miscellaneous income	10,000	By	Balance c/d	
To	Additional Capital (bal.fig.)	1,72,000		Cash	3,000
				Bank	1,500
		14,98,500			14,98,500

3. **Debtors account**

		₹			₹
To	Balance b/d	3,20,000	By	Cash and Bank	11,70,000
To	Creditors (Bills receivable dishonoured)	8,000	By	Discount	30,000
To	Sales (W.N.11)	13,98,000	By	Bills Receivable	2,00,000
			By	Balance c/d (bal.fig.)	3,26,000
		17,26,000			17,26,000

4. **Bills Receivable account**

		₹			₹
To	Debtors	2,00,000	By	Bank	1,22,500
			By	Discount	2,500
			By	Creditors	40,000
			By	Balance c/d (bal. fig.)	35,000
		2,00,000			2,00,000

5. Creditors account

	₹		₹
To Bank	7,84,000	By Balance b/d	2,20,000
To Discount	16,000	By Debtors (Bills receivable dishonoured)	8,000
To Bills receivable	40,000	By Purchases (bal. fig.)	9,12,000
To Balance c/d	3,00,000		
	11,40,000		11,40,000

6. Balance Sheet as on 1st April, 2015

Liabilities	₹	*Assets*	₹
Creditors	2,20,000	Furniture	1,20,000
Outstanding expenses	40,000	Debtors	3,20,000
Capital (balancing figure)	3,76,000	Stock	1,60,000
		Prepaid expenses	12,000
		Cash	4,000
		Bank balance	20,000
	6,36,000		6,36,000

7. Expenses incurred during the year

		₹
Expenses paid during the year		3,50,000
Add: Outstanding expenses as on 31.3.2016	36,000	
Prepaid expenses as on 31.3.2015	12,000	48,000
		3,98,000
Less: Outstanding expenses as on 31.3.2015	40,000	
Prepaid expenses as on 31.3.2016	14,000	(54,000)
Expenses incurred during the year		3,44,000

8. Interest on Government securities

2,00,000 x 12% x 6/12= ₹ 12,000

Interest on Government securities receivables for 6 months = ₹ 12,000

9. Discount allowed

		₹
Discount to Debtors	$\left(\frac{11,70,000}{97.5\%}\times 2.5\%\right)$	30,000
Discount on Bills Receivable	$\left(\frac{1,22,500}{98\%}\times 2\%\right)$	2,500
		32,500

10. Discount received

		₹
Discount to Creditors	$\left(\frac{7,84,000}{98\%}\times 2\%\right)$	16,000

11. Credit sales

Cost of Goods sold = Opening stock + Net purchases – Closing stock

= ₹ 1,60,000 + ₹ 9,12,000 – ₹ 1,40,000

= ₹ 9,32,000

Sales price = ₹ 9,32,000 + 50% of 9,32,000 = ₹ 13,98,000

12.

		₹
(i)	Price of two cars = ₹ 2,00,000 x 2	4,00,000
	Less: Depreciation for the first year @ 30%	1,20,000
		2,80,000
	Less: Depreciation for the second year = ₹ 2, 80,000 x $\frac{30}{100}$	84,000
	Agreed value of two cars taken back by the hire vendor	1,96,000
(ii)	Cash purchase price of one car	2,00,000
	Less: Depreciation on ₹ 2,00,000 @20% for the first year	40,000
	Written drown value at the end of first year	1,60,000
	Less: Depreciation on ₹ 1,60,000 @ 20% for the second year	32,000
	Book value of car left with the hire purchaser	1,28,000
(iii)	Book value of one car as calculated in working note (ii) above	1,28,000
	Book value of Two cars = ₹ 1,28,000 x 2	2,56,000

	Value at which the two cars were taken back, calculated in working note (i) above		1,96,000
	Hence, loss on cars taken back = ₹ 2,56,000 – ₹ 1,96,000 =		₹ 60,000
(iv)	Sale proceeds of cars repossessed		1,70,000
	Less: Value at which plant were taken back	₹ 1,96,000	
	Repair	₹ 10,000	2,06,000
	Loss on resale		36,000

13. Books of Muskaan Ltd.

Investment in 13.5% Debentures in Shorya Ltd. Account

(Interest payable on 31st March & 30th September)

Date	*Particulars*	*Nominal value ₹*	*Interest ₹*	*Amount ₹*	*Date*	*Particulars*	*Nominal value ₹*	*Interest ₹*	*Amount ₹*
2016					2016				
May 1	To Bank	5,00,000	5,625	5,19,375	Sept.30	By Bank (6 months Int)		50,625	
Aug.1	To Bank	2,50,000	11,250	2,45,000	Oct.1	By Bank	2,00,000		2,06,000
Oct.1	To P&L A/c			2,167					
Dec.31	To P&L A/c		52,313						
					Dec.31	By Balance c/d	5,50,000	18,563	5,60,542
		7,50,000	69,188	7,66,542			7,50,000	69,188	7,66,542

Note: Cost being lower than Market Value the debentures are carried forward at Cost.

Working Notes:

1. Interest paid on ₹ 5,00,000 purchased on May 1st, 2016 for the month of April 2016, as part of purchase price: 5,00,000 x 13.5% x 1/12 = ₹ 5,625

2. Interest received on 30th Sept. 2016

   On ₹ 5,00,000 = 5,00,000 x 13.5% x ½ = 33,750

   On ₹ 2,50,000 = 2,50,000 x 13.5% x ½ = 16,875

   Total ₹ 50,625

3. Interest paid on ₹ 2,50,000 purchased on Aug. 1st 2016 for April 2016 to July 2016 as part of purchase price:

   2,50,000 x 13.5% x 4/12 = ₹ 11,250

4. Loss on Sale of Debentures

Cost of acquisition

(₹ 5,19,375 + ₹ 2,45,000) x ₹ 2,00,000/₹ 7,50,000	=	2,03,833
Less: Sale Price (2000 x 103)	=	2,06,000
Profit on sale	=	₹ 2,167

5. Cost of Balance Debentures

(₹ 5,19,375 + ₹ 2,45,000) x ₹ 5,50,000/₹ 7,50,000 = ₹ 5,60,542

6. Interest on Closing Debentures for period Oct.-Dec. 2016 carried forward (accrued interest)

₹ 5,50,000 x 13.5% x 3/12 = ₹ 18,563

14. Statement of Claim

Items	***Cost (₹)***	***Depreciation (₹)***	***Salvage (₹)***	***Claim (₹)***
A	***B***	***C***	***D***	***(E=B-C-D)***
Stock (W.N. 2)	2,80,000		20,000	2,60,000
Buildings	3,75,000	1,25,000 + 9,375	4,000	2,36,625
Equipment	75,000	22,500 + 5,625	2,500	44,375
				5,41,000

Working Notes:

1. Memorandum Trading Account for the Period from 1.1.2016 to 30.6.2016

	₹		₹
To Opening Stock (1.1.2016)	1,50,000	By Sales	11,10,000
To Purchases	9,37,500		
To Cartage Inwards	17,500	By Closing Stock	2,80,000
To Wages	7,500	(Bal. Fig.)	
To Gross Profit (25% of ₹ 11,10,000)	2,77,500		
	13,90,000		13,90,000

2. Stock Destroyed Account

	₹		₹
To Trading Account	2,80,000	By Stock Salvaged Account	20,000
		By Balance c/d (For Claim)	2,60,000
	2,80,000		2,80,000

15. **Revaluation Account**

	₹			₹
To Buildings A/c	10,000	By Investments A/c		3,000
To Plant and Machinery A/c	26,000	By Loss to Partners:		
To Provision for Doubtful Debts A/c	27,800	P	30,400	
		Q	18,240	
		R	12,160	60,800
	63,800			63,800

Capital Accounts of Partners

Particulars	*P*	*Q*	*R*	*T*	*Particulars*	*P*	*Q*	*R*	*T*
	₹	₹	₹	₹		₹	₹	₹	₹
To Revaluation A/c	30,400	18,240	12,160	-	By Balance b/d	80,000	20,000	30,000	-
To Investments A/c	-	15,000	-	-	By Reserves A/c	10,000	6,000	4,000	-
To Q's Loan A/c	-	22,760	-	-	By R and T's Capital A/c	10,000	30,000	-	-
To P and Q's Capital A/c			20,000	20,000	By Bank A/c (balancing figure)	10,400	-	78,160	60,000
To Balance c/d	80,000	-	80,000	40,000					
	1,10,400	56,000	1,12,160	60,000		1,10,400	56,000	1,12,160	60,000

Bank Account

	₹		₹
To P's capital A/c	10,400	By Bank Overdraft A/c	44,000
To R's capital A/c	78,160	By Balance c/d	1,04,560
To T's capital A/c	60,000		
	1,48,560		1,48,560

Balance Sheet of NEHA Co.

as at 1st April, 2016

Liabilities		₹	*Assets*	₹
Capital Accounts:			Land	10,000
P	80,000		Buildings	1,90,000
Q	80,000		Plant and Machinery	1,04,000

R 40,000	2,00,000	Furniture	43,000
Long Term Debts	3,00,000	Inventories	1,30,000
Trade payables	1,70,000	Trade receivables 1,39,000	
Q's Loan Account	22,760	*Less:* Provision for Doubtful Debts (27,800)	1,11,200
		Balance at Bank	1,04,560
	6,92,760		6,92,760

16. Recently a growing trend has developed for outsourcing the accounting function to a third party. The consideration for doing this is to save cost and to utilise the expertise of the outsourced party. The third party maintains the accounting software and the client data, does the processing and hands over the report from time to time.

Benefits of outsourcing the accounting function to a third party:

1. **Saving of Time:** The organisation that outsources its accounting function is able to save time to concentrate on the core area of business activity.
2. **Expertise of the third party:** The organisation is able to utilise the expertise of the third party in undertaking the accounting work.
3. **Maintenance of data:** Storage and maintenance of the data is in the hand of professional people.
4. **Economical:** The organisation is not bothered about people leaving the organization in key accounting positions. The proposition is proving to be economically and more sensible as they do not have train the people again. Hence, the training cost is saved.

The choice of outsourcing vendor is made on the basis of the proposals received from these vendors. The proposals are evaluated and the decision is often taken based on the following criteria:

1. The type of services provided and whether the same matches with the requirements.
2. The reputation and background of the vendor.
3. The comparative costs of the various propositions.
4. The assurance of quality.

17. (a) The question deals with the issue of Applicability of Accounting Standards to a non-corporate entity. For availment of the exemptions, first of all, it has to be seen that M/s X& Co. falls in which level of the non-corporate entities. Its classification will be done on the basis of the classification of non-corporate entities as prescribed by the ICAI. According to the ICAI, non-corporate entities can be classified under 3 levels viz Level I, Level II (SMEs) and Level III (SMEs).

An entity whose turnover (excluding other income) does not exceed rupees fifty crore in the immediately preceding accounting year, will fall under the category of Level I entities. Non-corporate entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities:

(i) All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees one crore but does not exceed rupees fifty crore in the immediately preceding accounting year.

(ii) All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees one crore but not in excess of rupees ten crore at any time during the immediately preceding accounting year.

(iii) Holding and subsidiary entities of any one of the above.

As the turnover of M/s X& Co. is more than ₹ 1 crore, it falls under 1st criteria of Level II non-corporate entities as defined above. Even if its borrowings of ₹ 0.95 crores is less than ₹ 1 crores, it will be classified as Level II Entity. In this case, AS 3, AS 17, AS 21, AS 23, AS 27 will not be applicable to M/s X & Co. Relaxations from certain requirements in respect of AS 15, AS 19, AS 20, AS 25, AS 28 and AS 29 are also available to M/s X& Co.

(b) The decision of making provision for non-moving stocks on the basis of technical evaluation does not amount to change in accounting policy. Requirement to provide for non-moving stocks may be said as accounting policy but the basis for making provision will not constitute accounting policy. It will be considered as an accounting estimate. Further, the method of estimating the amount of provision may be changed in case a more prudent estimate can be made**.**

In the given case, considering the total value of stock, the change in the amount of required provision of non-moving stock from ₹ 3.5 lakhs to ₹ 2.5 lakhs is also not material. The disclosure can be made for such change in the following lines by way of notes to the accounts in the annual accounts of Mini Ltd. for the year 2015-16:

"The company has provided for non-moving stocks on the basis of technical evaluation unlike preceding years. Had the same method been followed as in the previous year, the profit for the year and the corresponding effect on the year end net assets would have been higher by ₹ 1 lakh."

18. (a) Calculation of cost of closing inventory

Particulars	**₹**
Opening Inventory	50,000
Purchases less returns (₹3,60,000 –₹ 10,000)	3,50,000

Freight Inwards	10,000
	4,10,000
Less: Net Sales (₹ 4,50,000 –₹ 11,250)	(4,38,750)
	(28,750)
Add: Gross Profits (₹ 4,38,750 x 20%)	87,750
Closing Inventory	59,000

(b) Case (a)

The company considers that the residual value, based on prices prevailing at the balance sheet date, will equal the cost.

There is, therefore, no depreciable amount and depreciation is zero.

Case (b)

The company considers that the residual value, based on prices prevailing at the balance sheet date, will be ₹ 9,00,000 and the depreciable amount is, therefore, ₹ 1,00,000.

Annual depreciation (on a straight line basis) will be ₹ 5,000 [{10,00,000 – 9,00,000} ÷ 20].

19. (a) According to para 14 of AS 7 (Revised) 'Construction Contracts', incentive payments are additional amounts payable to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to the contractor for early completion of the contract. Incentive payments are included in contract revenue when: (i) the contract is sufficiently advanced that it is probable that the specified performance standards will be met or exceeded; and (ii) the amount of the incentive payment can be measured reliably. In the given problem, the contract has not even begun and hence the contractor (Mr. Mehta) should not recognize any revenue of this contract.

(b) 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. K Ltd. should record the sale and recognize the profit of ₹ 20 lakhs in its profit and loss account. The building should be eliminated from the balance sheet.

20. (a) Constructing or acquiring a new asset may result in incremental costs that would have been avoided if the asset had not been constructed or acquired. These costs are not be included in the cost of the asset if they are not directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

Conclusion: The costs to be incurred by the company do not meet that requirement of AS 10 and cannot, therefore, be capitalised.

(b) As per AS 13 'Accounting for Investments', the accounting standard is not applicable to Bank, Insurance Company, Mutual Funds. In this case Z Bank is a bank, therefore, AS 13 does not apply to it. For banks, the RBI has issued guidelines for classification and valuation of its investment and Z Bank should comply with those RBI Guidelines/Norms. Therefore, though Z Bank has not followed the provisions of AS 13, yet it would not be said as non-compliance since, it is complying with the norms stipulated by the RBI.

ANNEXURE

AS 10: PROPERTY, PLANT AND EQUIPMENT

1. Introduction

The objective of this Standard is to prescribe Accounting treatment for Property, Plant and Equipment (PPE). The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them.

2. Scope of the Standard

As a general principle, AS 10 should be applied in accounting for PPE.

Exception:

When another Accounting Standard requires or permits a different accounting treatment.

This Standard does not apply to:

AS 10
Not Applicable to

- Biological Assets (***other than Bearer Plants***) Related to agricultural activity
- Wasting Assets including Mineral rights, Expenditure on the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources

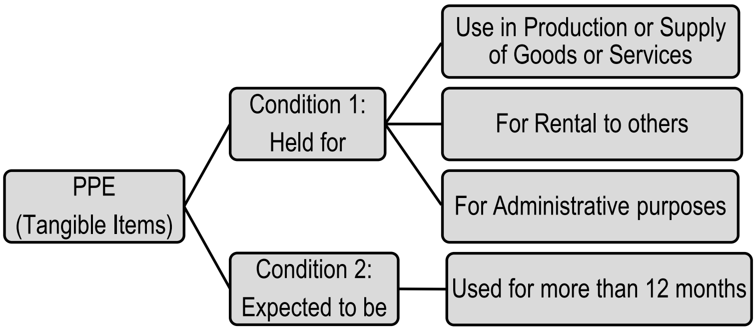
Note: AS 10 applies to Bearer Plants but it does not apply to the produce on Bearer Plants.

Clarifications:

1. AS 10 applies to PPE used to **develop or maintain** the assets described above.
2. Investment property (defined in AS 13), should be accounted for only in accordance with the **Cost model prescribed in this standard.**

3. Definition of Property, Plant and Equipment (PPE)

There are 2 conditions to be satisfied for a TANGIBLE item to be called PPE. PPE are ***tangible items*** that:



Note: Intangible items are covered under AS 26 which is not covered in syllabus of Paper 1 .

"Administrative purposes": The term 'Administrative purposes' has been used in **wider sense** to ***include all business purposes.*** **Thus, PPE would include assets used for:**

- Selling and distribution
- Finance and accounting
- Personnel and other functions

of an Enterprise.

Items of PPE may also be acquired for **safety or environmental reasons.**

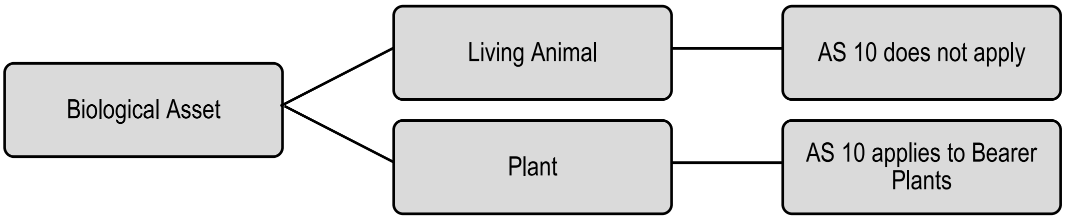
The acquisition of such PPE, although not directly increasing the future economic benefits of any particular existing item of PPE, may be necessary for an enterprise to obtain the future economic benefits from its other assets.

Such items of PPE qualify for recognition as assets because they enable an enterprise to derive future economic benefits from related assets in excess of what could be derived had those items not been acquired.

Example: A chemical manufacturer may install new chemical handling processes to comply with environmental requirements for the production and storage of dangerous chemicals; related plant enhancements are recognised as an asset because without them the enterprise is unable to manufacture and sell chemicals.

4. Other Definitions

1. **Biological Asset:** An Accounting Standard on "Agriculture" is under formulation, which will, inter alia, cover accounting for livestock. Till the time, the Accounting Standard on "Agriculture" is issued, accounting for livestock meeting the definition of PPE, will be covered as per AS 10 (Revised).



2. Bearer Plant:Is a plant that (satisfies all 3 conditions):

Is used in the production or supply	• Of Agricultural produce
Is expected to bear produce	• For more than a period of 12 months
Has a remote likelihood of being sold as Agricultural produce	• Except for incidental scrap sales

Note: When bearer plants are no longer used to bear produce they might be cut down and sold as scrap. For example - use as firewood. Such incidental scrap sales would not prevent the plant from satisfying the definition of a Bearer Plant.

The following are not Bearer Plants:

(a) Plants cultivated to be ***harvested*** *as* Agricultural produce

Example: Trees grown for use as lumber

(b) Plants cultivated ***to produce*** Agricultural produce when there is more than a remote likelihood that the entity will ***also harvest and sell*** the plant as agricultural produce, other than as incidental scrap sales

Example: Trees which are cultivated both for their fruit and their lumber

(c) Annual crops

Example: Maize and wheat

Agricultural Produce is the **harvested product** of **Biological Assets** of the enterprise.

3. Agricultural Activity: Is the **management** by an Enterprise of:

- Biological transformation; and
- Harvest of Biological Assets
- For sale, Or
- For conversion into Agricultural Produce, Or
- Into additional Biological Assets

5. Recognition Criteria for PPE

The ***cost of an item of PPE*** should be recognised as an asset ***if, and only if***:

(a) It is probable that future economic benefits associated with the item will flow to the enterprise, and

(b) The cost of the item can be measured reliably.

Notes:

1. It may be **appropriate to aggregate individually insignificant items**, such as moulds, tools and dies and to apply the criteria to the aggregate value.
2. An enterprise **may decide to expense an item** which could otherwise have been included as PPE, because the amount of the expenditure is not material.

When do we apply the above criteria for Recognition?

An enterprise evaluates under this recognition principle all its costs on **PPE at the time they are incurred.**

6. Treatment of Spare Parts, Stand by Equipment and Servicing Equipment

Case I **If they meet the definition of PPE as per AS 10:**

- Recognised as PPE as per AS 10

Case II **If they do not meet the definition of PPE as per AS 10:**

- Such items are classified as Inventory as per AS 2

7. Treatment of Subsequent Costs

Cost of day-to-day servicing

Meaning:

Costs of day-to-day servicing are primarily the costs of labour and consumables, and may include the cost of small parts. The purpose of such expenditures is often described as for the **'Repairs and Maintenance'** of the item of PPE.

Accounting Treatment:

An enterprise does not recognise in the carrying amount of an item of PPE the costs of the day-to-day servicing of the item. Rather, these costs are recognised in the Statement of Profit and Loss as incurred.

Replacement of Parts of PPE

Parts of some items of PPE may require replacement at regular intervals.

Examples:

1. A furnace may require relining after a specified number of hours of use.
2. Aircraft interiors such as seats and galleys may require replacement several times during the life of the airframe.
3. Major parts of conveyor system, such as, conveyor belts, wire ropes, etc., may require replacement several times during the life of the conveyor system.
4. Replacing the interior walls of a building, or to make a non-recurring replacement.

Accounting Treatment:

An enterprise recognises in the carrying amount of an item of PPE the cost of replacing part of such an item when that cost is incurred if the recognition criteria are met.

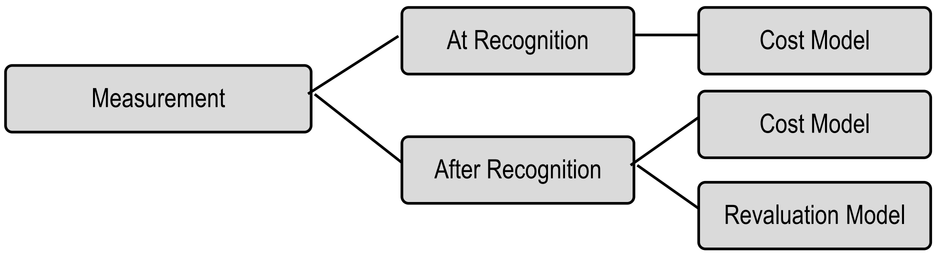
Note: The carrying amount of those parts that are **replaced is derecognised** in accordance with the de-recognition provisions of this Standard.

Regular Major Inspections - Accounting Treatment

When each major inspection is performed, its cost is recognised in the carrying amount of the item of PPE as a replacement, if the recognition criteria are satisfied.

Any remaining carrying amount of the cost of the previous inspection (as distinct from physical parts) is derecognised.

8. Measurement of PPE

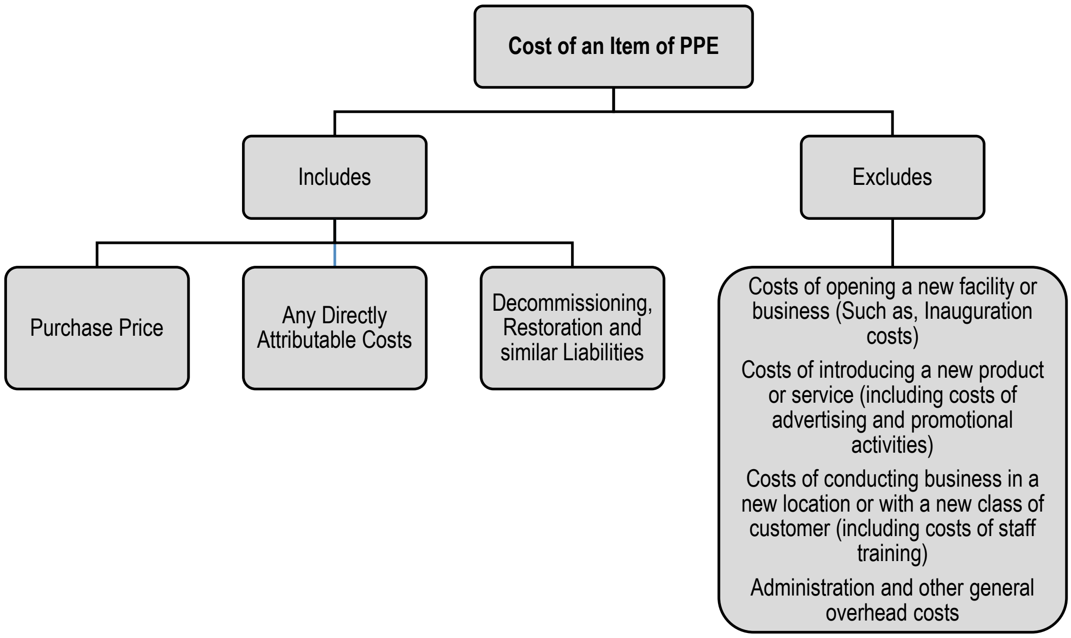


9. Measurement at Recognition

An item of PPE that qualifies for recognition as an asset should be measured **at its cost.**

What are the elements of Cost?

Cost of an item of PPE comprises:



Examples of directly attributable costs are:

1. Costs of employee benefits (as defined in AS 15) arising directly from the construction or acquisition of the item of PPE
2. Costs of site preparation
3. Initial delivery and handling costs
4. Installation and assembly costs
5. Costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment)
6. Professional fees

The following costs are not included in the carrying amount of an item of PPE:

1. Costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity.
2. Initial operating losses, such as those incurred while demand for the output of an item builds up. And
3. Costs of relocating or reorganising part or all of the operations of an enterprise.

Example: Income may be earned through using a building site as a car park until construction starts because incidental operations are not necessary to bring an item to the location and condition necessary for it to be capable of operating in the manner intended by management, the income and related expenses of incidental operations are recognised in the Statement of Profit and Loss and included in their respective classifications of income and expense.

C. Decommissioning, Restoration and similar Liabilities:

Initial estimate of the costs of dismantling, removing the item and restoring the site on which it is located, referred to as 'Decommissioning, Restoration and similar Liabilities', the obligation for which an enterprise incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes **other than** to produce inventories during that period.

Exception: An enterprise applies AS 2 "Valuation of Inventories", to the costs of obligations for dismantling, removing and restoring the site on which an item is located that are incurred during a particular period as a consequence of having used the item to produce inventories during that period.

Note: The obligations for costs accounted for in accordance with AS 2 or AS 10 are recognised and measured in accordance with AS 29* "Provisions, Contingent Liabilities and Contingent Assets".

** AS 29 is not covered in syllabus of paper-1*

10. Cost of a Self-constructed Asset

Cost of a self-constructed asset is determined using the same principles as for an acquired asset.

1. If an enterprise makes similar assets for sale in the normal course of business, the cost of the asset is usually the same as the cost of constructing an asset for sale (see AS 2). Therefore, any **internal profits are eliminated** in arriving at such costs.

2. Cost of **abnormal amounts** of wasted material, labour, or other resources incurred in self constructing an asset is **not included** in the cost of the asset.

3. AS 16* on Borrowing Costs, establishes criteria for the **recognition of interest** as a component of the carrying amount of a self-constructed item of PPE.

4. **Bearer plants** are accounted for in the same way as self-constructed items of PPE before they are in the location and condition necessary to be capable of operating in the manner intended by management.

11. Measurement of Cost

Cost of an item of PPE is the **cash price equivalent** at the recognition date.

A. If payment is deferred beyond normal credit terms:

Total payment - Cash price equivalent

- Is recognised as Interest over the period of credit
- unless such interest is capitalised in accordance with AS 16*

B. PPE acquired in Exchange for a Non-monetary Asset or Assets Or A combination of Monetary and Non-monetary Assets:

Cost of such an item of PPE is **measured at fair value unless:**

(a) Exchange transaction lacks commercial substance; Or

(b) Fair value of neither the asset(s) received nor the asset(s) given up is reliably measurable.

Note:

1. The acquired item(s) is/are measured in this manner even if an enterprise cannot immediately derecognise the asset given up.
2. If the acquired item(s) is/are not measured at fair value, its/their cost is measured at the carrying amount of the asset(s) given up.

C. PPE purchased for a Consolidated Price:

Where several items of PPE are purchased for a consolidated price, the consideration is apportioned to the various items on the basis of their respective fair values at the date of acquisition.

Note: In case the fair values of the items acquired cannot be measured reliably, these values are estimated on a fair basis as determined by competent valuers.

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* *AS 16 is not covered in syllabus of paper-1*

12. Measurement after Recognition

An enterprise should choose

- **Either** Cost model,
- **Or** Revaluation model

as its accounting policy and should apply that policy to an entire **class of PPE**.

Class of PPE: A class of PPE is a grouping of assets of a **similar nature and use** in operations of an enterprise.

Examples of separate classes:

(a) Land

(b) Land and Buildings

(c) Machinery

(d) Ships

(e) Aircraft

(f) Motor Vehicles

(g) Furniture and Fixtures

(h) Office Equipment

(i) Bearer plants

Cost Model

After recognition as an asset, an item of PPE should be carried at:

Cost **-** Any Accumulated Depreciation **-** Any Accumulated Impairment losses

Revaluation Model

After recognition as an asset, an item of PPE whose fair value can be measured reliably should be carried at a revalued amount.

Fair value at the date of the revaluation	-
Less: Any subsequent accumulated depreciation	(-)
Less: Any subsequent accumulated impairment losses	(-)
Carrying value	=

Revaluation for entire class of PPE

If an item of PPE is revalued, the entire class of PPE to which that asset belongs should be revalued.

Frequency of Revaluations

Revaluations should be made with **sufficient regularity** to ensure that the carrying amount does not differ materially from that which would be determined using Fair value at the Balance Sheet date.

The frequency of revaluations depends upon the changes in fair values of the items of PPE being revalued.

When the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is required.

A. Items of PPE experience significant and volatile changes in Fair value

Annual revaluation shall be done.

B. Items of PPE with only insignificant changes in Fair value

Revaluation shall be done at an interval of 3 or 5 years.

Determination of Fair Value

Fair value of items of PPE is usually determined from **market-based evidence** by appraisal that is normally undertaken by professionally qualified valuers.

If there is **no market-based evidence** of fair value because of the specialised nature of the item of PPE and the item is rarely sold, except as part of a continuing business, an enterprise may need to estimate fair value using an income approach.

Example:

Based on

- Discounted cash flow projections, Or
- A depreciated replacement cost approach

Which aims at making a **realistic estimate of the current cost** of acquiring or constructing an item that has the same service potential as the existing item.

13. Accounting Treatment of Revaluations

When an item of PPE is revalued, the carrying amount of that asset is adjusted to the revalued amount.

At the date of the revaluation, the asset is treated in one of the following ways:

A. Technique 1: Gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset.

Gross carrying amount

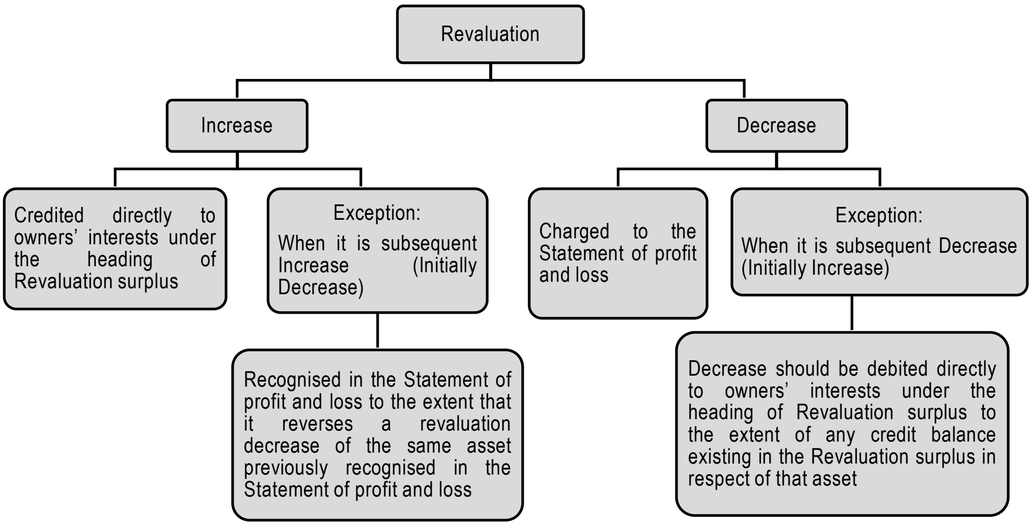
- May be restated by reference to observable market data, or
- May be restated proportionately to the change in the carrying amount.

Accumulated depreciation at the date of the revaluation is

- Adjusted to equal the difference between the gross carrying amount and the carrying amount of the asset after taking into account accumulated impairment losses

B. Technique 2: Accumulated depreciation Is eliminated against the Gross Carrying amount of the asset

Revaluation - Increase or Decrease



Treatment of Revaluation Surplus

The revaluation surplus included in owners' interests in respect of an item of PPE may be transferred to the **Revenue Reserves when the asset is derecognised.**

Case I : When whole surplus is transferred:

When the asset is:

- Retired; Or
- Disposed of

Case II : Some of the surplus may be transferred as the asset is used by an enterprise:

In such a case, the amount of the surplus transferred would be:

Depreciation (based on Revalued Carrying amount) – Depreciation (based on Original Cost)

Transfers from Revaluation Surplus to the Revenue Reserves are **not made** through the Statement of Profit and Loss.

14. Depreciation

Component Method of Depreciation:

Each part of an item of PPE with a cost that is **significant in relation to the total cost** of the item should be depreciated separately.

Depreciable Amount and Depreciation Period

What is "Depreciable Amount"?

Depreciable amount is:

Cost of an asset (or other amount substituted for cost i.e. revalued amount) - Residual value

The depreciable amount of an asset should be **allocated on a systematic basis** over its useful life.

Review of Residual Value and Useful Life of an Asset

Residual value and the useful life of an asset should be reviewed **at least at each financial year-end** and, if expectations differ from previous estimates, the change(s) should be accounted for as a **change in an accounting estimate**.

Note: Depreciation is recognised even if the Fair value of the Asset exceeds its Carrying Amount. Repair and maintenance of an asset do not negate the need to depreciate it.

Commencement of period for charging Depreciation

Depreciation of an asset begins when it is **available for use**, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by the management.

Cessesation of Depreciation

I. Depreciation ceases to be charged when asset's residual value exceeds its carrying amount

The residual value of an asset may increase to an amount equal to or greater than its carrying amount. If it does, depreciation charge of the asset is zero **unless and until** its residual value subsequently decreases to an amount below its carrying amount.

II. Depreciation of an asset ceases at the earlier of:

- The date that the asset is retired from active use and is held for disposal, and
- The date that the asset is derecognised

Therefore, depreciation does not cease when the asset becomes idle or is retired from active use (but not held for disposal) unless the asset is fully depreciated.

However, under usage methods of depreciation, the depreciation charge can be zero while there is no production.

Land and Buildings

Land and buildings are separable assets and are accounted for separately, **even when they are acquired together.**

A. Land: Land has an unlimited useful life and therefore is not depreciated.

Exceptions: Quarries and sites used for landfill.

Depreciation on Land:

I. If land itself has a limited useful life:

It is depreciated in a manner that reflects the benefits to be derived from it.

II. **If the cost of land includes the costs of site dismantlement, removal and restoration:**

That **portion of the land asset** is depreciated over the period of benefits obtained by incurring those costs.

B. Buildings:

Buildings have a limited useful life and therefore are depreciable assets.

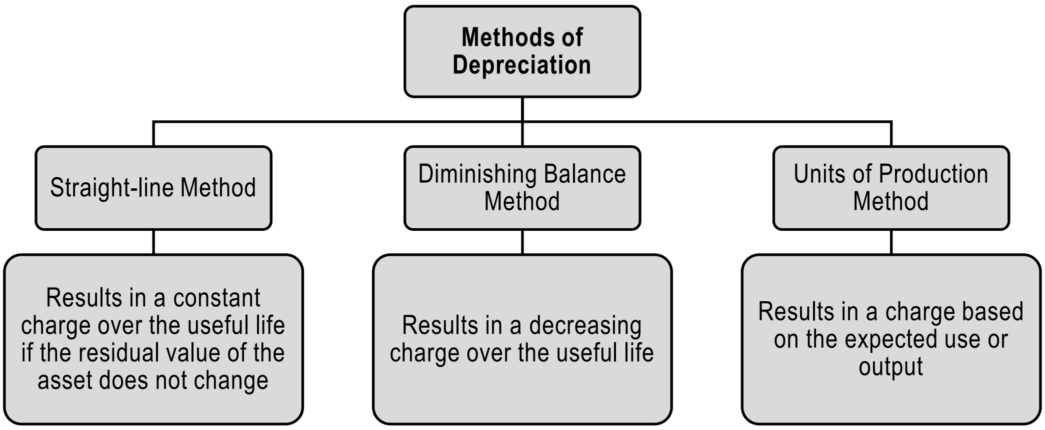
An increase in the value of the land on which a building stands does not affect the determination of the depreciable amount of the building.

15. Depreciation Method

The depreciation method used should **reflect the pattern in which the future economic benefits** of the asset are expected to be consumed by the enterprise.

The method selected is applied **consistently from period to period** unless:

- There is a change in the expected pattern of consumption of those future economic benefits; Or
- That the method is changed in accordance with the statute to best reflect the way the asset is consumed.



Review of Depreciation Method:

The depreciation method applied to an asset should be reviewed at **least at each financial year-end** and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method should be changed to reflect the changed pattern.

Such a change should be accounted for as a **change in an accounting estimate** .

Depreciation Method based on Revenue:

A depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is **not appropriate.**

16. Changes in Existing Decommissioning, Restoration and other Liabilities

The cost of PPE may undergo changes subsequent to its acquisition or construction on account of:

- Changes in Liabilities
- Price Adjustments
- Changes in Duties
- Changes in initial estimates of amounts provided for Dismantling, Removing, Restoration, and
- Similar factors

The above are **included in the cost of the asset.**

17. Retirements

Items of PPE retired from active use and held for disposal should be stated at the lower of:

- Carrying Amount, and
- Net Realisable Value

Note: Any write-down in this regard should be recognised immediately in the Statement of Profit and Loss.

18. De-recognition

The carrying amount of an item of PPE should be derecognised:

- On disposal
    - By sale
    - By entering into a finance lease, or
    - By donation, Or
- When no future economic benefits are expected from its use or disposal

19. Disclosure

General Disclosures:

The financial statements should disclose, for each class of PPE:

(a) The measurement bases (i.e., cost model or revaluation model) used for determining the gross carrying amount;

(b) The depreciation methods used;

(c) The useful lives or the depreciation rates used.

In case the useful lives or the depreciation rates used are different from those specified in the statute governing the enterprise, it should make a specific mention of that fact;

(d) The gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period; and

(e) A reconciliation of the carrying amount at the beginning and end of the period showing:

Additional Disclosures:

The financial statements should also disclose:

(a) The existence and amounts of restrictions on title, and property, plant and equipment pledged as security for liabilities;

(b) The amount of expenditure recognised in the carrying amount of an item of property, plant and equipment in the course of its construction;

(c) The amount of contractual commitments for the acquisition of property, plant and equipment;

(d) If it is not disclosed separately on the face of the statement of profit and loss, the amount of compensation from third parties for items of property, plant and equipment that were impaired, lost or given up that is included in the statement of profit and loss; and

(e) The amount of assets retired from active use and held for disposal.

Disclosures related to Revalued Assets:

If items of property, plant and equipment are stated at revalued amounts, the following should be disclosed:

(a) The effective date of the revaluation;

(b) Whether an independent valuer was involved;

(c) The methods and significant assumptions applied in estimating fair values of the items;

(d) The extent to which fair values of the items were determined directly by reference to observable prices in an active market or recent market transactions on arm's length terms or were estimated using other valuation techniques; and

(e) The revaluation surplus, indicating the change for the period and any restrictions on the distribution of the balance to shareholders.

20. Transitional Provisions

Previously Recognised Revenue Expenditure

Where an entity has in past recognized an expenditure in the Statement of Profit and Loss which is eligible to be included as a part of the cost of a project for construction of PPE in accordance with the requirements of this standard:

- It may do so **retrospectively** for such a project.

Note: The effect of such retrospective application, should be recognised **net-of-tax in Revenue reserves**.

PPE acquired in Exchange of Assets

The requirements of AS 10 regarding the initial measurement of an item of PPE acquired in an exchange of assets transaction should be **applied prospectively** only to transactions entered into after this Standard becomes mandatory.

Spare parts

On the date of this Standard becoming mandatory, the spare parts, which hitherto were being treated as inventory under AS 2, and are **now required to be capitalised** in accordance with the requirements of this Standard, should be capitalised at their respective carrying amounts.

Note: The spare parts so capitalised should be depreciated over their remaining useful lives prospectively as per the requirements of this Standard.

Revaluations

The requirements of AS 10 regarding the revaluation model should be **applied prospectively.**

In case, on the date of this Standard becoming mandatory, an enterprise **does not adopt** the revaluation model as its accounting policy but the carrying amount of item(s) of PPE reflects any previous revaluation it should adjust the amount outstanding in the Revaluation reserve against the carrying amount of that item.

Note: The carrying amount of that item should never be less than residual value. Any excess of the amount outstanding as Revaluation reserve over the carrying amount of that item **should be adjusted** in Revenue reserves.

PAPER – 2: BUSINESS LAW, ETHICS & COMMUNICATION

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR MAY, 2017 EXAMINATION

I. Applicability for May 2017 examinations

The Study Material (July 2015 edition), Practice Manual (April 2016 edition) along with the "Supplementary Study Paper 2016 for Paper 2: Business Law, Ethics and Communication" is relevant for May 2017 examinations. Supplementary Study Paper 2016 contains all relevant amendments/ circulars/ notifications etc. in the Business and the Company law part made from 1st May 2015 to 30th April, 2016. Further, all relevant amendments/ circulars/ notifications etc. in the Company law part for the period 1st May 2016 to 31st October, 2016 are mentioned below:

1. The Ministry of Corporate Affairs (MCA) vide Notification G.S.R. 639(E) dated 29th June, 2016, has amended the Companies (Acceptance of Deposits) Rules, 2014 through Companies (Acceptance of Deposits) Amendment Rules, 2016, wherein the key changes are:

Rule 16A – Disclosures in the financial statement has been inserted which provides,

"(1) Every company, **other than a private company**, shall disclose in its financial statement, by way of notes, about the money received from the director.

(2) **Every private company** shall disclose in its financial statement, by way of notes, about the money received from the directors, or relatives of directors."

[Refer Para 2.2, Page 6.62 of the SM (July 2015 edition)]

2. The MCA vide Notification G.S.R. 704(E) dated 19th July, 2016, has amended the Companies (Share Capital and Debentures) Rules, 2014 through Companies (Share Capital and Debentures) Third Amendment Rules, 2016, wherein the key changes have been made in Rule 8 (4) which deals with the issue of equity shares. The change is:

In rule 8, in sub-rule (4), after the first proviso, the following proviso shall be inserted, namely:-

"Provided further that a startup company, as defined in notification number GSR 180(E) dated 17th February, 2016 issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India, may issue sweat equity shares not exceeding fifty per cent of its paid up capital upto five years from the date of its incorporation or registration."

[Refer Para 3.11, Page 6.89 of the SM (July 2015 edition)]

3. The MCA vide Notification G.S.R. 743(E) dated 27th July, 2016, has amended the Companies (Incorporation) Rules, 2014 through Companies (Incorporation) Third Amendment Rules, 2016, wherein the key changes are pertaining to OPC, Particulars of subscibers to be filed with the Registrar at the time of incorporation, publication of name of company and alteration of memorandum due to change of name:

(i) In rule 3, for sub-rule (2), the following shall be substituted, namely:-

"A **natural person shall not be member of more than** a **One Person Company** at any point of time and the said person shall not be a nominee of more than a One Person Company"

[Refer Para 1.6, Page 6.17 for relevant Rule in SM]

(ii) In rule16, in sub-rule (1),-

in clause (m), the following Explanation shall be inserted, namely:-

"Explanation.- In case the subscriber is already holding a valid DIN, and the particulars provided therein have been updated as on the date of application, and the declaration to this effect is given in the application, the proof of identity and residence need not be attached.";

[Refer Para 1.6, Page 6.18 for relevant Rule in SM]

(iii) Rule 26 shall be substituted by:

"26. **Publication of name by company**.-

(1) Every company which has a website for conducting online business or otherwise, shall disclose/publish its name, address of its registered office, the Corporate Identity Number, Telephone number, fax number if any, email and the name of the person who may be contacted in case of any queries or grievances on the landing/home page of the said website.

(2) The Central Government may as and when required, notify the other documents on which the name of the company shall be printed."

[Refer Page 6.23 for relevant Rule in SM]

(iv) In rule 29, for sub-rule (1), the following shall be substituted, namely:-

"(1) The change of name shall not be allowed to a company which has not filed annual returns or financial statements due for filing with the Registrar or which has failed to pay or repay matured deposits or debentures or interest thereon:

Provided that the change of name shall be allowed upon filing necessary documents or payment or repayment of matured deposits or debentures or interest thereon as the case may be."

[Refer Para 1.8, Page 6.29 for relevant Rule in SM]

4. The MCA vide Notification G.S.R. 908(E) dated 23rd September, 2016, has amended the Companies (Management and Administration) Rules, 2014 through Companies (Management and Administration) Amendment Rules, 2016, wherein the key changes are with respect to Return of changes in shareholding position of promoters and top ten shareholders, calling of Extra Ordinary General meeting by requistionists, voting through electronic means and procedure to be followed for conducting business through postal ballot. The changes are:

(i) For rule 13 the following rule shall be substituted, namely:-

"Every listed company shall file with the Registrar, a return in Form No. MGT.10, with respect to changes in the shareholding position of promoters and top ten shareholders of the company, in each case, representing increase or decrease by two per cent or more of the paid-up share capital of the company, within fifteen days of such change."

[Refer Para 4.16, Page 6.125 for relevant Rule (SM July 2015 edition)]

(ii) In rule 17, in sub-section (2), in the Explanation, for the words "on working day", the words "on any day except national holiday" shall be substituted.

[Refer Page 6.131 point (2) for relevant Rule (SM July 2015 edition)]

(iii) In rule 20, for sub-rule (2), the following sub-rule shall be substituted, namely:-

"Every company which has listed its equity shares on a recognised stock exchange and every company having not less than one thousand members shall provide to its members facility to exercise their right to vote on resolutions proposed to be considered at a general meeting by electronic means:

Provided that a Nidhi, or an enterprise or institutional investor referred to in Chapter XB or Chapter XC of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009 is not required to provide the facility to vote by electronic means:

Explanation.- For the purpose of this sub-rule, "Nidhi" means a company which has been incorporated as a Nidhi with the object of cultivating the habit of thrift and savings amongst its members, receiving deposits from and lending to, its members only, for their mutual benefit, and which complies with such rules as are prescribed by the Central Government for regulation of such class of companies."

[Refer Para 4.10, Page 6.149 for relevant Rule (SM July 2015 edition)]

(iv) In rule 22, sub-rule (7) and sub-rule (14) shall be omitted.

Sub- Rule 7 dealt with "If a resolution is assented to by the requisite majority of the shareholders by means of postal ballot including voting by electronic means, it shall be deemed to have been duly passed at a general meeting convened in that behalf"

Sub – Rule 14 dealt with "The resolution shall be deemed to be passed on the date of at a meeting convened in that behalf".

[Refer Para 4.13, Page 6.164, point (5) & point (12) for relevant Rule (SM July 2015 edition)]

5. The MCA vide Notification G.S.R. 936(E) dated 1st October, 2016, has amended the Companies (Incorporation) Rules, 2014 through Companies (Incorporation) Fourth Amendment Rules, 2016, wherein the key changes are made by introducing Simplified Proforma for Incorporating Company Electronically (SPICe):

Simplified Proforma for Incorporating Company Electronically (SPICe)

The Ministry of Corporate Affairs has taken various initiatives for ease of business. In a step towards easy setting up of business, MCA has simplified the process of filing of forms for incorporation of a company through Simplified Proforma for incorporating company electronically.

Following are the steps for SPICe:

(1) The application for allotment of Director Identification Number upto three Directors, reservation of a name, incorporation of company and appointment of Directors of the proposed company shall be filed in Integrated Form No. INC-32, for One Person Company, Private company, Public Company and Producer Company, with the Registrar within whose jurisdiction the registered office of the company is proposed to be situated, alongwith the fee of rupees two thousand in addition to the registration fee as specified in Companies (Registration of Offices and Fees) Rules, 2014.

(2) For the purposes of filing Integrated Incorporation form, the particulars of maximum of three directors shall be allowed to be filed in INC-32 and allotment of Director Identification Number of maximum of three proposed directors shall be permitted in Form INC-32 in case of proposed directors not having approved Director Identification Number.

(3) The promoter or applicant of the proposed company shall propose only one name in e-form No. INC-32.

(4) The promoter or applicant of the proposed company may prepare Memorandum of Association as per templates in Form INC-33 and may opt for templates of Articles of Association in Form INC-34 in accordance with the provisions of rule 13 for preparation of Memorandum of Association and Article of Association.

(5) The promoter or the applicant shall sign and witness, the Memorandum of Association and Articles of Association in the forms downloaded from the portal of the Ministry of Corporate Affairs and scanned legibly and attach to e-form INC-32 in accordance with the provisions of rule 16 for preparation of Memorandum of Association and Articles of Association.

(6) The facility to file Integrated application for incorporation in Form INC-32 is available as an option to the process for separate applications for allotment of Director Identification Number, reservation of name and Incorporation of a company as provided in these rules.

(7) For an application filed using the Integrated process of incorporation as provided in this rule, the provisions of sub clause (i) of sub-section (5) of section 4 of the Act and rule 9 of these rules shall not apply.

(8) A company using the provisions of this rule may furnish verification of its registered office under sub-section (2) of section 12 of the Act by filling e-Form INC -32 in which case the company shall attach along with such e-Form INC-32, any of the documents referred to in sub-rule (2) of rule 25.

(9) The requirement of filing e-Form INC-28 may be dispensed with if, the proposed company maintains its registered office at the given correspondence address.

(10) The Registrar within whose jurisdiction the registered office of the company is proposed to be situated shall process INC-32 including application for allotment of Director Identification Number.

(11) (a) Where the Registrar, on examining e-form INC-32, finds that it is necessary to call for further information or finds such application or document to be defective or incomplete in any respect, he shall give intimation to the application to remove the defects and re-submit the e-form within 15 days from the date of such intimation given by the Registrar.

(b) After the resubmission of the document, if the registrar still finds that the document is defective or incomplete in any respect, he shall give one more opportunity of 15 days to remove such defects or deficiencies.

(ba) After the re-submission of the documents and on completion of second opportunity, if the registrar still finds that the documents are defective or incomplete, he shall give third opportunity to remove such defects and deficiencies;

Provided that the total period for re-submission of documents shall not exceed a total period of 30 days.

(c) In case, the Registrar is of the opinion that the document is defective or incomplete in any respect after giving such three opportunities, the e-form INC-29 of the proposed company shall be rejected.

(12) The Certificate of Incorporation shall be issued by the Registrar in Form No. INC-11.

[Refer Page 6 of the Supplementary Study Paper 2016 for relevant Rule 36 which have been omitted and repealed with this Simplified Process of filing forms for incorporating company electronically]

II. Non-Applicability of the following relevant sections of the Companies Act, 2013 for May 2017 examinations

S.No.	Section No.	Section title
1.	Section 48	Variation of shareholders' right
2.	Section 66	Reduction of share capital

PART – II : QUESTIONS AND ANSWERS

QUESTIONS

PART – A: BUSINESS LAWS

The Indian Contract Act,1872

1. (a) Examine what is the legal position, as to the following:

    (i) Mr. A offered to sell his house to Mr. B for ₹ 15,00,000. Mr. B accepted the offer by post. On the very next day Mr. B sent a telegram revoking the acceptance which reached Mr. A before the letter of acceptance. Is the revocation of acceptance valid? Would it make any difference if both the letter of acceptance and the telegram of revocation of acceptance reach Mr. A at the same time?

    (ii) Sohan induced Suraj to buy his motorcycle saying that it was in a very good condition. After taking the motorcycle, Suraj complained that there were many defects in the motorcycle. Sohan proposed to get it repaired and promised to pay 40% cost of repairs. After a few days, the motorcycle did not work at all. Now Suraj wants to rescind the contract. Explain the concept of 'misrepresentation' in matters of contract. In the instant situation, whether Suraj can rescind the contract on the grounds of misrepresentation.

    (b) Zarine rent out his house situated at Mumbai to Wasabi for a rent of ₹ 10,000 per month. A sum of ₹ 5 lac, the house tax payable by Zarine to the Municipal Corporation being in arrears, his house is advertised for sale by the corporation. Wasabi pays the corporation, the sum due from Zarine to avoid legal consequences. Referring to the provisions of the Indian Contract Act, 1872 decide whether Wasabi is entitled to get the reimbursement of the said amount from Zarine.

2. (a) M lends a sum of ₹ 5,000 to B, on the security of two shares of a Limited Company on 1st April 2016. On 15th June, 2016, the company issued two bonus shares. B returns the loan amount of ₹ 5,000 with interest but M returns only two shares which were pledged and refuses to give the two bonus shares. Advise B in the light of the provisions of the Indian Contract Act, 1872.

    (b) Ashish appoints Megha, a minor, as his agent to sell his watch for cash at a price not less than ₹ 1700. Megha sells it to Diwan for ₹ 1200. Is the sale valid? Explain the legal position of Megha and Diwan, referring to the provisions of the Indian Contract Act, 1872.

The Negotiable Instruments Act, 1881

3. A cheque payable to bearer is crossed generally and marked "not negotiable". The cheque is lost or stolen and comes into possession of Vishnu who takes it in good faith and gives value for it. Vishnu deposits the cheque into his own bank and his banker

presents it and obtains payment for his customer from the bank upon which it is drawn. The true owner of the cheque claims refund of the amount of the cheque from Vishnu. Explain whether the banks are liable or not?

4. A draws a bill on B. B accepts the bill without any consideration. The bill is transferred to C without consideration. C transferred it to D for value. Decide-.

   (i) Whether D can sue the prior parties of the bill, and

   (ii) Whether the prior parties other than D have any right of action inter se?

   Give your answer in reference to the Provisions of Negotiable Instruments Act, 1881.

The Payment of Bonus Act, 1965

5. Vikas is working as a salesman in a company on salary basis. The following payments were made to him by the company during the previous financial year –

   (i) overtime allowance,

   (ii) dearness allowance

   (iii) commission on sales

   (iv) employer's contribution towards pension fund

   (v) value of food.

   Examine as to which of the above payments may form part of "salary" of Vikas under the provisions of the Payment of Bonus Act, 1965.

6. Ganesh limited company earned super profits during financial year 2015 - 2016. It intends to give maximum bonus to its employees. In this regard you are asked to advice the company on permissible maximum bonus under the Payment of Bonus Act, 1965.

The Employees' Provident Funds and Miscellaneous Provisions Act, 1952

7. While calculating/computing the 'Basic Wages' of Mr. Aman, an employee of Glory Ltd. under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952., the following payments were included-

   (a) Emoluments earned by an employee while on duty and which are paid to him or payable in cash to him.

   (b) Cash value of food concession

   (c) Dearness allowance

   (d) Diwali gift

   Explain stating clearly the meaning of the term 'Basic wages' as defined under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952. State also what is not included in the term 'Basic Wages'.

8. An employee of a limited company filed a claim for provident fund settlement with the Provident Fund Commissioner. However, he did not get any settlement from the authority even after six months. Referring to the Employees' Provident Funds & Miscellaneous Provisions Act, 1952 what is the role of commissioner in this respect. Also, state the penalty, if any, for default in payment.

The Payment of Gratuity Act, 1972

9. Peacock Limited decided to forfeit the amount of gratuity of its employees X and Y on account of disorderly conduct and other acts which caused loss to the property belonging to the company. X and Y committed the following acts:

   (i) X committed theft under law involving offence of moral turpitude.

   (ii) Y after superannuation continued to occupy the quarter belonging to the company for six months.

   Against the decision of the company, X and Y applied to the appropriate authorities for relief. The company contented that the right to gratuity is not a statutory right and the forfeiture of the amount of gratuity was within the law.

   Examine the contention of the company and the decision taken by the company to forfeit the amount of gratuity in the light of the Payment of Gratuity Act, 1972.

10. Mr. Yellow was an employee of White Sugars, Ltd. The whole of undertaking of White Sugars Ltd. was taken-over by a new company named Modern Sugars Ltd. The services of Mr. Yellow remained continuous in the new company. After serving for one year Mr. Yellow met with an accident and became permanently disabled. Mr. Yellow applied to the new company for the payment of gratuity. The new company refused to pay gratuity on the ground that Mr. Yellow has served only for a year in the new company.

    Examine the validity of the refusal by the company in the light of the provisions of the Payment of Gratuity Act, 1972.

The Companies Act, 2013

11. Glowing Products Ltd., wishes to sell one of its line of Business and decides to call an extra ordinary general meeting (EGM) and to pass a resolution thereat. State the material facts to be set out in the statement to be annexed to the notice of the EGM on this special business to be transacted at the meeting.

12. (a) The Articles of Impression Limited clearly stated that Mr. Swift will be the solicitor of the company. The company in its general meeting of the shareholders resolved unanimously to appoint Mr. Best in place of Mr. Swift as the solicitor of the company by altering the articles of association. Examine, whether the company can do so? State the reasons clearly.

    (b) The Secretary of a Company issued a share certificate to 'Prem' under the Company's seal with his own signature and the signature of a Director forged by him. ‘Prem’ borrowed money from ‘Amar’ on the strength of this certificate. ‘Amar’ wanted to realise the security and requested the company to register him as a holder of the shares. Explain whether ‘Amar’ will succeed in getting the share registered in his name.

Explain with the help of the doctrine of ‘Indoor management’ in brief.

13. A company issued a prospectus. All the statements contained therein were literally true. It also stated that the company had paid dividends for a number of years, but did not disclose the fact that the dividends were not paid out of trading profits, but out of capital profits. An allottee of shares wants to avoid the contract on the ground that the prospectus was false in material particulars. Decide.
14. The date of approval of financial statements by the Board of Directors of KMP Ltd. is 17th July, 2016 and the date of notice of Annual General meeting (AGM) is 25th August, 2016. Accountant of KMP Ltd. has advised that the time gap between date of approval of financial statements by the Board of Directors and the date of notice of AGM should be 45 days. The Directors have approached you to advise them regarding the same in view of the provisions of Companies Act, 2013.
15. Mr Antriksh entered into an agreement for purchasing a commercial property in Delhi belonging to NRT Ltd. At the time of registration, Mr Antriksh comes to know that the title deed of the company is not free and the company expresses its inability to get the title deed transferred in the name of Mr Antriksh saying that he ought to have had the knowledge of charge created on the property of the company. Explain with the help of ‘Notice of a charge’, whether the contention of NRT LTD. is correct?

PART – B: ETHICS

16. State the ethical issues which are being faced by an individual at the workplace of an industrial organization.
17. Differentiate between 'consumer interest' and 'public interest'.
18. State the Common Corporate Social responsibility (CSR) policies for business organizations.
19. Explain the fundamental principles relating to ethics.
20. State, how far a sound ethical environment in a company may be created and corporate scandals may be avoided.

PART – C: COMMUNICATION

21. Explain the various forms of formal communication.
22. Explain the functions of interpersonal communication.
23. Explain the factors which are responsible for the growing importance of communication of an organization.

24. Suggest guidelines to handle communication ethics dilemmas.

25. Board of Directors of ABC Traders Private Limited proposes to convene an Extraordinary General Meeting for changing the name of the company to ABC International Private Limited. Draft the notice for calling the Extraordinary General Meeting of the Members.

SUGGESTED ANSWERS

1. (a) (i) Communication and revocation of acceptance when complete: The problem is related with the communication and time of acceptance and its revocation. As per Section 4 of the Indian Contract Act, 1872, the communication of an acceptance is complete as against the acceptor when it comes to the knowledge of the proposer.

Whereas section 5 of the Indian Contract Act, 1872 says that an acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

Referring to the above provisions

(1) Yes, the revocation of acceptance by Mr. B (the acceptor) is valid.

(2) If Mr. A opens the telegram first (and this would be normally so in case of a rational person) and reads it, the acceptance stands revoked. If he opens the letter first and reads it, revocation of acceptance is not possible as the contract has already been concluded.

(ii) Misrepresentation: According to Section 18 of the Indian Contract Act, 1872, misrepresentation is present:

1. When a person positively asserts that a fact is true when his information does not warrant it to be so, though he believes it to be true.
2. When there is any breach of duty by a person, which brings an advantage to the person committing it by misleading another to his prejudice.
3. When a party causes, however, innocently, the other party to the agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

The aggrieved party, in case of misrepresentation by the other party, can avoid or rescind the contract [Section 19, Indian Contract Act, 1872]. The aggrieved party loses the right to rescind the contract if he, after becoming aware of the misrepresentation, takes a benefit under the contract or in some way affirms it. Accordingly in the given case, Suraj could not rescind the contract, as his acceptance to the offer of Sohan to bear 40% of the cost of repairs impliedly amounts to final acceptance of the sale.

(b) Section 69 of the Indian Contract Act, 1872 provides that "A person who is interested in the payment of money which another is bound by law to pay, and who therefore pays it, is entitled to be reimbursed by the other".

In the given problem Wasabi has made the payment of lawful dues of Zarine in which Wasabi had an interest. Therefore, Wasabi is entitled to get the reimbursement from Zarine.

2. (a) Bailee's Duties and Liabilities: The problem as asked in the question is based on the provisions of Section 163(4) of the Indian Contract Act, 1872. As per the section, "in the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, any increase or profit which may have accrued from the goods bailed."

Applying the provisions to the given case, the bonus shares are an increase on the shares pledged by B to M. So M is liable to return the shares along with the bonus shares and hence B the bailor, is entitled to them also.

(b) According to the provisions of Section 184 of the Indian Contract Act, 1872, as between the principal and a third person, any person, may become an agent, but no person who is not of the age of majority and of sound mind can become an agent, so as to be responsible to his principal.

A person in order to be an agent must have authority to contract. So, minor has no capacity to contract but may have authority to act as agent. An agent brings about a contractual relationship between the principal and third persons and therefore his contractual capacity is immaterial Thus, if a person who is not competent to contract is appointed as an agent, the principal is liable to the third party for the acts of the agent. Thus, in the given case, Diwan gets a good title to the watch. Megha is not liable to Ashish for her negligence in the performance of her duties.

3. The cheque in the given case was crossed generally and marked 'Not Negotiable'. Thereafter, the cheque was lost or stolen and came into the possession of Vishnu, who takes it in good faith and gives value for it.

Section 130 of the Negotiable Instruments Act, 1881 provides that a person taking a cheque crossed generally or specially, bearing in either case the words 'not negotiable', shall not have, and shall not be capable of giving a better title to the cheque than that which the person from whom he took it had. In view of these provisions, Vishnu, even though he was a holder in due course, did not acquire any title to the cheque as against its true owner. The addition of the words 'not negotiable' entirely takes away the main feature of negotiability, which is, that a holder with a defective title can give a good title to a subsequent holder in due course. Vishnu did not obtain any better title than his immediate transferor, who had either stolen or found the cheque and was not the true owner of the cheque. Therefore, as regards the true owner, Vishnu was in no better position than the transferor. Vishnu is also liable to repay the amount of the cheque to the true owner. He can, however, proceed against the person from whom he took the cheque.

In the given case, both the collecting banker and the paying bankers would be exonerated. Since the collecting banker, in good faith and without negligence, had received payment for Vishnu, who was its customer of the cheque which was crossed generally, the banker would not be liable, in case the title proved to be defective, to the true owner by reason only of having received the payment of the cheque for his customer (as per Section 131). Since the paying banker on whom the crossed cheque was drawn, had paid the same in due course, the banker would also not be liable to the true owner (as per Section 128).

4. Section 43 of the Negotiable Instruments Act, 1881 provides that a negotiable instrument made, drawn, accepted, indorsed or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction. But if any such party has transferred the instrument with or without endorsement to a holder for consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor for consideration or any prior party thereto.

(i) In the problem, as asked in the question, A has drawn a bill on B and B accepted the bill without consideration and transferred it to C without consideration. Later on in the next transfer by C to D is for value. According to provisions of the aforesaid section 43, the bill ultimately has been transferred to D with consideration. Therefore, D can sue any of the parties i.e. A, B or C, as D arrived a good title on it being taken with consideration.

(ii) As regards to the second part of the problem, the prior parties before D i.e., A, B, and C have no right of action inter se because first part of Section 43 has clearly laid down that a negotiable instrument, made, drawn, accepted, indorsed or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction prior to the parties who receive it on consideration.

5. **Computation of Salary / Wages:** According to Section 2(21) of the Payment of Bonus Act, 1965 salary and wages means all remuneration other than remuneration in respect of overtime work, capable of being expressed in terms of money, which would if the terms of employment, express or implied, were fulfilled, be payable to an employee in respect of his employment, or of work done in such employment and includes dearness allowance, i.e. all cash payment by whatever name called, paid to an employee on account of a rise in the cost of living. But the term excludes:

(i) Any other allowance which the employee is for the time being entitled to;

(ii) The value of any house accommodation or of supply of light, water, medical attendance or other amenities of any service or of any concessional supply of food grains or other articles;

(iii) Any traveling concession;

(iv) Any bonus including incentive, production or attendance bonus;

(v) Any contribution paid or payable by the employer to any pension fund or for benefit of the employee under any law for the time being in force.

(vi) Any retrenchment compensation or any gratuity or other retirement benefit payable to the employee or any ex-gratia payment made to him; and

(vii) Any commission payable to the employee.

It has been clarified in the explanation to the section that where an employee is given, in lieu of the whole or part of the salary or wage payable to him, free food allowance or free food by his employer, such food allowance or the value of such food shall be deemed to form part of the salary or wage for such employee.

In view of the provisions of Section 2(21) explained above, the payment of dearness allowance and value of free food by the employer forms part of salary of Vikas while the remaining three payments i.e. payment for overtime, commission on sales and employer's contribution towards pension funds shall not form part of his salary, under the provisions of the Payment of Bonus Act, 1965.

6. Where, in respect of any accounting year referred to in Section 10 of the Payment of Bonus Act,1965, the allocable surplus exceeds the amount of minimum bonus payable to the employees under that section, the employer shall, in lieu of such minimum bonus, be bound to pay to every employee in respect of that accounting year bonus which shall be an amount in proportion to the salary or wage earned by the employee during the accounting year subject to a maximum 20% of such salary or wage.

In the given case therefore, the company will be free to give bonus at any rate exceeding 8.33% upto a maximum of 20% of the salary or wage earned by the employees during the accounting year. From the facts given, it may be presumed that the bonus at 20% may be payable during the Financial Year 2015 - 2016.

However, in relation to the maximum bonus payable the most important term to understand is "allocable surplus". The eligibility for maximum bonus arises from the "allocable surplus" but is not limited by it, as the allocable surplus may justify a bonus at a rate higher than 20% but bonus will still be limited to 20%.

7. **Basic Wages:** As per Section 2(b) of the Employees' Provident Funds and Miscellaneous Provision Act, 1952, "Basic Wages" mean all emoluments which are earned by an employee while on duty or on leave or on holidays with wages in either case in accordance with the terms of the contract of employment and which are paid or payable in cash to him, but does not include:

(i) the cash value of any food concessions;

(ii) any dearness allowance (that is to say all cash payments, by whatever name called, paid to an employee on account of a rise in the cost of living), house rent allowance, overtime allowance, bonus commission or any other similar allowance payable to the employee in respect of his employment or of work done in such employment; or

(iii) any presents made by the employer.

The key characteristics of basic wages are:

(a) All emoluments (of whatever nature) earned during duty or during paid leave or during paid holidays;

(b) The above emoluments are in accordance with the terms of employment of the employee;

(c) The above emoluments are paid or payable in cash.

Therefore, emoluments or benefits of a non cash nature or any payment not in accordance with the terms of employment shall not form part of basic wage. Thus, if an employer pays any amount as a reward to the employee out of his own will without being under the obligation to do so under the terms of employment of the employee, such payment shall not be basic wage under this Act.

Applying the above provisions of this Act to the given problem, the Basic wages of Aman will include only Emoluments earned while on duty and which are paid to him or payable in cash to him but will exclude the Cash value of food concession, Dearness allowance, and Diwali gift.

8. The Provident Fund "claims" complete in all respects submitted along with the requisite documents are required to be settled and the benefit amount to be paid to the beneficiaries within 30 days from the date of its receipt of the complete "claims" by the Commissioner.

If there is any deficiency in the claim, the same shall be recorded in writing and communicated to the applicant within 30 days from the date of receipt of such application.

In case the Commissioner fails without sufficient cause to settle a claim complete in all respects within 30 days, the Commissioner shall be liable for the delay beyond the said period and penal interest at the rate of 12% per annum may be charged on the benefit amount and the same may be deducted from the salary of the Commissioner.

9. **Forfeiture of Gratuity:** In accordance with the provisions of Section 4(6) of the Payment of Gratuity Act, 1972, if the services of any employee have been terminated for any act, willful omission, or negligence causing any damage or loss to or destruction of, property belonging to the employer, the gratuity shall be forfeited to the extent of the damage or loss so caused.

Further, if the services of such an employee have been terminated for any act which constitutes an offence involving moral turpitude, provided that such offence is committed by him in the course of his employment, the gratuity payable to the employee may be wholly or partially forfeited.

Under section 4(1) of the Payment of Gratuity Act, 1972 gratuity is payable to an employee on termination of employment provided he completes five years of continuous service with the employer. The condition of the completion of five years' continuous service is not essential in case of the termination of the employment of any employee due to death or disablement.

The gratuity payable is an obligation of the employer and any forfeiture in full or part of the gratuity payable to an employee can be made only in terms of section 4(6).

The correctness of the decision taken by Peacock Ltd. in the given case, regarding forfeiture of the gratuity to its employees X and Y may be tested in the light of Section 4(6) of the Payment of Gratuity Act, 1972 as referred above.

(i) The offence of theft committed by X, under law involves moral turpitude and his gratuity stands wholly forfeited in view of Section 4(6) of the Act. It is presumed that such theft is committed by X in the course of his employment.

(ii) Y had wrongfully occupied the company's quarter after the termination of his employment for six months. Y may have caused a deliberate loss to the company by his wrongful occupation for 6 months as the quarter could not be given to another employee and the company may have incurred the cost of rent in such case. Hence, the company is entitled to charge the rent from him and after adjusting other dues the remaining amount of gratuity may be paid.

10. (1) **Entitlement to Gratuity:** According to Section 4 (1) of the Payment of Gratuity Act, 1972, gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous service for not less than five years on his superannuation, or, on his retirement or resignation or on his death or disablement due to accident or disease.

The proviso to the said section states that the condition of the completion of five years of continuous service is not essential in case of the termination of the employment of any employee due to death or disablement for the purpose of this section.

(2) **Disablement:** Disablement has been explained as such disablement which incapacitates an employee for the work which he was capable of performing before the accident or disease resulting in such disablement.

(3) **Change in Ownership of Company:** When there is change of ownership, the relationship of employer and employees subsists and the new employer cannot escape from the liability of payment of gratuity to the employees.

The given problem fulfils all the above requirements as stated. Therefore, Mr. Yellow is entitled to recover gratuity after becoming permanently disabled and continuous service of five years is not required in this case. Hence, the company cannot refuse to pay gratuity on the ground that he has served only for a year.

11. Following are the material facts to be set out in the explanatory statement to be annexed to the Notice of EGM of Glowing Products Ltd. as per Section 102(1) of Companies Act, 2013:

(a) the nature of concern or interest, financial or otherwise, if any, in respect of each items of-

(i) every director and the manager, if any;

(ii) every other key managerial personnel; and

(iii) relatives of the persons mentioned in sub-clauses (i) and (ii);

(b) any other information and facts that may enable members to understand the meaning, scope and implications of the items of business and to take decision thereon.

Further, where any item of special business to be transacted at a meeting of the company relates to or affects any other company, the extent of shareholding interest in that other company of every promoter, director, manager, if any, and of every other key managerial personnel of the first mentioned company shall, if the extent of such shareholding is not less than two percent of the paid up share capital of that company, also be set out in the statement.

12. (a) According to Section 10(1) of the Companies Act, 2013, the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed by the company and by each member and contained covenants on its and his part to observe all the provisions of the memorandum and articles.

Further, under Section 14 (1) subject to the provisions of this Act and to the conditions contained in the Memorandum, a company may, by a special resolution, alter its Articles.

Moreover, under section 14 (2) the company will be required to file with the Registrar every alteration of the Articles and a copy of the order of the Tribunal approving the alteration, together with the printed copy of the altered Articles, within 15 days. On receipt of all documents the Registrar shall register the same.

Section 14 (3) further provides that any alterations in the Articles registered will be valid as if they were originally in the Articles.

In the present case, the company has altered the Articles by a unanimous resolution of the members passed at a general meeting. Hence, the alteration is valid and after registration of the altered Articles, the appointment of Mr. Best will stand and Mr. Swift will be terminated.

(b) The doctrine of Indoor Management is laid down in the *Royal British Bank vs. Turquand (1956) 6E&B 327 case* in which the directors of RBB (Royal British Bank) gave a bond to one T (Turquand) without the required resolution being passed. The Articles empowered the directors to issue such bonds under the authority of a proper resolution. In fact no such resolution was passed. It was decided in the case that notwithstanding the non passing of the required resolution, T could sue on the bonds on the ground that he was entitled to assume that the resolution had been duly passed. Thus, the persons dealing with the company are entitled to assume that the acts of the directors or the officers of the company are validly performed, if they are within the scope of their apparent authority.

However, this doctrine is not applicable where the person dealing with the company has notice of irregularity or when an instrument purporting to be enacted on behalf of the company is a forgery.

In the instant problem, the doctrine of indoor management will not apply as the certificate is a forgery which does not give a good title to Prem and thereby to Amar. Hence, Amar will not succeed in getting the share registered in his name.

13. The Companies Act, 2013 vide sections 34 and 35 lay down the criminal and civil liabilities of the guilty parties in case of mis-statements and misleading inclusions and omissions in a prospectus. Further, section 36 lays down the punishment for fraudulently inducing persons to invest moneys.

However, the present case before us is not in respect of liability for a possible mis-statement but on the right of the allottee to avoid the contract of purchasing the shares from the company. In order to decide this, key factor is to determine if any material mis-representation or concealment of a material fact has taken place and if such misrepresentation is fraudulent.

The non disclosure of the fact that dividends were paid out of capital profits is a concealment of material fact as a company is normally required to distribute dividend only from trading or revenue profits and under exceptional circumstances can do so out of capital profits. Hence, a material misrepresentation has been made.

Hence, in the given case the allottee can avoid the contract of allotment of shares.

14. Section 101 of the Companies Act, 2013 dealing with Notice of meeting, states that a general meeting of a company may be called by giving at least clear 21 days' notice.

However, the Companies Act, 2013 does not prescribe the time limit between the date of approval of financial statements by the Board of Directors of a company and the date of notice of Annual General Meeting.

Hence, in the given question, the Board of directors of KMP Ltd. should ensure that the gap between the board meeting in which the financial statements are approved and the AGM, should have a minimum gap of 21 clear days (in order to ensure at least 21 days' clear notice), unless the meeting is at a shorter notice.

15. Notice of Charge: According to section 80 of the Companies Act, 2013, where any charge on any property or assets of a company or any of its undertakings is registered under section 77 of the Companies Act, 2013, any person acquiring such property, assets, undertakings or part thereof or any share or interest therein shall be deemed to have notice of the charge from the date of such registration.

Thus, the section clarifies that if any person acquires a property, assets or undertaking for which a charge is already registered, it would be deemed that he has complete knowledge of charge from the date the charge is registered.

Thus, the contention of NRT Ltd. is correct.

16. Ethical decisions are influenced by three key factors: Individual moral standards, the influence of managers and co-workers and the opportunity to engage in misconduct. While one may have great control over personal ethics outside the workspace, co-workers and the management exert significant control on one's choices at work. The activities and examples set by co-workers along with rules and policies are critical in gaining consistent ethical compliance in an organization. If a company fails to provide good examples and direction for appropriate conduct, confusion and conflict will develop and result in the opportunity for unethical behaviour. *Example:* If the boss or co-workers leave work early, one may be tempted to do so as well. If one sees co-workers making personal long distance phone calls at work and charging them to the company, one may be more likely to do so also. In addition having sound personal values contributes to an ethical work place.

Some examples of ethical issues faced by an individual in the workplace are:

1. Relationships with suppliers and business partners
   a. Bribery and immoral entertainment
   b. Discrimination between suppliers
   c. Dishonesty in making and keeping contracts
2. Relationship with customers
   a. Unfair pricing
   b. Cheating customers
   c. Dishonest advertising
3. Relationship with employees
   a. Discrimination in hiring, promoting, etc

b. Unequal treatment

4. Management of resources: Misuse of official funds

b. Tax evasion.

17. Consumer interest and public interest: Apparently it seems that public interest and consumer interest are synonymous, but it is not so. They may be differentiated as under:

(i) In the name of public interest, many Governmental policies are formulated which manifest themselves in anti-competitive behaviour. If the consumer is at the fulcrum, consumer interest and welfare should have primacy in all governmental policy formulations.

(ii) Consumer is a member of a broad class of people who purchase, use, maintain and dispose of products and services. They are being affected by pricing policy, financing practice, quality of goods, services and trade practices. They are clearly distinguished from manufacturers who produce goods for wholesalers, retailers who sell goods in public interest.

(iii) Public interest is something in which the society as a whole has some interest, and is seen as an externality to competitive markets. There is also a justifiable apprehension that in the name of public interest, Governmental policies may be fashioned and introduced which may not be in the ultimate interest of the consumers. In fact in such situations, there is the possibility that a conflict could arise between public interest and consumer interest.

18. Common Policies under Corporate Social Responsibilities are as under:

- ♦ Commitment to diversity in hiring employees and barring discrimination;
- ♦ Adoption of internal controls reform;
- ♦ 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.

19. The fundamental principles relating to ethics may be summarized as under:

1. **The Principle of Integrity:** It calls upon all accounting and finance professionals to adhere to honesty and straightforwardness while discharging their respective professional duties.

2. **The Principle of Objectivity:** This principle requires accounting and finance professionals to stick to their professional and financial judgment.
3. **The Principle of Confidentiality:** This principle requires practitioners of accounting and financial management to refrain from disclosing confidential information related to their work.
4. **The Principle of Professional Competence and due care:** Finance and accounting professionals need to update their professional skills from time to time in order to provide competent professional services to their clients.
5. **The Principle of Professional Behaviour**: This principle requires accounting and finance professionals to comply with relevant laws and regulations and avoid such actions which may result in discrediting the profession.

20. Creating an ethical environment in company: A sound ethical environment in a company may be created and corporate scandals may be avoided by adopting the following methods:

(i) Ensuring that employees are aware of their legal and ethical responsibilities.

Some ethical organisations are having policies to train and motivate employees towards ethical behaviour. To start with, such initiation should be from the top. A number of companies in India and abroad are being known for their quality and soundness of their ethics programmes. Companies like Raytheon, Texas Instruments, Wipro are pioneers in establishing ethical environment among the employees enabling them to take ethical decisions.

(ii) Providing a communication system between the management and employees so that anyone in the company can report fraud and mismanagement without the fear of being reprimanded.

In India, Wipro has introduced a helpline comprising of senior members of the company, who are available for guidance on any moral, legal or ethical issues that an employee of the company may face.

(iii) Ensuring fair treatment to those who act as whistle blowers.

This is perhaps the most important and sensitive issue. Fair treatment to whistle blowers is a basic necessity to check fraud. Some acts must be appreciated and that appreciation should be extended from within the company rather than outside.

21. A formal communication flows along prescribed channels which all organizational members desirous of communicating with one another are obliged to follow. Every organization has built-in hierarchical system, communication in an organization is multidirectional. On the basis of various directions in which communications are sent, we can classify formal communication in these forms:

(i) Downward Communication

(ii) Upward Communication

(iii) Horizontal or Lateral Communication

(iv) Diagonal or Crosswise Communication

Communication generally flows from top to bottom. Downward communication means communication from superior to subordinate in the hierarchical system of the organization. It includes orders and instructions. In upward communication, message flows from the subordinate to superior in the form of request, reports, instructions complaints and suggestions. Communication between co-workers with different areas of responsibility is called horizontal (lateral) communication. Communication among the functional managers of a company is the best example of horizontal communication. Diagonal communication means communication among the various Department/ employees of the organization without any hierarchical system in case of emergency.

22. Functions of Interpersonal Communication: Interpersonal communication is important because of the following functions it achieves:

Gaining Information: One reason, we engage in interpersonal communication, is to gain knowledge about another individual. We attempt to gain information about others so that we can interact with them more effectively.

Building Understanding: Interpersonal communication helps us to understand better what someone says in a given context. Words can mean very different things depending on how they are said or in what context. **Content Messages** refer to the surface level meaning of a message. **Relationship Messages** refer to how a message is said. The two are sent simultaneously, but each affects the meaning assigned to the communication and helps us understand each other better.

Establishing Identity: We also engage in interpersonal communication to establish an identity based on our relationships and the image we present to others.

Interpersonal Needs: We also engage in interpersonal communication to express interpersonal needs. William Schutz has identified three such needs: inclusion, control, and affection.

- Inclusion is the need to establish identity with others.
- Control is the need to exercise leadership and prove one's abilities.
- Affection is the need to develop relationships with people. Groups are an excellent way to make friends and establish relationships.

23. The importance of communication in the industrial organization has increased immensely in these days. The following factors are responsible for the growing importance of communication:

(a) Growth in the size and multiple locations of organizations: Most of the organizations are growing larger and larger in size. The people are working in the country and abroad, of these organizations. Keeping in touch, sending directions across and getting feedback is possible only when communication lines are kept working effectively.

(b) **Growth of trade unions:** Over the last so many decades, trade unions have been growing strong. No management can be successful without taking the trade unions into confidence. Effective communication will create relationship between the management and the workers.

(c) **Growing importance of human relations:** Workers in an organization are not like machines. They have their own hopes and aspirations. Management has to recognize them and should work with the spirit of integration so that human relations may be maintained. This may only be achieved though effective communication.

(d) **Public relations:** Every organization has a social responsibility towards customers, government, suppliers and the public at large. Communication is the only way an organization can project a positive image of itself.

(e) **Advances in behavioral sciences:** Modern management is deeply influenced by exciting discoveries made in behavioral sciences like psychology, sociology, transactional analysis etc. All of them throw light on suitable aspects of human nature and help in developing a positive attitude towards life and building up meaningful relationship. This is possible only through communication.

(f) **Technological advancement:** The world is changing very fast, owing to scientific and technological advancements. These advancements deeply affect not only the methods of work but also the compositions of groups. In such a situation, proper communication between superiors and subordinates becomes very necessary.

24. Guidelines to handle communication ethics dilemmas:

(a) Maintain candour: Candour refers to truthfulness, honesty, frankness and one should stick to these elements while communicating with others.

(b) Keep message accurate: At the time of relaying information from one source to another, communicate the original message as accurately as possible.

(c) Secrecy: One has to maintain secrecy and confidence in communication. So one should not divulge such information to others

(d) Ensure timeliness of communication: The timing of messages can be critical. Delay in sending messages can be assumed unethical.

(e) Avoid deception: Ethical communicators are always vigilant in their quest to avoid deception, fabrication, intentional distortion or withholding of information in their communication.

(f) Confront unethical behaviour: One must confront an unethical behaviour in order to ensure a consistent ethical view point.

25. Notice for Extraordinary General Meeting of the Members

Notice is hereby given that extraordinary General Meeting of the members of ABC Traders Private Limited will be held on Monday, the ……day of 2017, 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 13 of the Companies Act,2013, the name of the company be and is changed from ABC Traders Private Limited to ABC International Private 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 Traders Private Limited.

Secretary…………………………….

Place:…………………………………

Date:…………………………………

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART I: COST ACCOUNTING

QUESTIONS

Material

1. Aditya Ltd. has a monthly requirement for an item of raw material is 1,000 units. The purchase price per unit of material is ₹60. The cost of processing an order is ₹540 and the carrying cost is 20%. There is a single supplier for the material which offers quantity discounts as under:

Order Quantity (in units)	Price per unit (₹)
Less than 2,000 units	60.00
2,000 units and less than 4,000 units	59.80
4,000 units and less than 6,000 units	59.50
6,000 units and less than 8,000 units	58.90
8,000 units and above	58.40

The company uses the cash credit facility provided by the company's banker to finance its raw material purchase. The bank due to its own infrastructural constraint, can accommodate a maximum of five fund transfer (NEFT/ RTGS) requests for any single beneficiary per annum. The company in short term is unable to arrange any other source of finance.

Required:

(i) Calculate the optimum purchase order size for the company;

(ii) Calculate the order level where the company could have minimised its total cost;

(iii) The amount of loss that the company has to bear due to bank's inability to process fund transfer requests.

Labour

2. Jigyasa Ltd. pays a basic wage of ₹ 125 per hour to its production workers. The company works 6 days a week in a single shift of 8:00 AM. to 4:30 PM. The company also pays overtime to its workers apart from basic wages for work beyond its normal working hours. The overtime rule is as under:

(i) No over-time is paid for any work upto 5:30 PM.

(ii) ₹ 62.50 per hour for any work done after 5:30 PM.

(iii) The Maximum over-time payment is restricted to ₹ 375 for a day, However, workers are paid ₹ 80 as diet allowance for work done beyond 8:30 PM.

(iv) On Sunday or any holiday, workers are paid ₹ 375 provided they work atleast for 4 hours.

The extract of attendance for three workers is as follows:

	Worker- A	Worker- B	Worker- C
Monday	8:00AM – 6:30 PM	8:00 AM – 7:30 PM	8:00 AM – 9:30 PM
Tuesday (Holiday)	8:00 AM – 5:30 PM	8:00 AM – 12:30 PM	Absent
Wednesday	8:00 AM – 10:30 PM	8:00 AM – 5:30 PM	8:00 AM – 11:30 PM
Thursday	8:00 AM – 4:30 PM	8:00 AM – 9:30 PM	8:00 AM – 8:30 PM
Friday	8:00 AM – 11:00 PM	8:00 AM – 4:30 PM	8:00 AM – 4:30 PM
Saturday	Absent	8:00 AM – 5:30 PM	8:00 AM – 7:30 PM
Sunday	Absent	8:00 AM – 1:30 PM	8:00 AM – 4:30 PM

Required:

(i) Calculate the amount of overtime and diet allowance payable to each worker.

(ii) Calculate the amount and accounting treatment of overtime and diet allowance in each case:

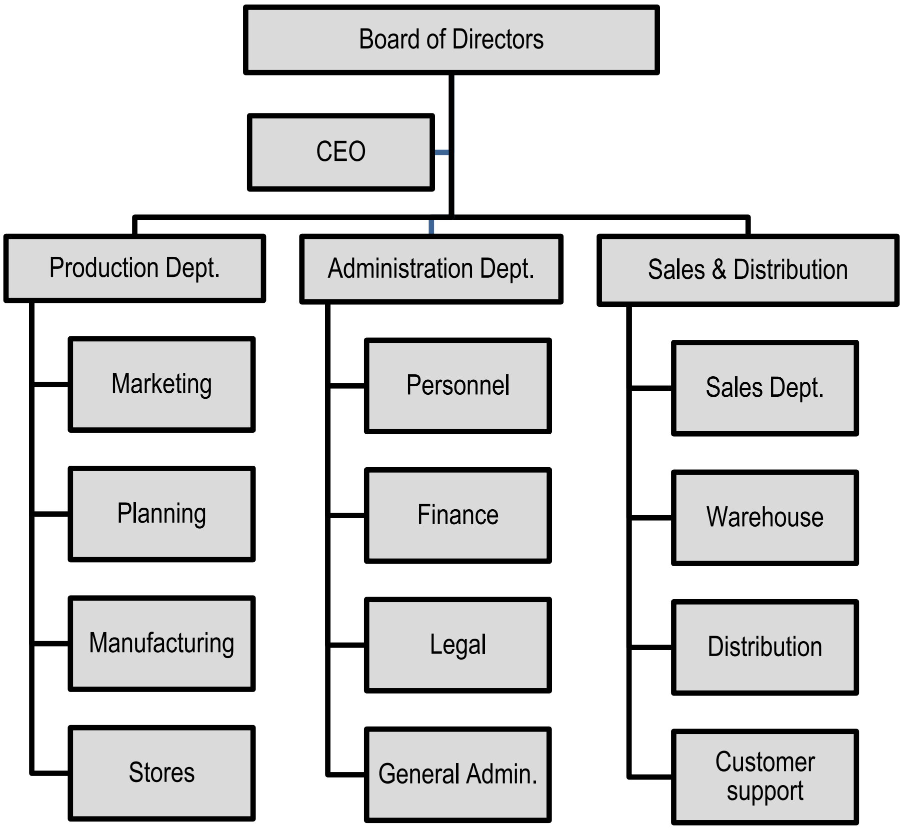
(a) Worker A and C were involved in a specific job work assigned to them.

(b) Overtime was due to under-estimation of sales demand provided by the sales department.

(c) Overtime was due to make up a shortfall in production due to sudden demand.

Overheads

3. Arnav Ltd. manufactures and sells three products namely A, B and C. The organisational structure of the company is as follows:



The work of Board of Directors and CEO is also known as General Management.

The extract from the budget for the next financial year is as follows:

		Explanations
Raw Material Cost	₹ 4,25,00,000	Consumed in manufacturing of all three products in the ratio of 2:3:2
Indirect material cost	₹ 10,36,000	Manufacturing - ₹ 6,00,000, Stores - ₹ 10,000, Planning - ₹ 6,000, General administration - ₹ 3,20,000, Personnel - ₹ 80,000 and Sales - ₹ 20,000
Salary & wages	₹ 3,40,00,000	It includes direct wages paid to manufacturing workers (not on roll) ₹ 1,40,00,000.
Rent & Property tax	₹ 1,00,000	Warehouse rent of ₹ 80,000 and Property tax ₹ 20,000.
Depreciation on non-current assets (on WDV basis)	₹ 22,50,000	It includes ₹9,00,000 for factory and office building, ₹ 1,50,000 on Air Conditioner, ₹ 12,00,000 on Machinery.

Power & Fuel ₹ 4,10,000	It consists of ₹ 4,00,000 for manufacturing activities and others related with fuel cost of delivery vans.
Insurance premium on machinery	4% of the opening written down value of the machinery.
Insurance premium on employees group insurance (excluding direct workers and General management) ₹ 2,50,000	Premium amount depends on the gross salary of the employees on roll.
Printing & Stationery ₹ 7,00,800	Planning Dept.- ₹4,800, Marketing- ₹ 12,000, Finance- ₹ 4,80,000, Legal- ₹ 24,000 and Sales Dept. ₹ 1,80,000
Audit fee ₹ 1,20,000	For statutory and concurrent audit.
Electricity expenses ₹ 3,20,000	Each division has separate meters. The expected electricity consumption (in units, 1 unit = 1,000 kWh) will be as follows: Production Dept.- 4,800, Administration Dept.- 9,600, Sales & Distribution- 3,600 and General Management - 1,200.
Telephone & Mobile expenses ₹ 4,23,000	Marketing- ₹ 1,10,000, Personnel- ₹ 42,000, General Management – ₹ 26,000, Sales Dept. ₹ 65,000 and Customer support- ₹ 1,80,000
Travelling expenses ₹ 20,33,000	Marketing- ₹ 4,80,000, General Management ₹ 10,25,000, Sales Dept. ₹ 5,28,000.
Subsidy for meal coupons ₹ 1,83,000	It is given uniformly to all employees on roll @ ₹ 3,000.
Software licence renewal fee ₹ 14,24,000	Planning- ₹ 7,20,000, Finance- ₹ 1,20,000, Store- ₹ 24,000, Customer support- ₹ 5,60,000.
Other miscellaneous expenditure ₹ 8,05,085	

Other Information:

No. of employees on roll	Production Dept. 18; Administration Dept. 19 and Sales & Distribution Dept. 24
Average Gross Salary	Production Dept. ₹ 6,00,000, Administration Dept. ₹ 3,50,000, Sales & Distribution ₹ 3,00,000 and General Management ₹ 2,50,000.
Building floor area	Production dept- 9,000 sq. mtr., Administration dept- 3,000 sq. mtr., S&D – 2,500 sq. mtr., General management- 1,500 sq. mtr.
Air Conditioner	Production dept- 6,000 RT, Administration dept- 3,000 RT,

	S& D – 2,800 RT, General management- 1,200 RT
Rate of Depreciation	Building- 5%, Air Conditioner- 15%, Machinery- 10%
Other miscellaneous expenditure	It may be apportioned on the basis of direct allocated expenses.

General Management devotes their 70% time for Sales strategy, 20% for Production and marketing and 10% for internal administration.

Administration department works 45% for production and 55% for sales department.

Required:

(i) Prepare a schedule of Cost Allocation for Production Dept., Administration Dept., Sales & Distribution Dept. and General Management.

(ii) Prepare a schedule of Cost Apportionment (Primary Distribution) for Production Dept., Administration Dept., Sales & Distribution Dept. and General Management.

(iii) Prepare a schedule of Secondary distribution of Administration Dept. and General Management costs.

Non- Integrated Accounting

4. The following is the Trading and Profit & Loss Account of ABC Limited:

Dr. Cr.

Particulars	(₹)	Particulars		(₹)
To Materials	28,06,000	By Sales (30,000 units)		68,75,000
To Direct wages	18,05,750	By Finished goods stock (1,000 units)		1,30,000
To Production Overheads	9,92,250	By Work-in-progress:		
To Administration Overheads	5,10,375	Materials	55,250	
To Selling and Distribution Overheads	3,68,875	Wages	26,000	
To Preliminary Expenses written off	22,750	Production Overheads	16,250	97,500
To Goodwill written off	45,500			
To Fines	7,250	By Dividends received		4,90,000
To Interest on term loan	13,000	By Interest from bank deposits		95,000
To Loss on Sale of machine	16,250			
To Tax	1,95,000			
To Net Profit for the year	9,04,500			
	76,87,500			76,87,500

ABC Limited manufactures a standard unit.

The Cost Accounting records of ABC Ltd. show the following:

(i) Production overheads have been charged to work-in-progress at 20% on Prime cost.

(ii) Administration Overheads have been recovered at ₹15.75 per finished Unit.

(iii) Selling & distribution Overheads have been recovered at ₹ 13 per Unit sold.

(iv) The Under- or Over-absorption of Overheads have not been transferred to costing P/L A/c.

Required:

(i) Prepare a proforma Costing Profit & Loss statement, indicating net profit.

(ii) Prepare Control accounts for Production overheads, Administration Overheads and Selling & Distribution Overheads.

(iii) Prepare a statement reconciling the profit disclosed by the Cost records with that shown in Financial accounts.

Contract Costing

5. The following details have been extracted from the books of DKG Construction LLP, which closes its books on 31st March every year.

	Contract 101	**Contract 102**
Date of commencement	1st April, 2015	1st December, 2015
Expected date of completion	31st September, 2016	31st December, 2016
	Amount (₹'000)	**Amount (₹'000)**
Contract price	4,000	1,100
Material issued to construction site	1,400	300
Material returned to store	160	60
Plant & Machinery sent to construction site	2,000	300
Inter-contract material transfer	(80)	80
Materials at site on 31st March, 2016	150	30
Plant hire charges	400	60
Wages paid to workers	600	540
Overhead apportioned	150	36
Other direct expenses	50	8
Value of work certified	3,000	750

Cost of work not certified	320	40
Progress payment received from contractees	2,880	700
Estimated cost of completion	270	220

Depreciation is charged on plant and machinery @ 15% p.a. using straight line method.

Required:

Prepare contract account for each contract using columnar format, showing Cost of work certified and Notional profit / loss on each contract.

Operating Costing

6. Happy Transport Service is a Delhi based national goods transport service provider, owning four trucks for this purpose. The cost of running and maintaining these trucks are as follows:

Particulars	Amount
Diesel cost	₹13.75 per km.
Engine oil	₹ 4,200 for every 13,000 km.
Repair and maintenance	₹ 12,000 for every 10,000 km.
Driver's salary	₹18,000 per truck per month
Cleaner's salary	₹7,500 per truck per month
Supervision and other general expenses	₹12,000 per month
Cost of loading of goods	₹150 per Metric Ton (MT)

Each trucks were purchased for ₹ 20 lakhs with an estimated life of 7,20,000 km.

During the next month, it is expecting 6 bookings, the details are as follows:

Sl. No.	Journey	Distance in km	Weight- Up (in MT)	Weight- Down (in MT)
1.	Delhi to Kochi	2,700	14	6
2.	Delhi to Guwahati	1,890	12	0
3.	Delhi to Vijayawada	1,840	15	0
4.	Delhi to Varanasi	815	10	0
5.	Delhi to Asansol	1,280	12	4
6.	Delhi to Chennai	2,185	10	8
	Total	10,710	73	18

Required

(i) Calculate the total absolute Ton-km for the vehicles.

(ii) Calculate the cost per ton-km.

Joint Products & By-Products

7. In an Oil Mill four products emerge from a refining process. The total cost of input during the quarter ending March 2016 is ₹1,48,000. The output, sales and additional processing costs are as under:

Products	Output in Litres	Additional processing cost after split off (₹)	Sales value (₹)
ACH	8,000	43,000	1,72,500
BCH	4,000	9,000	15,000
CSH	2,000	–	6,000
DSH	4,000	1,500	45,000

In case these products were disposed-off at the split off point that is before further processing, the selling price per litre would have been:

ACH (₹)	BCH (₹)	CSH (₹)	DSH (₹)
15.00	6.00	3.00	7.50

Prepare a statement of profitability based on:

(i) If the products are sold after further processing is carried out in the mill.

(ii) If they are sold at the split off point.

Standard Costing

8. XYZ Ltd. produces two products M and N by using two inputs Material A and B. The standard price per unit of Material A is ₹20 and of Material B is ₹10. The standard quantities of materials for each product are as follows:

Products	Materials	
	A (units)	B (units)
M	2	3
N	1	4

The company actually produced 11,000 units of M and 9,000 units of N and used 32,500 units of Material A at a cost of ₹6,59,750 and 67,000 units of Material B at a cost of ₹ 6,83,400.

Calculate:

(i) Material Price Variance;

(ii) Material Usage Variance;

(iii) Material Cost Variance.

Marginal Costing

9. A Company manufactures a product, currently utilizing 80% capacity with a turnover of ₹ 8,00,000 at ₹ 25 per unit. The cost data are as under:

Material cost ₹7.50 per unit, Labour cost ₹6.25 per unit.

Semi variable cost (including variable cost of ₹3.75 per unit) ₹1,80,000. Fixed cost ₹ 90,000 upto 80% level of output, beyond this an additional ₹20,000 will be incurred.

Calculate:

(i) Level of output at Break-even Point

(ii) Number of units to be sold to earn a net income of 8% of sales.

(iii) Level of output needed to earn a profit of ₹95,000

(iv) What should be the selling price per unit, if break-even point is to be brought down to 40% activity level?

Budget & Budgetary Control

10. Vivekananda Primary School has a total of 150 students consisting of 5 sections with 30 students per section. The school plans for a picnic around the city during the weekend to places such as the zoo, the Japanese park, Birla planetarium etc. A private transport operator has come forward to lease out the buses for taking the students. Each bus will have a maximum capacity of 50 (excluding 2 seats reserved for the teachers accompanying the students.) The school will employ two teachers for each bus paying them an allowance of ₹500 per teacher. It will also lease out the required number of buses. The following are the other cost estimates:

Particulars	Cost per student (₹)
Breakfast	50
Lunch	100
Tea	30
Entrance fee at zoo	20
Bus hire charge	6,500 per bus
Special permit fee	500 per bus
Block Entrance fee at the planetarium	2,500
Prizes to students for games	2,500

No costs are incurred in respect of the accompanying teachers (except the allowances of ₹ 500 per teacher).

You are required to prepare:

(a) A flexible budget estimating the total cost for the students' levels of 30, 60, 90, 120 and 150. Each item of cost is to be indicated separately.

(b) Compute the average cost per student at these levels.

(c) What will be your conclusions regarding the break-even level of students if the school proposes to collect ₹ 450 per student.

SUGGESTED ANSWERS

1. (i) Calculation of optimum purchase order size or Economic Order Quantity (EOQ):

$$EOQ = \sqrt{\frac{2 \times A \times O}{C \times i}}$$

Where, A = Annual requirement for inventory = 1,000 units × 12 months = 12,000 units

O = Ordering cost = ₹ 540

C = Cost per unit = ₹60

C × i = Carrying cost per unit per annum = 20% × ₹60 = ₹ 12

$$EOQ = \sqrt{\frac{2 \times 12{,}000\,\text{units} \times ₹540}{₹12}} = \sqrt{\frac{1{,}29{,}60{,}000}{12}} = 1{,}039.23 \text{ or } 1{,}039 \text{ units.}$$

(ii)

Order Size (in units)	**1,500**	**2,000**	**4,000**	**6,000**	**8,000**
No. of order	8	6	3	2	1.5*
Cost per order (₹)	540	540	540	540	540
Average inventory	750	1,000	2,000	3,000	4,000
Cost per unit (₹)	60.00	59.80	59.50	58.90	58.40
Carrying cost per unit @20% (₹)	12.00	11.96	11.90	11.78	11.68
(a) Ordering Cost (₹)	4,320	3,240	1,620	1,080	810
(b) Carrying cost (₹)	9,000	11,960	23,800	35,340	46,720
(c) Material cost (₹)	7,20,000	7,17,600	7,14,000	7,06,800	7,00,800
Total Cost {(a) + (b) + (c)} (₹)	7,33,320	7,32,800	7,39,420	7,43,220	7,48,330

*(This may also be taken as 2 orders)

At order level of 2,000 units, the total cost to the company is least.

(iii) Calculation of amount of loss due to bank's inability to process more than five fund transfer requests:

No. of orders	5
Purchase quantity per order (12,000 units ÷ 5)	2,400 units
Cost per unit	₹59.80
(a) Ordering Cost (₹540 × 5 orders)	₹2,700
(b) Carrying Cost (20% of ₹59.80 ×1,200 units)	₹14,352
(c) Material Cost (₹59.80 × 12,000 units)	₹7,17,600
Total Cost {(a) + (b) + (c)}	₹7,34,652
Minimum cost at 2,000 units order level	₹7,32,800
Loss	₹1,852

2. Working:

	Worker- A		**Worker- B**		**Worker- C**	
	Total hours	**Overtime Hours**	**Total hours**	**Overtime Hours**	**Total hours**	**Overtime Hours**
Normal days						
- Monday	10.5	1.0	11.5	2.0	13.5	4.0*
- Wednesday	14.5	5.0*	9.5	-	15.5	6.0*
- Thursday	8.5	-	13.5	4.0*	12.5	3.0
- Friday	15.0	5.5*	8.5	-	8.5	-
- Saturday	-	-	9.5	-	11.5	2.0
Holiday & Sunday						
- Tuesday	9.5	6.0	4.5	6.0	-	-
- Sunday	-	-	5.5	6.0	8.5	6.0
Total Hours	58.0	17.5	62.5	18.0	70.0	21.0

* Eligible for diet allowance

(i) Calculation of Overtime and diet Allowance payable to the workers:

Worker	Overtime Allowance (₹)	Diet Allowance (₹)	Total (₹)
A	1,093.75 (₹ 62.50 × 17.5)	160.00 (₹80 × 2 days)	1,253.75
B	1,125.00 (₹ 62.50 × 18.0)	80.00 (₹80 × 1 day)	1,205.00

C	1,312.50 (₹ 62.50 × 21.0)	160.00 (₹80 × 2 days)	1,472.50
Total	3,531.25	400.00	3,931.25

(ii) Accounting Treatment of overtime and diet allowance:

(a) Worker A & C were involved in a specific job assigned to them:

Overtime and diet allowance of ₹ 2,726.25 payable to worker A & C shall be charged to the specific job and are treated as cost for the job.

Further, Overtime and diet allowance of ₹1,205 payable to Worker-B, will be charged to:

Either, as Cost of production as a part of labour if it is due to labour shortage.

Or, as Cost of production as a part of factory overhead, if it is irregular and to meet production requirement, which arises due to some uncontrollable developments.

Or, either to Responsibility centre in fault or Costing Profit & Loss A/c., if it is irregular and to meet production requirement, which arises due to some controllable developments.

(b) Overtime was due to under-estimation of sales demand provided by the sales department:

The total amount of overtime allowance and diet allowance of ₹ 3,931.25 shall be charged to Sales Department.

(c) Overtime was due to make up a shortfall in production due to sudden demand:

The total amount of overtime allowance and diet allowance of ₹ 3,931.25 shall be charged to Cost of production as factory overhead.

3. (i) Schedule of Cost Allocation among the Departments

	Total	Production Dept.	Administration Dept.	Selling & Distribution Dept.	General Management	Amount to be apportioned
Raw Material Cost	4,25,00,000	4,25,00,000	-	-	-	-
Indirect Material Cost:	10,36,000					-
- Manufacturing		6,00,000	-	-	-	-
- Stores		10,000	-	-	-	-
- Planning		6,000	-	-	-	-
- General admin.		-	3,20,000	-	-	-

- Personnel		-	80,000	-	-	-
- Sales		-	-	20,000	-	-
Salary & Wages	3,40,00,000	1,40,00,000	-	-	-	2,00,00,000
Rent & Property tax	1,00,000	-	-	80,000	-	20,000
Depreciation	22,50,000	12,00,000	-	-	-	10,50,000
Power & fuel	4,10,000	4,00,000	-	10,000	-	-
Insurance premium on machinery	4,80,000	4,80,000	-	-	-	-
Printing & Stationery:	7,00,800					
- Planning		4,800	-	-	-	-
- Marketing		12,000	-	-	-	-
- Finance		-	4,80,000	-	-	-
- Legal		-	24,000	-	-	-
- Sales		-	-	1,80,000	-	-
Audit fees	1,20,000	-	-	-	1,20,000	-
Telephone & Mobile expenses:	4,23,000					
- Marketing		1,10,000	-	-	-	-
- Personnel		-	42,000	-	-	-
- General Management.		-	-	-	26,000	-
- Sales		-	-	65,000	-	-
- Customer Support		-	-	1,80,000	-	-
Travelling exp.:	20,33,000					
- Marketing		4,80,000	-	-	-	-
- Board of Directors & CEO		-	-	-	10,25,000	-
- Sales		-	-	5,28,000	-	-
Software licence renewal fees:	14,24,000					
- Planning		7,20,000	-	-	-	-

- Finance		-	1,20,000	-	-	-
- Store		24,000	-	-	-	-
- Customer support		-	-	5,60,000		-
Total	8,54,76,800	6,05,46,800	10,66,000	16,23,000	11,71,000	2,10,70,000

(ii) Schedule of Cost Apportionment (Primary Distribution)

	Basis	Total	Production Dept.	Administration Dept.	Selling & Distribution Dept.	General Management
Allocated Cost	Direct	6,44,06,800	6,05,46,800	10,66,000	16,23,000	11,71,000
Salary & Wages	Gross Salary (12:7:6:5)	2,00,00,000	80,00,000	46,66,667	40,00,000	33,33,333
Rent & Property tax	Floor area (18:6:5:3)	20,000	11,250	3,750	3,125	1,875
Depreciation:						
- Building	Floor area (18:6:5:3)	9,00,000	5,06,250	1,68,750	1,40,625	84,375
- Air Conditioner	RT (30:15:14:6)	1,50,000	69,231	34,615	32,308	13,846
Insurance premium for employees	Gross Salary (12:7:6)	2,50,000	1,20,000	70,000	60,000	-
Electricity exp.	Units (4:8:3:1)	3,20,000	80,000	1,60,000	60,000	20,000
Subsidy for Meal coupons	No. of employees (18:19:24)	1,83,000	54,000	57,000	72,000	-
Other miscellaneous expenditure	Direct expenses (allocated expenses)	8,05,085	7,56,835	13,325	20,287.5	14,637.5
Total		8,70,34,885	7,01,44,366	62,40,107	60,11,345.5	46,39,066.5

(iii) Schedule of Secondary Distribution:

	Basis	Total	Production Dept.	Administration Dept.	Selling & Distribution Dept.	General Management
Total		8,70,34,885	7,01,44,366	62,40,107	60,11,345.5	46,39,066.5

Allocated and Apportioned costs						
General Management	(2:1:7)	46,39,066.5	9,27,813.3	4,63,906.65	32,47,346.55	(46,39,066.5)
			7,10,72,179.3	67,04,013.65	92,58,692.05	
Administration dept.	(9:11)	67,04,013.65	30,16,806.14	(67,04,013.65)	36,87,207.51	
Total			7,40,88,985.44	-	1,29,45,899.56	

4. (i) Costing Profit & Loss statement

		(₹)
	Materials	28,06,000
	Wages	18,05,750
	Prime Cost	46,11,750
	Production overheads (20% of Prime Cost)	9,22,350
		55,34,100
Less:	Work in Progress	(97,500)
	Manufacturing cost incurred during the period	54,36,600
Add:	Administration Overheads (₹15.75 x 31,000 units)	4,88,250
	Cost of Production	59,24,850
Less:	Closing Finished goods stock($\left(₹59,24,850 \times \frac{1,000}{31,000}\right)$	(1,91,124)
	Cost of Goods Sold	57,33,726
Add:	Selling & Distribution Overheads (₹13 × 30,000 units)	3,90,000
	Cost of Sales	61,23,726
	Profit (Balancing figure)	7,51,274
	Sales	68,75,000

(ii) Production OH A/c

	(₹)		(₹)
To Gen ledger Adj. A/c	9,92,250	By WIP A/c	9,22,350
		By Overhead adj. A/c (Under-absorption)	69,900
	9,92,250		9,92,250

Administration Overheads A/c

	(₹)		(₹)
To Gen Ledger Adj. A/c	5,10,375	By Finished goods A/c	4,88,250
		By Overhead adj. A/c (Under-absorption)	22,125
	5,10,375		5,10,375

Selling & Distribution Overheads A/c

	(₹)		(₹)
To Gen. Ledger Adj A/c	3,68,875	By Cost of Sales A/c	3,90,000
To Overhead Adj. A/c (Over-absorption)	21,125		
	3,90,000		3,90,000

(iii) Reconciliation Statement

		(₹)	(₹)
	Profits as per cost accounts		7,51,274
Add:	Selling & Distribution Overheads- over absorbed	21,125	
	Dividend received	4,90,000	
	Interest on bank deposits	95,000	6,06,125
			13,57,399
Less:	Production Overheads- under-absorbed	69,900	
	Administration Overheads- under-absorbed	22,125	
	Preliminary exp. Written off	22,750	
	Goodwill written off	45,500	
	Fines	7,250	
	Interest on term loan	13,000	
	Loss on sale of machinery	16,250	
	Taxation	1,95,000	
	Write-down of Finished stock (₹1,91,124 – ₹1,30,000)	61,124	(4,52,899)
	Profit as per Financial Accounts		9,04,500

5. **Contract Accounts of M/s DKG LLP for the year ended 31st March, 2016:**

Amount (₹'000)

Particulars	Contract 101	Contract 102	Particulars	Contract 101	Contract 102
To Stores	1,400	300	By Stores return	160	60
To Plant & Machinery	2,000	300	By Transfer to 102	80	-
To Transfer from 101	-	80	By Materials at site	150	30
To Plant hire charges	400	60	By Plant at site	1,700	285
To Wages	600	540	By Cost of work not certified	320	40
To Overheads	150	36	By Cost of work certified (bal. fig) c/d	2,190	909
To Other direct expenses	50	8			
	4,600	1,324		4,600	1,324
To Cost of work certified b/d	2,190	909	By Value of work certified	3,000	750
To Notional profit	810	-	By Notional loss	-	159
	3,000	909		3,000	909

6. (i) **Calculation of Absolute Ton-km for the next month:**

Journey	Distance in km	Weight-Up (in MT)	Ton-km	Weight-Down (in MT)	Ton-km	Total
	(a)	(b)	(c)=(a)×(b)	(d)	(e)=(a)×(d)	(c)+(e)
Delhi to Kochi	2,700	14	37,800	6	16,200	54,000
Delhi to Guwahati	1,890	12	22,680	0	0	22,680
Delhi to Vijayawada	1,840	15	27,600	0	0	27,600
Delhi to Varanasi	815	10	8,150	0	0	8,150
Delhi to Asansol	1,280	12	15,360	4	5,120	20,480
Delhi to Chennai	2,185	10	21,850	8	17,480	39,330
Total	10,710	73	1,33,440	18	38,800	1,72,240

Total Ton-Km = 1,72,240 ton-km

(ii) Calculation of cost per ton-km:

Particulars	Amount (₹)	Amount (₹)
A. Running cost:		
- Diesel Cost {₹13.75 × (10,710 × 2)}	2,94,525.00	
- Engine oil cost $\left(\frac{₹4,200}{13,000\,km}\times 21,420\,km\right)$	6,920.31	
- Cost of loading of goods {₹150 × (73+18)}	13,650.00	
- Depreciation $\left(\frac{₹20,00,000}{7,20,000\,km}\times 21,420\,km\right)$	59,500.00	3,74,595.31
B. Repairs & Maintenance Cost $\left(\frac{₹12,000}{10,000\,km}\times 21,420\,km\right)$		25,704
C. Standing Charges		
- Drivers' salary (₹18,000 × 4 trucks)	72,000	
- Cleaners' salary (₹7,500 × 4 trucks)	30,000	
- Supervision and other general exp.	12,000	1,14,000
Total Cost (A + B + C)		5,14,299.31
Total ton-km		1,72,240
Cost per ton-km		2.99

7. (i) Statement of profitability of an Oil Mill (after carrying out further processing) for the quarter ending 31st March 2016.

Products	Sales Value after further processing	Share of Joint cost	Additional processing cost	Total cost after processing	Profit (loss)
ACH	1,72,500	98,667	43,000	1,41,667	30,833
BCH	15,000	19,733	9,000	28,733	(13,733)
CSH	6,000	4,933	--	4,933	1,067
DSH	45,000	24,667	1,500	26,167	18,833
	2,38,500	1,48,000	53,500	2,01,500	37,000

(ii) Statement of profitability at the split off point

Products	Selling price of split off	Output in units	Sales value at split off point	share of joint cost	profit at split off point
ACH	15.00	8,000	1,20,000	98,667	21,333
BCH	6.00	4,000	24,000	19,733	4,267
CSH	3.00	2,000	6,000	4,933	1,067
DSH	7.50	4,000	30,000	24,667	5,333
			1,80,000	1,48,000	32,000

Note: Share of Joint Cost has been arrived at by considering the sales value at split off point.

8. Standard and actual costs of material for actual output:

Material	SQ	SP (₹)	SQ × SP (₹)	AQ	AQ × AP (₹)	AQ × SP (₹)
A	31,000*	20	6,20,000	32,500	6,59,750	6,50,000
B	69,000**	10	6,90,000	67,000	6,83,400	6,70,000
	1,00,000		13,10,000	99,500	13,43,150	13,20,000

*Material A- 11,000 × 2 + 9,000 × 1 = 31,000 units

**Material B- 11,000 × 3 + 9,000 × 4 = 69,000 units

(i) Material Price Variance = Actual Quantity (Std. Price – Actual Price)

= AQ × SP – AQ × AP

= 13,20,000 – 13,43,150 = 23,150 (Adverse)

(ii) Material Usage Variance = Std. Price (Std. Qty. – Actual Qty.)

= SP × SQ – SP × AQ

= 13,10,000 – 13,20,000 = 10,000 (Adverse)

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

= 13,10,000 – 13,43,150 = 33,150 (Adverse)

9. Working Note:

1. Current utilization 80% capacity and Turnover is ₹ 8,00,000

   No. of units = ₹8,00,000/₹25 = 32,000 units

Variable Cost per units:

Material	7.50
Labour cost	6.25
Variable overheads	3.75
Total Variable Cost	17.50
Selling price	25.00
Contribution per unit (Selling price – Variable Cost)	7.50

Calculation of Total Fixed Cost

Particulars	(₹)
Semi-variable cost	1,80,000
Less: Variable cost (32,000 units × ₹3.75)	1,20,000
Fixed Cost	60,000
Add: Fixed cost upto 80% level	90,000
Total Fixed Cost	1,50,000

2. Present Profit:

Contribution (32,000 units at ₹ 7.50)	2,40,000
Less: Fixed cost	1,50,000
Profit	90,000

(i) Break-even point = Total Fixed Cost /Contribution per unit

= ₹1,50,000/ ₹7.50 = 20,000 Units

At 20,000 units, output level is = $\frac{20,000}{32,000} \times 80\% = 50\%$

i.e. at 50% activity level, this company reaches at BEP.

(ii) Sales (Units) = $\frac{\text{Fixed Cost + Profit}}{\text{Contribution per unit}}$

8% of sales = 8% of ₹25 = ₹ 2 per unit profit.

Let us assume 'S' is the no. of units to be sold, hence profit will be 2S

So, S = $\frac{₹1,50,000 + 2S}{₹7.50}$

Or, 7.50 S – 2 S = 1,50,000

Or, S = 1,50,000 ÷ 5.50 = 27,273 units.

(iii) Sales (units) = $\frac{₹1,50,000 + ₹95,000}{₹7.50}$

= ₹ 2,45,000 ÷ ₹ 7.50 = 32,667 units

32,667 units is beyond 80% activity level. In such case, the fixed cost will be increased by ₹ 20,000 to ₹ 1,70,000.

Then, S = $\frac{₹1,70,000 + ₹95,000}{₹7.50} = 35,333$ units i.e. $\frac{35,333}{40,000} \times 100$ = 88.33% activity level.

(iv) When BEP is 40% of activity level, i.e., 40% of 40,000 = 16,000 units BEP

Variable Cost (16,000 × ₹17.50)	= ₹ 2,80,000
Add: fixed cost	= ₹ 1,50,000
Total cost	₹ 4,30,000
Total cost	= Sales at BEP ₹ 4,30,000

Selling price per unit = ₹ 4,30,000 ÷ 16,000 units = ₹ 26.875 per unit.

10. (a) Flexible Budget

Level of students	30	60	90	120	150
Variable Costs (₹)					
Breakfast at ₹ 50	1,500	3,000	4,500	6,000	7,500
Lunch at ₹ 100	3,000	6,000	9,000	12,000	15,000
Tea at ₹ 30	900	1,800	2,700	3,600	4,500
Entrance fee at zoo at ₹ 20	600	1,200	1,800	2,400	3,000
Variable cost at ₹ 200	6,000	12,000	18,000	24,000	30,000
Semi-variable costs (₹)					
Bus hire charge	6,500	13,000	13,000	19,500	19,500
Special permit fee	500	1,000	1,000	1,500	1,500
Allowance to teachers	1,000	2,000	2,000	3,000	3,000
	8,000	16,000	16,000	24,000	24,000
Fixed costs (₹)					
Block entrance fee other than zoo	2,500	2,500	2,500	2,500	2,500

Prizes to students for games	2,500	2,500	2,500	2,500	2,500
	5,000	5,000	5,000	5,000	5,000
Total Cost	19,000	33,000	39,000	53,000	59,000
(b) Average cost per student (Total Cost /Number of Students)	633.33	550.00	433.33	441.67	393.33

(c) Calculation of Break-even level of students:

Collection per student	₹ 450
Variable cost per student	₹ 200
Contribution per student	₹ 250

Semi-variable costs for levels of 50, 100 and 150 students.

Level of students	50	100	150
Semi-variable costs	8,000	16,000	24,000
Fixed costs	5,000	5,000	5,000
	13,000	21,000	29,000
Break- even students [Fixed cost / Contribution per student]	52	84	116

There are two practically possible break-even levels, i.e., 84 students and 116 students. Break-even level of 52 is outside the level of 50 and hence shall be ignored.

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART II: FINANCIAL MANAGEMENT

QUESTIONS

Time Value of Money

1. Ms. A has purchased a smart phone from a shop for ₹25,000. She has paid ₹5,000 as down payment and the rest will be paid in equated monthly instalments (EMI) for 2 years. The interest rate charged by the bank is 14% p.a.

   Required:

   (i) Calculate the amount of EMI

   (ii) Calculate the total amount of interest payable to the bank.

Ratio Analysis

2. From the following information, prepare a summarised Balance Sheet as at 31st March, 2016:

Working Capital	₹2,40,000
Bank overdraft	₹40,000
Fixed Assets to Proprietary ratio	0.75
Reserves and Surplus	₹1,60,000
Current ratio	2.5
Liquid ratio	1.5

Fund Flow Analysis

3. The following are the Balance Sheet of Peacock Limited as on 31st March, 20X8 and 31st March, 20X9.

	Rupees 31st March, 20X8	Rupees 31st March, 20X9
Liabilities		
Share capital	44,00,000	66,00,000
Reserves and Surplus	27,50,000	38,50,000
Depreciation	8,80,000	13,20,000
Bank Loan	17,60,000	8,80,000
Trade Payables	13,20,000	14,85,000
Proposed dividend	4,00,000	6,00,000
Provision for taxation	4,00,000	5,50,000

	1,19,10,000	1,52,85,000
Assets		
Land	33,00,000	44,00,000
Plant and Machinery	50,60,000	69,30,000
Inventories	19,80,000	22,00,000
Trade Receivables	11,00,000	17,05,000
Cash and Bank balances	4,70,000	50,000
	1,19,10,000	1,52,85,000

Additional Information:

(a) The machine which was purchased earlier for ₹ 6,00,000 was sold during the financial year 20X8-20X9 for ₹ 40,000. The book value of the machine was ₹ 60,000. A new machinery was purchased during the financial year.

(b) The company had issued new shares to the extent of ₹22,00,000.

You are required to prepare:

1. Statement showing changes in the Working Capital;
2. Statement of Sources and Application of funds.

Cost of Capital

4. XYZ Ltd. is currently earning a profit after tax of ₹25,00,000 and its shares are quoted in the market at ₹450 per share. The company has 1,00,000 shares outstanding and has not debt in its capital structure. It is expected that the same level of earnings will be maintained for future years also. The company has 100 per cent pay-out policy.

   Required:

   (i) Calculated the Cost of equity

   (ii) If the company's pay-out ratio is assumed to be 70% and it earns 20% rate of return on its investment, then what would be the firm's cost of equity?

Capital Structure

5. A Company needs ₹31,25,000 for the construction of a new plant. The following three plans are feasible:

   I The Company may issue 3,12,500 equity shares at ₹10 per share.

   II The Company may issue 1,56,250 equity shares at ₹10 per share and 15,625 debentures of ₹100 denomination bearing an 8% rate of interest.

   III The Company may issue 1,56,250 equity shares at ₹10 per share and 15,625 preference shares at ₹ 100 per share bearing an 8% rate of dividend.

(i) If the Company's earnings before interest and taxes are ₹ 62,500, ₹1,25,000, ₹ 2,50,000, ₹3,75,000 and ₹ 6,25,000, what are the earnings per share under each of three financial plans? Assume a Corporate Income tax rate of 40%.

(ii) Which alternative would you recommend and why?

(iii) Determine the EBIT-EPS indifference points by formulae between Financing Plan I and Plan II and Plan I and Plan III.

Leverages

6. Calculate the operating leverage, financial leverage and combined leverage from the following data under Situation I and II and Financial Plan A and B:

Installed Capacity	4,000 units
Actual Production and Sales	75% of the Capacity
Selling Price	₹30 per unit
Variable Cost	₹15 per unit

Fixed Cost:

Under Situation I	₹15,000
Under Situation-II	₹20,000

Capital Structure:

	Financial Plan	
	A (₹)	B (₹)
Equity	10,000	15,000
Debt (Rate of Interest at 20%)	10,000	5,000
	20,000	20,000

Investment Decisions/ Capital Budgeting

7. A company has to make a choice between two projects namely A and B. The initial capital outlay of two Projects is ₹1,35,000 and ₹2,40,000 respectively for A and B. There will be no scrap value at the end of the life of both the projects. The opportunity cost of capital of the company is 16%. The annual incomes are as under:

Year	Project A	Project B	Discounting factor @ 16%
1	–	60,000	0.862
2	30,000	84,000	0.743
3	1,32,000	96,000	0.641

4	84,000	1,02,000	0.552
5	84,000	90,000	0.476

You are required to calculate for each project:

(i) Discounted payback period

(ii) Profitability index

(iii) Net present value

Management of Working Capital

8. The following information has been extracted from the records of a company:

Product cost sheet	₹ per unit
Raw materials	45
Direct labour	20
Overheads	40
Total	105
Profit	15
Selling price	120

– Raw materials are in stock on an average of two months.

– The materials are in process on an average for 4 weeks. The degree of completion is 50%.

– Finished goods stock on an average is for one month.

– Time lag in payment of wages and overheads is 1½ weeks.

– Time lag in receipt of proceeds from debtors is 2 months.

– Credit allowed by suppliers is one month.

– 20% of the output is sold against cash.

– The company expects to keep a cash balance of ₹1,00,000.

– Take 52 weeks per annum.

The company is poised to manufacture and sell 1,44,000 units in the year.

You are required to prepare a statement showing the Working Capital requirements of the company.

Receivable Management

9. A Ltd. has a total sale of ₹ 3.2 crores and its average collection period is 90 days. The past experience indicates that bad-debt losses are 1.5% on sales. The expenditure

incurred by the firm in administering its receivable collection efforts are ₹5,00,000. A factor is prepared to buy the firm's receivables by charging 2% commission. The factor will pay advance on receivables to the firm at an interest rate of 18% p.a. after withholding 10% as reserve.

Calculate the effective cost of factoring to the Firm.

Miscellaneous

10. (a) The profit maximization is not an operationally feasible criterion." Comment on it.

(b) What is debt securitisation? Explain the basics of debt securitisation process.

SUGGESTED ANSWERS

1. (i) Calculation of the amount of EMI:

$$\text{EMI} = \text{Amount}\left[\frac{i(1+i)^n}{(1+i)^n - 1}\right]$$

Where, i = rate of interest divided by 12 i.e. 0.14 ÷ 12 = 0.01167

n = Tenure of loan in months i.e. 24 months

Amount = ₹ 25,000 – ₹ 5,000 = ₹ 20,000.

$$\text{EMI} = ₹20{,}000\left[\frac{0.01167(1+0.01167)^{24}}{(1+0.01167)^{24} - 1}\right] = ₹20{,}000\left[\frac{0.01167(1.01167)^{24}}{(1.01167)^{24} - 1}\right]$$

$$\text{Or, EMI} = ₹20{,}000\left[\frac{0.01167 \times 1.32}{1.32 - 1}\right] = ₹20{,}000 \times \frac{0.0154}{0.32} = ₹\ 962.5$$

(ii) Calculation of total amount of interest payable to bank:

Amount of EMI × No. of months – Amount of loan

= ₹962.5 × 24 – ₹20,000 = ₹3,100

[Value of EMI and Interest may slightly differ due to rounding off error]

2. Working notes:

1. Computation of Current Assets and Current Liabilities:

$$\frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{2.5}{1} \text{ or } \frac{\text{Current Assets}}{2.5} = \frac{\text{Current Liabilities}}{1} = k \text{ (say)}$$

Or, Current Assets = 2.5 k and Current Liabilities = k

Or, Working capital = (Current Assets – Current Liabilities)

Or, ₹2,40,000 = k (2.5 – 1) = 1.5 k

Or, k = ₹1,60,000

∴ Current liabilities = ₹1,60,000

Current assets = ₹1,60,000 × 2.5 = ₹4,00,000

2. Computation of Inventories

$$\text{Liquid ratio} = \frac{\text{Liquid assets}}{\text{Current liabilities}}$$

$$\text{Or, } 1.5 = \frac{\text{Current assets - Inventories}}{₹1,60,000}$$

Or, 1.5 × ₹1,60,000 = ₹4,00,000 – Inventories

Or, Inventories = ₹1,60,000

3. Computation of Proprietary fund; Fixed assets; Capital and Trade payables

$$\text{Proprietary ratio} = \frac{\text{Fixed assets}}{\text{Proprietary fund}} = 0.75$$

∴ Fixed assets = 0.75 Proprietary fund

and Net working capital = 0.25 Proprietary fund

Or, ₹2,40,000/0.25 = Proprietary fund

Or, Proprietary fund = ₹9,60,000

and Fixed assets = 0.75 proprietary fund

= 0.75 × ₹9,60,000

= ₹7,20,000

Capital = Proprietary fund – Reserves & Surplus

= ₹9,60,000 – ₹1,60,000

= ₹8,00,000

Trade payables = (Current liabilities – Bank overdraft)

= (₹1,60,000 – ₹40,000)

= ₹1,20,000

Construction of Balance sheet

(Refer to working notes 1 to 3)

Balance Sheet as at 31st March, 2016

Liabilities	(₹)	Assets	(₹)
Capital	8,00,000	Fixed assets	7,20,000
Reserves & Surplus	1,60,000	Inventories	1,60,000
Bank overdraft	40,000	Current assets (other than inventories)	2,40,000
Trade Payables	1,20,000		
	11,20,000		11,20,000

3. (1) Statement of Changes in Working Capital

Particulars	31st March		Working Capital	
	20X8 (₹)	20X9 (₹)	Increase (₹)	Decrease (₹)
A Current Assets:				
Inventories	19,80,000	22,00,000	2,20,000	--
Trade Receivables	11,00,000	17,05,000	6,05,000	--
Cash and Bank	4,70,000	50,000	--	4,20,000
Total (A)	35,50,000	39,55,000		
B Current Liabilities:				
Trade Payables	13,20,000	14,85,000	--	1,65,000
Provision for Taxation	4,00,000	5,50,000	--	1,50,000
Total (B)	17,20,000	20,35,000		
Working Capital (A – B)	18,30,000	19,20,000		
Increase in Working Capital	90,000			90,000
Total	19,20,000	19,20,000	8,25,000	8,25,000

(2) Funds Flow Statement for the year ending 31st March, 20X9

	(₹)
A. Sources of Funds:	
(i) Fund from Business Operations (WN-1)	27,00,000
(ii) Proceeds from issue of shares	22,00,000

	(iii) Proceeds from sale of machinery	40,000
	Total sources	49,40,000
B.	**Application of Funds:**	
	(i) Payment of dividend	4,00,000
	(ii) Repayment of bank loan	8,80,000
	(iii) Purchase of land	11,00,000
	(iv) Purchase of machinery (WN-3)	24,70,000
	Total uses	48,50,000
	Net Increase in Working Capital (A – B)	90,000

Working Notes:

1. Computation of Funds from Business Operation

		(₹)
	Reserve and surplus as on March 31, 20X9	38,50,000
Add:	Provision for depreciation (WN- 2)	9,80,000
	Proposed dividend	6,00,000
	Loss on sale of machinery	20,000
		54,50,000
Less:	Profit and loss as on March 31, 20X8	27,50,000
	Fund from Operations	27,00,000

2. Provision for Depreciation A/c

	(₹)		(₹)
To Plant & Machinery A/c	5,40,000	By Balance b/d	8,80,000
To Balance c/d	13,20,000	By Profit & Loss A/c (Balancing figure)	9,80,000
	18,60,000		18,60,000

3. Plant & Machinery A/c

	(₹)		(₹)
To Balance b/d	50,60,000	By Prov. for Dep. A/c	5,40,000
To Bank (Purchases)	24,70,000	By Cash	40,000
		By Profit & Loss A/c (Loss on Sale)	20,000

		By Balance c/d	69,30,000
	75,30,000		75,30,000

4. (i) Since, the earnings for the company will remain same for future years and the pay-out ratio is 100 per cent too. It indicates that the dividend is equal to earnings per share and growth rate is zero per cent.

Therefore, the Cost of equity (K_e) = $\frac{\text{Earnings per share (EPS)}}{\text{Market price per share }(P_0)}$

Where, EPS = $\frac{\text{Earnings available to shareholders}}{\text{No. of shares outstanding}} = \frac{₹25,00,000}{1,00,000}$ = ₹25

and P_0 = ₹450

Therefore, K_e = $\frac{₹25}{₹450}$ = 0.055 or 5.55%

(ii) In this case pay-out ratio is 70% and the earning rate on investment is 20%, which means the amount retained after payment of dividend can be invested to earn an interest of 20% p.a.

The Cost of Equity (K_e) = $\frac{\text{Earnings per share (EPS)} \times \text{payout ratio}}{\text{Market price per share }(P_0)} + \text{growth rate}$

$= \frac{₹25 \times 70\%}{₹450} + (30\% \times 20\%)$

$= \frac{₹17.5}{₹450} + 0.06$ = 0.0988 or 9.89%

5. (i) Computation of EPS under three-financial plans.

Plan I: Equity Financing

	(₹)	(₹)	(₹)	(₹)	(₹)
EBIT	62,500	1,25,000	2,50,000	3,75,000	6,25,000
Interest	0	0	0	0	0
EBT	62,500	1,25,000	2,50,000	3,75,000	6,25,000
Less: Taxes 40%	(25,000)	(50,000)	(1,00,000)	(1,50,000)	(2,50,000)
PAT	37,500	75,000	1,50,000	2,25,000	3,75,000
No. of equity shares	3,12,500	3,12,500	3,12,500	3,12,500	3,12,500
EPS	0.12	0.24	0.48	0.72	1.20

Plan II: Debt – Equity Mix

	(₹)	(₹)	(₹)	(₹)	(₹)
EBIT	62,500	1,25,000	2,50,000	3,75,000	6,25,000
Less: Interest	(1,25,000)	(1,25,000)	(1,25,000)	(1,25,000)	(1,25,000)
EBT	(62,500)	0	1,25,000	2,50,000	5,00,000
Less: Taxes 40%	25,000*	0	(50,000)	(1,00,000)	(2,00,000)
PAT	(37,500)	0	75,000	1,50,000	3,00,000
No. of equity shares	1,56,250	1,56,250	1,56,250	1,56,250	1,56,250
EPS	(0.24)	0	0.48	0.96	1.92

* The Company will be able to set off losses against other profits. If the Company has no profits from operations, losses will be carried forward.

Plan III: Preference Shares – Equity Mix

	(₹)	(₹)	(₹)	(₹)	(₹)
EBIT	62,500	1,25,000	2,50,000	3,75,000	6,25,000
Less: Interest	0	0	0	0	0
EBT	62,500	1,25,000	2,50,000	3,75,000	6,25,000
Less: Taxes (40%)	(25,000)	(50,000)	(1,00,000)	(1,50,000)	(2,50,000)
PAT	37,500	75,000	1,50,000	2,25,000	3,75,000
Less: Pref. dividend	(1,25,000)*	(1,25,000)*	(1,25,000)	(1,25,000)	(1,25,000)
PAT for equity shareholders	(87,500)	(50,000)	25,000	1,00,000	2,50,000
No. of Equity shares	1,56,250	1,56,250	1,56,250	1,56,250	1,56,250
EPS	(0.56)	(0.32)	0.16	0.64	1.60

*In case of cumulative preference shares, the dividend gets accumulated if there is insufficient profit to pay dividend. If we assume it as non-cumulative preference shares, then in this case dividend amount will be lower of PAT and amount of preference dividend.

(ii) The choice of the financing plan will depend on the state of economic conditions. If the company's sales are increasing, the EPS will be maximum under Plan II: Debt – Equity Mix. Under favourable economic conditions, debt financing gives more benefit due to tax shield availability than equity or preference financing.

(iii) EBIT – EPS Indifference Point- Plan I and Plan II:

$$\frac{(\text{EBIT})\times(1\text{-}T_C)}{N_1} = \frac{(\text{EBIT}-\text{Interest})\times(1-T_C)}{N_2}$$

$$\frac{\text{EBIT}(1-0.40)}{3,12,500} = \frac{(\text{EBIT}-1,25,000)\times(1-0.40)}{1,56,250}$$

$$\text{EBIT} = \frac{3,12,500}{3,12,500-1,56,250}\times 1,25,000$$

= ₹2,50,000

EBIT – EPS Indifference Point: Plan I and Plan III

$$\frac{\text{EBIT}(1-T_c)}{N_1} = \frac{\text{EBIT}(1-T_c)-\text{Pref. Div.}}{N_2}$$

$$\text{EBIT} = \frac{N_1}{N_1-N_2}\times\frac{\text{Pref. Div.}}{1\text{-}T_C}$$

$$= \frac{3,12,500}{3,12,500-1,56,250}\times\frac{1,25,000}{1-0.4} = ₹4,16,666.67$$

6. (i) Operating leverages:

Particulars	Situation-I (₹)	Situation-II (₹)
Sales (S) (3,000 units @ ₹ 30/- per unit)	90,000	90,000
Less: Variable Cost (VC) @ ₹15 per unit	(45,000)	(45,000)
Contribution (C)	45,000	45,000
Less: Fixed Cost (FC)	15,000	20,000
EBIT	30,000	25,000
Operating Leverage $\left(\frac{C}{\text{EBIT}}\right)$	$\frac{45,000}{30,000}$	$\frac{45,000}{25,000}$
	= 1.5	= 1.8

(ii) Financial Leverages:

	A (₹)	B (₹)
Situation I:		
EBIT	30,000	30,000
Less: Interest on debt	(2,000)	(1,000)
EBT	28,000	29,000
Financial Leverage $\left(\frac{EBIT}{EBT}\right)$	$\frac{30,000}{28,000}$	$\frac{30,000}{29,000}$
	= 1.07	= 1.03
Situation-II:		
EBIT	25,000	25,000
Less: Interest on debt	(2,000)	(1,000)
EBT	23,000	24,000
Financial Leverage $\left(\frac{EBIT}{EBT}\right)$	$\frac{25,000}{23,000}$	$\frac{25,000}{24,000}$
	= 1.09	= 1.04

(iii) Combined Leverages:

	A (₹)	B (₹)
(a) Situation I	1.5 × 1.07 = 1.61	1.5 × 1.03 = 1.55
(b) Situation II	1.8 × 1.09 = 1.96	1.8 × 1.04 = 1.87

7. Working Notes:

(1) Computation of Net Present Values of Projects

Year	Cash flows		Discounting factor @ 16%	Discounted Cash flow	
	Project A (₹) (1)	Project B (₹) (2)	(3)	Project A (₹) (3) × (1)	Project B (₹) (3) × 2)
0	(1,35,000)	(2,40,000)	1.000	(1,35,000)	(2,40,000)
1	–	60,000	0.862	–	51,720
2	30,000	84,000	0.743	22,290	62,412
3	1,32,000	96,000	0.641	84,612	61,536

4	84,000	1,02,000	0.552	46,368	56,304
5.	84,000	90,000	0.476	39,984	42,840
Net Present Value				58,254	34,812

(2) Computation of Cumulative Present Values of Projects Cash inflows

Year	Project A (₹)		Project B (₹)	
	PV of cash inflows	Cumulative PV	PV of cash inflows	Cumulative PV
1	–	–	51,720	51,720
2	22,290	22,290	62,412	1,14,132
3	84,612	1,06,902	61,536	1,75,668
4	46,368	1,53,270	56,304	2,31,972
5	39,984	1,93,254	42,840	2,74,812

(i) **Discounted payback period**: (Refer to Working note 2)

Cost of Project A = ₹1,35,000

Cost of Project B = ₹2,40,000

Cumulative PV of cash inflows of Project A after 4 years = ₹1,53,270

Cumulative PV of cash inflows of Project B after 5 years = ₹2,74,812

A comparison of projects cost with their cumulative PV clearly shows that the project A's cost will be recovered in less than 4 years and that of project B in less than 5 years. The exact duration of discounted payback period can be computed as follows:

	Project A	Project B
Excess PV of cash inflows over the project cost (₹)	18,270 (₹1,53,270 – ₹1,35,000)	34,812 (₹2,74,812 – ₹2,40,000)
Computation of period required to recover excess amount of cumulative PV over project cost (Refer to Working note 2)	0.39 year (₹18,270 / ₹46,368)	0.81 years (₹34,812 / ₹42,840)
Discounted payback period	3.61 year (4 – 0.39) years	4.19 years (5 – 0.81) years

(ii) Profitability Index: $= \dfrac{\text{Sum of discount cash inflows}}{\text{Initian cash outlay}}$

Profitability Index (*for Project A)* $= \dfrac{₹1,93,254}{₹1,35,000} = 1.43$

Profitability Index (*for Project B)* $= \dfrac{₹2,74,812}{₹2,40,000} = 1.15$

(iii) Net present value= ₹ 58,254

(for Project A)

(Refer to Working note 1)

Net present value = ₹ 34,812 (for Project B)

8. Statement showing the Working Capital Requirement of the Company

		(₹)
A.	**Current Assets:**	
	Stock of raw materials [(₹64,80,000 / 12 months) × 2 months]	10,80,000
	Work-in-progress [(₹1,51,20,000 × 4) / 52 weeks × 50%]	5,81,538
	Finished goods (₹1,51,20,000 / 12 months)	12,60,000
	Receivables (Refer to Working note 2)	20,16,000
	Cash balances	1,00,000
		50,37,538
B.	**Current Liabilities:**	
	Creditors of raw materials (₹64,80,000 / 12 months)	5,40,000
	Creditors for wages & overheads $\left(\dfrac{₹86,40,000}{52 \text{ weeks}} \times 1.5 \text{ weeks}\right)$	2,49,231
		7,89,231
	Net Working Capital (A – B)	42,48,307

Working Notes:

1.	Annual raw materials requirements (₹) (1,44,000 units × ₹45)	64,80,000
	Annual direct labour cost (₹) (1,44,000 units × ₹20)	28,80,000
	Annual overhead costs (₹) (1,44,000 units × ₹40)	57,60,000
	Total Cost (₹)	1,51,20,000
2.	Total Cost of Sales: (1,44,000 units × ₹105)	1,51,20,000
	Total cost of credit sales (80% of ₹1,51,20,000)	1,20,96,000
	Two months' sales (₹1,20,96,000 / 12 × 2 months)	20,16,000

9.

	(₹)
Average level of Receivables (₹3,20,00,000 × 90/360)	80,00,000
Factoring commission (₹80,00,000 × 2/100)	(1,60,000)
Factoring reserve (₹80,00,000 × 10/100)	(8,00,000)
Amount available for advance [₹80,00,000 - (₹1,60,000 + ₹ 8,00,000)]	70,40,000
Factor will deduct his interest @ 18%: $\left(\frac{70,40,000 \times 18 \times 90}{100 \times 360}\right)$	3,16,800

Advance to be paid = ₹70,40,000 – ₹3,16,800 = ₹67,23,200

	(₹)
Annual Cost of Factoring to the Firm:	
Factoring commission (₹1,60,000 × 360/90)	6,40,000
Interest charges (₹3,16,800 × 360/90)	12,67,200
Total	19,07,200
Firm's Savings on taking Factoring Service:	
Cost of credit administration saved	5,00,000
Cost of Bad Debts (₹3,20,00,000 × 1.5/100) avoided	4,80,000
Total	9,80,000
Net Cost to the firm (₹19,07,200 – ₹9,80,000)	9,27,200
Effective rate of interest to the firm = $\left(\frac{₹9,27,200 \times 100}{₹67,23,200}\right)$	13.79%

Note: The number of days in a year have been assumed to be 360 days.

10. (a) "The profit maximisation is not an operationally feasible criterion." This statement is true because Profit maximisation can be a short-term objective for any organisation and cannot be its sole objective. Profit maximization fails to serve as an operational criterion for maximizing the owner's economic welfare. It fails to provide an operationally feasible measure for ranking alternative courses of action in terms of their economic efficiency. It suffers from the following limitations:

(i) Vague term: The definition of the term profit is ambiguous. Does it mean short term or long term profit? Does it refer to profit before or after tax? Total profit or profit per share?

(ii) Timing of Return: The profit maximization objective does not make distinction between returns received in different time periods. It gives no consideration to the time value of money, and values benefits received today and benefits received after a period as the same.

(iii) It ignores the risk factor.

(iv) The term maximization is also vague.

(b) **Debt Securitisation:** It is a method of recycling of funds. It is especially beneficial to financial intermediaries to support the lending volumes. Assets generating steady cash flows are packaged together and against this asset pool, market securities can be issued, e.g. housing finance, auto loans, and credit card receivables.

Process of Debt Securitisation

(i) The origination function – A borrower seeks a loan from a finance company, bank. The credit worthiness of borrower is evaluated and contract is entered into with repayment schedule structured over the life of the loan.

(ii) The pooling function – Similar loans on receivables are clubbed together to create an underlying pool of assets. The pool is transferred in favour of Special Purpose Vehicle (SPV), which acts as a trustee for investors.

(iii) The securitisation function – SPV will structure and issue securities on the basis of asset pool. The securities carry a coupon and expected maturity which can be asset-based/mortgage based. These are generally sold to investors through merchant bankers. Investors are – pension funds, mutual funds, insurance funds.

The process of securitization is generally without recourse i.e. investors bear the credit risk and issuer is under an obligation to pay to investors only if the cash flows are received by him from the collateral. The benefits to the originator are that assets are shifted off the balance sheet, thus giving the originator recourse to off-balance sheet funding.

PAPER – 4: TAXATION

PART – I: STATUTORY UPDATE

Significant Notifications and Circulars in income-tax and indirect taxes issued between 1st May, 2016 and 31st October, 2016

A. INCOME TAX

The income-tax law, as amended by the Finance Act, 2016, including significant notifications/circulars issued up to 31st October, 2016 are applicable for May, 2017 examination. The relevant assessment year for May, 2017 examination is A.Y.2017-18. The September 2016 edition of the Study Material for Paper 4: Taxation Part I: Income-tax is based on the provisions of income-tax law as amended by the Finance Act, 2016 and significant notifications/circulars issued upto 30th April, 2016. The significant notifications and circulars issued between 1st May, 2016 and 31st October, 2016, which are also relevant for May, 2017 examination, are given hereunder:

I. NOTIFICATIONS

1. Notification of Cost Inflation Index for Financial Year 2016-17 [Notification No. 42/2016, dated 2.6.2016]

Clause (v) of Explanation to section 48 defines "Cost Inflation Index", in relation to a previous year, to mean such Index as the Central Government may, by notification in the Official Gazette, specify in this behalf, having regard to 75% of average rise in the Consumer Price Index (Urban) for the immediately preceding previous year to such previous year.

Accordingly, the Central Government has, in exercise of the powers conferred by clause (v) of Explanation to section 48, specified the Cost Inflation Index for the financial year 2016-17 as 1125.

S. No.	Financial Year	Cost Inflation Index	S. No.	Financial Year	Cost Inflation Index
1.	1981-82	100	19.	1999-2000	389
2.	1982-83	109	20.	2000-01	406
3.	1983-84	116	21.	2001-02	426
4.	1984-85	125	22.	2002-03	447
5.	1985-86	133	23.	2003-04	463
6.	1986-87	140	24.	2004-05	480
7.	1987-88	150	25.	2005-06	497
8.	1988-89	161	26.	2006-07	519
9.	1989-90	172	27.	2007-08	551
10.	1990-91	182	28.	2008-09	582

11.	1991-92	199	29.	2009-10	632
12.	1992-93	223	30.	2010-11	711
13.	1993-94	244	31.	2011-12	785
14.	1994-95	259	32.	2012-13	852
15.	1995-96	281	33.	2013-14	939
16.	1996-97	305	34.	2014-15	1024
17.	1997-98	331	35.	2015-16	1081
18.	1998-99	351	**36.**	**2016-17**	**1125**

2. Method for determining the amount of expenditure in relation to income which does not form part of the total income under Rule 8D [Notification No 43/2016, dated 02-06-2016]

As per section 14A(1), for the purposes of computing the total income under Chapter IV of the Income-tax Act, 1961, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income, which does not form part of total income under the Income-tax Act, 1961.

Section 14A(2) provides that the Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under Income-tax Act, 1961 in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure.

Rule 8D prescribes the method for determining the amount of expenditure in relation to income not includible in total income. Since there have been considerable number of disputes on the application of the formula prescribed therein, the Finance Minister had, in para 167 of his Budget Speech [Union Budget 2016-17] proposed to amend Rule 8D to restrict the disallowance to 1% of the average monthly value of investments yielding exempt income, but not exceeding the actual expenditure claimed.

Accordingly, vide this notification, the Central Government has substituted sub-rule (2) and omitted sub-rule (3) of the said Rule 8D. New sub-rule (2) provides that the expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts:

(i) the amount of expenditure directly relating to income which does not form part of total income; and

(ii) an amount equal to 1% of the annual average of the monthly averages of the opening and closing balances of the value of investment, income from which does not or shall not form part of total income:

However, the amount referred to in clause (i) and clause (ii) shall not exceed the total expenditure claimed by the assessee.

3. **Exemption from TDS on specified payments made to banks etc. [Notification No. 47/2016, dated 17-06-2016]**

Section 197A(1F) provides that no deduction of tax shall be made from such specified payment to such institution, association or body or class of institutions, associations or bodies as may be notified by the Central Government.

Accordingly, the Central Government has notified that no deduction of tax under Chapter XVII of the Income-tax Act, 1961 shall be made on specified payments, in case such payments are made by a person to a bank listed in the Second Schedule to the Reserve Bank of India Act, 1934, excluding a foreign bank, or to any payment systems company authorised by the Reserve Bank of India under section 4(2) of the Payment and Settlement Systems Act, 2007. The specified payments are:

(i) bank guarantee commission;

(ii) cash management service charges;

(iii) depository charges on maintenance of DEMAT accounts;

(iv) charges for warehousing services for commodities;

(v) underwriting service charges;

(vi) clearing charges (MICR charges) including interchange fee or any other similar charges, by whatever name called, charged at the time of settlement or for clearing activities under the Payment and Settlement Systems Act, 2007;

(vii) credit card or debit card commission for transaction between merchant establishment and acquirer bank.

4. **Relaxation from deduction of tax at higher rate under section 206AA [Notification No 53/2016, dated 24-06-2016]**

Under section 206AA, any person who is entitled to receive any sum or income or amount on which tax is deductible under Chapter XVIIB shall furnish his Permanent Account Number (PAN) to the person responsible for deducting such tax, failing which tax shall be deducted at –

(1) the rate mentioned in the relevant provisions of the Act or

(2) the rate or rates in force or

(3) the rate of 20%

whichever is higher.

The provisions of section 206AA also apply to non-residents, on account of which they have to obtain and furnish PAN. Otherwise, higher rate of tax deduction is attracted even if tax on such income is payable at a lower rate on account of applicability of special provisions of the Act or the relevant double taxation avoidance agreement.

The benefit of non-applicability of the provisions of section 206AA was so far only in respect of payment of interest on long-term bonds by an Indian company or a business trust as referred to in section 194LC to non-corporate non-residents or foreign companies.

For the purpose of reducing the compliance burden, sub-section (7) of section 206AA has been substituted with effect from 1st June, 2016 to provide for non-applicability of the requirements contained in section 206AA to a non-corporate non-resident or a foreign company, in respect of any other payment, other than interest on long-term bonds as referred to in section 194LC, subject to such conditions as may be prescribed.

Accordingly, the CBDT has, vide this notification, inserted Rule 37BC to provide that the provisions of section 206AA shall not apply to a non-corporate non-resident, or to a foreign company not having PAN in respect of payments in the nature of interest, royalty, fees for technical services and payments on transfer of any capital asset on furnishing the following details and documents to the deductor:

- Name, e-mail id, contact number;
- address in the country or specified territory outside India of which the deductee is a resident;
- a certificate of his resident in any country or specified territory outside India from the Government of that country or specified territory, if the law of that country or specified territory provides for issuance of such certificate;
- Tax Identification Number of the deductee in the country or specified territory of his residence and in case no such number is available, then a unique number on the basis of which the deductee is identified by the Government of that country or specified territory of which he claims to be a resident.

5. Backward districts of states of Telangana, West Bengal, Bihar and Andhra Pradesh notified for the purposes of eligibility for higher additional depreciation under section 32(1)(iia) and investment allowance under section 32AD [Notification No. 61/2016, dated 20-07-2016 and Notification No. 85/2016, dated 28-09-2016]

Under section 32, depreciation on assets used for the purposes of business and profession is allowable as deduction while computing income under the head "Profits and gains of business or profession".

Section 32(1)(iia) provides for additional depreciation @ 20% for new machinery or plant (other than ships and aircraft), acquired and installed, by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation or generation and distribution of power.

In order to promote economic activities in the backward areas of the states of Andhra Pradesh, Telangana, West Bengal and Bihar, the Finance Act, 2015 had inserted a proviso to section 32(1)(iia) to provide an increased rate of additional depreciation @ 35% to an assessee who sets up an undertaking or enterprise for manufacture or production of any article or thing, on or after 01.04.2015 in any backward area notified by the Central Government in this behalf, in such states, and acquires and installs any new machinery or plant (other than ships and aircraft) for the purposes of the said undertaking or enterprise during the period from 01.04.2015 to 31.3.2020 in the said backward area.

Further, section 32AD was inserted by the Finance Act, 2015 to provide incentive in the form of an additional investment allowance @ 15% of the cost of the new plant and machinery acquired and installed by an assessee who sets up an undertaking or enterprise for manufacture or production of any article or thing, on or after 01.04.2015 in any backward area notified by the Central Government in this behalf, in such states, and acquires and installs any new asset for the purposes of the said undertaking or enterprise during the period from 1.4.2015 to 31.3.2020 in the said backward area.

Both for the purpose of claim of investment allowance under section 32AD and higher additional depreciation under section 32(1)(iia), the Central Government has, vide this notification, notified the following districts of the states of Telangana, West Bengal, Bihar and Andhra Pradesh as backward areas:

S.No.	Telangana	West Bengal	Bihar	Andhra Pradesh
1.	Adilabad	South 24 Parganas	Arwal	Anantapur
2.	Nizamabad	Bankura	Banka	Chittoor
3.	Karimnagar	Birbhum	Begusarai	Cuddapah
4.	Warangal	Dakshin Dinajpur	Bhagalpur	Kurnool
5.	Medak	Uttar Dinajpur	Buxar	Srikakulam
6.	Mahbubnagar	Jalpaiguri	Gopalganj	Vishakhapatnam
7.	Rangareddy	Malda	Khagaria	Vizianagaram
8.	Nalgoda	East Medinipur	Kishanganj	
9.	Khammam	West Medinipur	Madhepura	
10.		Murshidabad	Munger	
11.		Purulia	West Champaran	
12.			East Champaran	
13.			Saharsa	
14.			Saran	
15.			Sheikhpura	
16.			Sitamarhi	
17.			Siwan.	

***Note** – The above list has been given so that the students are aware that backward areas have been notified in each of the four States for the purpose availing deduction under section 32AD and higher additional depreciation under section 32(1)(iia). Students are not expected to rote learn or memorize the names of the backward areas in each State.*

6. Scope of qualifications for e-Return Intermediary extended to include Company Secretaries, Cost Accountants and Tax Return Preparer [Notification No 66/2016, dated 09-08-2016]

Section 139(1B) provides for an alternative method to furnish return of income. Vide Notification No 210/2007, dated 27.07.2007, an Electronic Furnishing of Return of Income Scheme, 2007 was notified for the said purpose. The scheme, *inter alia* provides that an eligible person may, at his option, furnish his return of income which he is required to furnish under various provisions of the Act, to an e-Return Intermediary who shall digitize the data of such return and transmit the same electronically to a server designated for this purpose by the e-Return Administrator, on or before the due date.

Para 5 of the said Notification lays down the qualifications of an e-Return Intermediary. A firm of Chartered Accountants or Advocates, which has been allotted a Permanent Account Number, as well as a Chartered Accountant or an Advocate who has been allotted a Permanent Account Number, *inter alia,* qualified to be an e-Return intermediary.

Vide this Notification, a firm of Company Secretaries or Cost Accountants, if the firm has been allotted PAN as well as a Company Secretary or a Cost Accountant or Tax Return Preparer, who has been allotted a Permanent Account Number, would also qualify to be an e-Return intermediary.

7. Rescinding of initially notified Income Computation Disclosure Standards (ICDSs) *[Notification No S.O. 3078(E) dated 29.9.2016]* and Notification of new ICDSs to be applicable from A.Y.2017-18 *[Notification No. S.O. 3079(E) dated 29-09-2016]*

Section 145 of the Income-tax Act, 1961 provides for the method of accounting. Section 145(1) requires income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" to be computed in accordance with either the cash or mercantile system of accounting regularly employed by the assessee, subject to the provisions of section 145(2). Under section 145(2), the Central Government is empowered to notify in the Official Gazette from time to time, **income computation and disclosure standards (ICDSs)** to be followed by any class of assessees or in respect of any class of income.

Accordingly, the Central Government had, vide Notification No.S.O.892(E) dated 31.3.2015, in exercise of the powers conferred by section 145(2), notified ten income computation and disclosure standards (ICDSs) to be followed by all assessees, following the mercantile system of accounting, for the purposes of computation of income chargeable to income-tax under the head "Profit and gains of business or profession" or

"Income from other sources". This notification was to come into force with effect from 1st April, 2015, to be applicable from A.Y. 2016-17.

However, the Central Government has, *vide* Notification No.S.O.3078(E) dated 29.9.2016, rescinded Notification No.S.O.892(E) dated 31.3.2015. Simultaneously, *vide* Notification No.S.O.3079(E) dated 29.9.2016, the Central Government has notified ten new ICDSs to be applicable from A.Y.2017-18.

The newly notified ICDSs have to be followed by all assessees (other than an individual or a Hindu undivided family who is not required to get his accounts of the previous year audited in accordance with the provisions of section 44AB) following the mercantile system of accounting, for the purposes of computation of income chargeable to income-tax under the head "Profits and gains of business or profession" or "Income from other sources", from A.Y.2017-18.

Note – Students are advised to refer to the Annexure to the October 2016 Edition of the Practice Manual of IIPCC Paper 4: Taxation Part I: Income-tax which explains the significant changes in the ICDSs notified on 29.9.2016 vis-à-vis ICDSs initially notified on 31.3.2015 (since rescinded). The Annexure also contains the text of the new ICDSs notified on 29.9.2016.

8. Expenditure for obtaining right to use spectrum for telecommunication services [New Rule 6A] [Notification No. 89/2016, dated 04-10-2016]

The Finance Act, 2016 has inserted new section 35ABA to provide for tax treatment of spectrum fee. Section 35ABA provides that where any capital expenditure has been incurred for acquisition of any right to use spectrum for telecommunication services either before the commencement of the business or thereafter, at any time during the previous year and for which payment has actually been made to obtain a right to use spectrum, appropriate fraction of the amount of such expenditure (1/total number of relevant previous years) would be allowed as deduction for the relevant previous years during which the spectrum, for which the fee is paid, shall be in force.

As per clause (iii) of *Explanation* to section 35ABA, the phrase "payment has actually been made" means the actual payment of expenditure irrespective of the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee or payable in such manner as may be prescribed.

Accordingly, the CBDT has, vide this Notification, inserted new Rule 6A which substantiates the meaning of the phrase 'payment has actually been made' :

(a) **In a case where upfront payment of spectrum fee has been made:** Where an assessee has opted and been allowed by the Department of Telecommunications, Government of India to make full upfront payment of spectrum fee, the actual payment of expenditure irrespective of the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee;

(b) **<u>In a case where deferred payment is made</u>:** Where an assessee has opted and been allowed by the Department of Telecommunications, Government of India to make deferred payment, the amount which would have been payable by the assessee had he opted for full upfront payment of spectrum fee irrespective of the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee.

However, in case of deferred payment referred to in (b) above, where there is failure by the assessee to comply with any of the conditions specified by the scheme of the Department of Telecommunications, Government of India and Department of Telecommunications terminates the allotment or assignment of spectrum, the Assessing Officer shall, in exercise of power vested in him under section 35ABA(3), re-compute the total income of the assessee for the previous year in which the deduction has been claimed and granted to him by deeming that,-

(i) the total amount of spectrum fee paid up to the date of termination is the amount of "payment actually been made";

(ii) the spectrum was in force up to the date of its termination for the purpose of computing "relevant previous year".

II. CIRCULARS

1. Eligibility for grant of additional depreciation under section 32(1)(iia) in the case of an assessee engaged in printing or printing and publishing [Circular No. 15/2016, dated 19-05-2016]

An assessee, engaged in the business of manufacture or production of an article or thing, is eligible to claim additional depreciation under section 32(1)(iia) in addition to the normal depreciation under section 32(1).

The CBDT has, vide this Circular, clarified that the business of printing or printing and publishing amounts to manufacture or production of an article or thing and is, therefore, eligible for additional depreciation under section 32(1)(iia).

2. Admissibility of claim of deduction of bad debts under section 36(1)(vii) read with section 36(2) [Circular No. 12/2016, dated 30-05-2016]

The CBDT has clarified, vide this Circular, that claim for any debt or part thereof in any previous year, shall be admissible under section 36(1)(vii), if it is written off as irrecoverable in the books of accounts of the assessee for that previous year and it fulfills the conditions stipulated in section 36(2). There is no requirement in law that the assessee has to establish that the debt has, in fact, become irrecoverable.

3. Clarification regarding attaining prescribed age of 60 years/80 years on 31st March itself, in case of senior/very senior citizens whose date of birth falls on 1st April [Circular No. 28/2016, dated 27-07-2016]

An individual who is resident in India and of the age of 60 years or more (senior citizen) and 80 years or more (very senior citizen) is eligible for a higher basic exemption limit of ₹3,00,000 and ₹5,00,000, respectively.

The CBDT has, vide this Circular, clarified that a person born on 1st April would be considered to have attained a particular age on 31st March, the day preceding the anniversary of his birthday. In particular, the question of attainment of age of eligibility for being considered a senior/very senior citizen would be decided on the basis of above criteria.

Therefore, a resident individual whose 60^{th} birthday falls on 1^{st} April, 2017, would be treated as having attained the age of 60 years in the P.Y.2016-17, and would be eligible for higher basic exemption limit of ₹ 3 lakh in computing his tax liability for A.Y.2017-18. Likewise, a resident individual whose 80^{th} birthday falls on 1^{st} April, 2017, would be treated as having attained the age of 80 years in the P.Y.2016-17, and would be eligible for higher basic exemption limit of ₹ 5 lakh in computing his tax liability for A.Y.2017-18.

4. Clarification on applicability of TDS provisions of section 194-I on lumpsum lease premium paid for acquisition of long term lease [Circular No.35/2016, dated 13-10-2016]

Under section 194-I, tax is required to be deducted at source at the prescribed rates from payment of any income by way of rent. For the purposes of this section, "rent" has been defined as any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of any land or building or machinery or plant or equipment or furniture or fittings.

The issue of whether or not TDS under section 194-I is applicable on 'lump sum lease premium' or 'one-time upfront lease charges" paid by an assessee for acquiring long-term leasehold rights for land or any other property has been examined by the CBDT.

Accordingly, the CBDT has, vide this Circular, clarified that lump sum lease premium or one-time upfront lease charges, which are not adjustable against periodic rent, paid or payable for acquisition of long-term leasehold rights over land or any other property are not payments in the nature of rent within the meaning of section 194-I. Therefore, such payments are not liable for TDS under section 194-I.

5. Clarification on taxability of the compensation received by the land owners for the land acquired under the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013 (RFCTLARR Act) [Circular No. 36/2016, dated 25-10-2016]

Under the existing provisions of the Income-tax Act, 1961, an agricultural land which is not situated in specified urban area, is not regarded as a capital asset. Hence, capital gains arising from the transfer (including compulsory acquisition) of such agricultural land is not taxable. The Finance (No.2) Act, 2004 has inserted section 10(37) from 1-4-2005 to provide specific exemption to the capital gains arising to an Individual or a HUF from compulsory acquisition of an agricultural land situated in specified urban limit, subject to fulfilment of certain conditions. Therefore, compensation received from compulsory acquisition of an agricultural land is not taxable under the Act (subject to fulfilment of certain conditions for specified urban land).

The RFCTLARR Act which came into effect from 1st January, 2014, in section 96, *inter alia* provides that income-tax shall not be levied on any award or agreement made (except those made under section 46) under the RFCTLARR Act. Therefore, compensation received for compulsory acquisition of land under the RFCTLARR Act (except those made under section 46 of RFCTLARR Act), is exempted from the levy of income-tax.

As no distinction has been made between compensation received for compulsory acquisition of agricultural land and non-agricultural land in the matter of providing exemption from income-tax under the RFCTLARR Act, the exemption provided under section 96 of the RFCTLARR Act is wider in scope than the tax-exemption provided under the existing provisions of Income-tax Act, 1961. This has created uncertainty in the matter of taxability of compensation received on compulsory acquisition of land, especially those relating to acquisition of non-agricultural land.

The matter has been examined by the CBDT and it has been clarified that compensation received in respect of award or agreement which has been exempted from levy of income-tax vide section 96 of the RFCTLARR Act shall also not be taxable under the provisions of Income-tax Act, 1961 even if there is no specific provision for exemption of such compensation in the Income-tax Act, 1961.

III. Amendments made by the Taxation Laws (Amendment) Act, 2016

(1) Splitting up or reconstruction of an erstwhile public sector company into separate companies as a result of transfer of its shares by the Central Government deemed to be a demerger [Section 2(19AA)]

Effective from: A.Y.2017-18

(i) The existing provisions of the Income-tax Act, 1961 provide for tax neutrality in matters relating to transfer of capital asset, carry forward of loss, claim of certain deductions, etc., in case of demerger of entities.

(ii) Upto A.Y.2016-17, the definition of the term "demerger" as per section 2(19AA) of the Income-tax Act, 1961, did not include within its scope, the splitting up or the reconstruction of a company, which ceased to be a public sector company as a result of transfer of its shares by the Government, into separate companies, even if such splitting up or reconstruction has been made to give effect to the conditions attached to the said transfer of shares by the Government.

(iii) With a view to facilitate the splitting up or the reconstruction of erstwhile public sector companies and to give effect to the conditions attached to the transfer of shares by the Government, *Explanation 5* has been inserted in section 2(19AA) with effect from A.Y.2017-18 to provide that the reconstruction or splitting up of a company, which ceased to be a public sector company as a result of transfer of its shares by the Central Government, into separate companies, shall be deemed to be a demerger, if such reconstruction or splitting up has been made to give effect to any condition attached to the said transfer of shares and also fulfils such other conditions as may be notified by the Central Government in the Official Gazette.

(iv) Consequently, as per section 47, transfer of a capital asset in the scheme of demerger would not be regarded as a transfer, and hence capital gains tax liability would not be attracted. Further, the accumulated loss and unabsorbed depreciation of the demerged public sector company can be carried forward for set-off in the hands of the resulting company as per the provisions of section 72A(4). Also, the profit-linked tax deductions under section 80-IA to 80-IE, which was available to the erstwhile demerged public sector company, would be available to the resulting company for the unexpired period. An Indian company incurring expenditure wholly and exclusively for the purposes of demerger of the undertaking would be entitled to deduction under section 35DD of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the year of demerger.

(2) Relaxation of minimum period of employment of an employee for the purpose of deduction under section 80JJAA, in case of assessees engaged in apparel business [Section 80JJAA]

Effective from: A.Y.2017-18

(i) Upto A.Y.2016-17, deduction under section 80JJAA in respect of employment of new workmen was available to assessees deriving profits and gains from manufacture of goods in a factory. In order to extend this employment generation incentive to all sectors, section 80JJAA has been substituted by the Finance Act, 2016 with effect from A.Y.2017-18.

(ii) Under new section 80JJAA, deduction is available in respect of employment of new employees, where the gross total income of an assessee **to whom section 44AB applies**, includes any profits and gains derived from business.

(iii) In case of such assessees, deduction of an amount equal to 30% of additional employee cost incurred in the course of such business in the previous year, would be allowed for three assessment years including the assessment year relevant to the previous year in which such employment is provided, subject to the fulfillment of certain specified conditions. One of the conditions is that the employee should be employed for a period of not less than 240 during the previous year.

(iv) Considering the seasonal nature of the business of manufacturing of apparel, the minimum period of employment of an employee who is employed in this business has been reduced from 240 days to 150 days during the previous year. Therefore, in the case of an assessee engaged in the business of manufacturing of apparel, deduction under section 80JJAA would be allowable in respect of additional employee cost incurred in respect of employees employed for a period of atleast 150 days during the previous year.

PART II : INDIRECT TAXES

Indirect tax laws as amended by the Finance Act, 2016 including significant notifications/circulars issued up to 31st October, 2016 are applicable for May, 2017 examinations. The Study Material [Edition : September, 2015; Reprint Edition: October, 2016] contains all the relevant amendments made by the Finance Act, 2015 and significant notifications/circulars issued up to 30.04.2015. The Supplementary Study Paper, 2016 contains the amendments made by the Finance Act, 2016 and significant notifications/circulars issued from 01.05.2015 to 30.04.2016. In case of service tax and CENVAT credit, notifications/circulars issued till 01.06.2016 have been included in the Supplementary Study Paper, 2016. The remaining notifications/circulars i.e., the ones issued from 02.06.2016 to 31.10.2016 for service tax and CENVAT credit and from 01.05.2016 to 31.10.2016 for others are given below.

The amendments are given chapter-wise to facilitate co-relation with the Study Material. The chapter reference given in the Supplementary Study Paper, 2016 corresponds to the parallel chapter number of the Study Material.

Chapter 1 : Basic Concepts of Indirect Taxes

Unit-2: Central Excise Duty

1. Threshold exemption (SSI exemption) raised from ₹ 6 crore to ₹ 10 crore for jewellery manufacturers with simultaneous increase in eligibility limit from ₹ 12 crore to ₹ 15 crore

SSI exemption for articles of jewellery or parts of articles of jewellery or both [excluding silver jewellery not studded with diamonds/other precious stones] has been enhanced from ₹ 6 crore to ₹ 10 crore with simultaneous increase in the eligibility limit from ₹ 12 crore to ₹ 15 crore in the preceding year.

Notification No. 8/2003 CE dated 01.03.2003 has been amended vide ***Notification No. 28/2016 CE dated 26.07.2016*** to carry out the above amendment.

[Effective from 26.07.2016]

2. ***Notification No. 8/2016 CE (NT) dated 01.03.2016*** has extended the facility for revision of returns to central excise returns. The amendment was to become effective from a date to be notified *[Refer Unit 2 : Central Excise Duty of Chapter 1 : Basic Concepts of Indirect Taxes of Supplementary Study Paper-2016]*. ***Notification No. 42/2016 CE (NT) dated 11.08.2016*** has now notified 17.08.2016 as the date when the said amendment would become effective.

Chapter 5 : Exemptions and Abatements

1. **Services provided by a senior advocate to a business entity with a turnover up to ₹ 10 lakh in the preceding financial year exempted**

With effect from 01.04.2016, *Notification No. 25/2012 ST dated 20.06.2012* had been amended to *inter alia* withdraw the exemptions available in respect of the legal services provided by a senior advocate to-:

(i) an advocate or partnership firm of advocates providing legal services

(ii) a business entity with a turnover up to ₹ 10 lakh in the preceding financial year

However, services provided by a "senior advocate by way of legal services to a person other than a person ordinarily carrying out any activity relating to industry, commerce or any other business or profession" continued to remain exempted [Refer Chapter 5: Exemptions and Abatements in the Supplementary Study Paper-2016].

With effect from 06.06.2016, ***Notification No. 32/2016 ST dated 06.06.2016*** has amended *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012* to exempt services provided by a senior advocate by way of legal services to a business entity with a turnover up to ₹ 10 lakh in the preceding financial year. Further, the exemption available to services provided by senior advocates to person other than persons ordinarily carrying out any activity relating to industry, commerce or any other business or profession has been reworded. As per the reworded exemption, *"services provided by a senior advocate by way of legal services to any person other than a business entity"* has been exempted.

Therefore, with effect from 06.06.2016, the taxability of legal services provided by a senior advocate and other advocates is explained as under:

Service	Senior Advocate	Other advocates / Partnership firm of advocates
Legal service provided to an advocate or partnership firm of advocates providing legal	Not exempt	Exempt

services with turnover exceeding ₹ 10 lakh in the preceding financial year		
Legal service provided to an advocate or partnership firm of advocates providing legal services with turnover upto ₹ 10 lakh in the preceding financial year	Exempt	Exempt
Legal service provided to a business entity with a turnover up to ₹ 10 lakh in the preceding financial year	Exempt	Exempt
Legal service provided to any person other than a business entity	Exempt	Exempt

[Effective from 06.06.2016]

2. Services billed and provided prior to 01st June, 2016 exempted from Krishi Kalyan Cess (KKC)

Taxable services the invoice for which have been issued on or before the 31st May, 2016 have been exempted from the whole of **Krishi Kalyan Cess** vide ***Notification No. 35/2016 ST dated 23.06.2016*** if the provision of service has been completed on or before the 31st May, 2016.

[Effective from 23.06.2016]

3. Services of transportation of goods by a vessel from outside India upto customs station in India which have been billed prior to 01st June, 2016 exempted from service tax on fulfilment of specified conditions

Taxable services by way of transportation of goods by a vessel from outside India upto the customs station in India for which the invoice has been issued on or before 31.05.2016 have been exempted from service tax on fulfilment of the following conditions:

(i) the import manifest or import report required to be delivered under section 30 of the Customs Act, 1962 has been delivered on or before 31.05.2016; and

(ii) the service provider or recipient produces customs certified copy of such import manifest or import report ***[Notification No. 36/2016 ST dated 23.06.2016].***

[Effective from 23.06.2016]

4. 90% abatement granted to transport of passengers by air embarking from or terminating in Regional Connectivity Scheme (RCS) Airport for a period of 1 year

Notification No. 38/2016 ST dated 30.08.2016 has amended *Notification No. 26/2012 ST dated 20.06.2012* to grant abatement of 90% on service of transport of passengers, with or without accompanied belongings, by air, embarking from or terminating in a RCS Airport. The abatement would be available if the CENVAT credit on inputs, capital goods and input services, used for providing the said taxable service has not been taken by the service provider under the provisions of the CENVAT Credit Rules, 2004.

Further, the abatement will be valid only for a period of **1 year** from the date of commencement of operations of the RCS Airport as notified by the Ministry of Civil Aviation.

[Effective from 30.08.2016]

5. **One time upfront amount payable on long term leases of industrial plots granted by State Government Industrial Development Corporations/ Undertakings to industrial units exempted from service tax**

   Taxable services provided by State Government Industrial Development Corporations/ Undertakings to industrial units by way of granting long term (30 years, or more) lease of industrial plots have been exempted from so much of service tax leviable thereon as is leviable on the one time upfront amount (called as premium, salami, cost, price, development charges or by any other name) payable for such lease ***[Notification No. 41/2016 ST dated 22.09.2016]***. However, subsequent payments, if any, will not enjoy such an exemption and will be liable to service tax.

   [Effective from 22.09.2016]

6. **No service tax on services by way of advancement of yoga provided by entities registered under section 12AA of the Income-tax Act, 1961 from 01.07.2012 to 20.10.2015**

   With effect from 21.10.2015, services relating to advancement of yoga provided by charitable entities registered under section 12AA of the Income-tax Act, 1961 have been exempted from service tax vide *Notification No. 20/2015 ST dated 21.10.2015 [Refer Chapter 5: Exemptions and Abatements in the Supplementary Study Paper-2016].*

   According to the practice generally prevalent during the period from 01.07.2012 to 20.10.2015 there was non-levy of service tax on such services. Thus, service tax was not being paid on such services on account of the said practice even though such services were liable to service tax.

   Now the Central Government, in exercise of the power conferred by section 11C of the Central Excise Act, 1944 read with section 83 of the Finance Act, 1994, has directed that no service tax will be required to be paid on the services provided by way of advancement of yoga by entities registered under section 12AA of Income-tax Act, 1961 for the period from 01.07.2012 to 20.10.2015 ***[Notification No. 42/2016 ST dated 26.09.2016].***

   [Effective from 01.07.2012 till 20.10.2015]

<u>Chapter 6 : Service Tax Procedures</u>

1. **(i) In case of legal services provided by senior advocates, service tax to be paid by the recipient of service under reverse charge (ii) In case of representational service provided by senior advocates if the senior advocate is engaged by another lawyer, service tax to be paid by the litigant**

With effect from 01.04.2016, service tax had been made payable under forward charge in case of legal services provided by senior advocates. For this purpose, necessary amendments were made in rule 2(1)(d)(i)(D) of Service Tax Rules, 1994.

However, rule 2(1)(d)(i)(D) has now been amended again vide ***Notification No. 33/2016 ST dated 06.06.2016*** to provide, inter alia, that in relation to service provided by an individual advocate or a firm of advocates by way of legal services other than representational services by senior advocates to any business entity located in the taxable territory, the person liable to pay service tax is the recipient of such service.

Further, another item (DD) has been inserted after item (D) in rule 2(1)(d)(i) to provide that "in relation to service provided or agreed to be provided by a senior advocate by way of representational services before any court, tribunal or authority, directly or indirectly, to any business entity located in the taxable territory, including where contract for provision of such service has been entered through another advocate or a firm of advocates, and the senior advocate is providing such services, the person liable to pay service tax is the recipient of such services, which is the business entity who is litigant, applicant, or petitioner, as the case may be".

To summarise,

(i) where legal services are provided by senior advocates to business entities, service tax will be payable by the recipient of service.

(ii) where representational services are provided by the senior advocates to any business entity, service tax will be payable by the recipient of service which is the business entity who is litigant, applicant, or petitioner.

(iii) where the contract for representational services provided by the senior advocates to any business entity has been entered through another advocate or a firm of advocates, service tax will be payable by the recipient of service which is the business entity who is litigant, applicant, or petitioner.

Further, reverse charge *Notification No. 30/2012 ST dated 20.06.2012* has been amended vide ***Notification No. 34/2016 ST dated 06.06.2016*** to provide that 100% of such service tax will be payable by the recipient of service i.e., there will be full reverse charge on services provided by senior advocates. It has been clarified by inserting an explanation in the notification that the business entity located in the taxable territory who is litigant, applicant or petitioner, as the case may be, shall be treated as the person who receives the legal services for the purpose of this notification.

[Effective from 06.06.2016]

2. Form ST 3 amended to include KKC etc.

Service tax return form ST 3 has been amended vide ***Notification No. 43/2016 ST dated 28.09.2016*** to incorporate columns and entries relating to KKC, disclosure of reversal of CENVAT credit under rule 6 of CENVAT Credit Rules, 2004 etc.

[Effective from 28.09.2016]

Chapter 7: CENVAT Credit

1. Following amendments have been made in the CENVAT Credit Rules, 2004:

(a) Definition of manufacturer or producer amended [Rule 2(naa)]

The definition of manufacturer or producer under clause (naa) of rule 2 has been amended vide ***Notification No. 36/2016 CE (NT) dated 26.07.2016***. As per the amended definition, *"manufacturer or producer*

(i) in relation to articles of jewellery or parts of articles of jewellery or both, falling under heading 7113 of the First Schedule to the Excise Tariff Act, includes a person who is liable to pay duty of excise leviable on such goods under sub-rule (1) of rule 9 of the Articles of Jewellery (Collection of Duty) Rules, 2016;

(ia) in relation to articles of precious metals falling under heading 7114 of the First Schedule to the Excise Tariff Act, includes a person who is liable to pay duty of excise leviable on such goods under sub-rule (1) of rule 12AA of the Central Excise Rules, 2002;

(ii) in relation to goods falling under Chapters 61, 62 or 63 of the First Schedule to the Excise Tariff Act, includes a person who is liable to pay duty of excise leviable on such goods under sub-rule (1A) of rule 4 of the Central Excise Rules, 2002."

[Effective from 26.07.2016]

(b) Jewellery manufacturer with turnover upto ₹ 15 crore in preceding year eligible to avail 100% CENVAT credit on capital goods in the year of purchase [Rule 4(2)(a)]

As per explanation to rule 4(2)(a) read with third proviso to the said rule, an assessee whose aggregate value of clearances of all excisable goods for home consumption in the preceding financial year does not exceed ₹ 4 crores (computed in accordance with SSI notification), can take 100% CENVAT credit on capital goods in the financial year when the same are received by him.

With effect from 01.03.2016, explanation to rule 4(2)(a) has been amended to provide that a manufacturer of articles of jewellery [excluding silver jewellery, other than studded with diamonds/ ruby/ emerald/ sapphire] will be allowed to take 100% CENVAT credit on capital goods in the year of purchase, if his aggregate value of clearances of all excisable goods for home consumption in the preceding financial year, did not exceed ₹ 12 crore *[Refer Chapter 7 : CENVAT Credit in the Supplementary Study Paper – 2016].*

However, with effect from 26.07.2016, the said explanation has been amended again vide ***Notification No. 36/2016 CE (NT) dated 26.07.2016*** to provide that a manufacturer of articles of jewellery or parts of articles of jewellery or both, falling under heading 7113 of the First Schedule of the Central Excise Tariff Act, will be allowed to take 100% CENVAT credit on capital goods in the year of purchase, if his aggregate value of clearances of all excisable goods for home consumption in the preceding financial year, did not exceed ₹ 15 crore.

[Effective from 26.07.2016]

(c) Requirement of enclosing photocopies of the railway receipts with STTG for availing CENVAT credit dispensed with [Rule 9(1)(fa)]

Notification No. 45/2016 CE (NT) dated 20.09.2016 has amended rule 9(1)(fa) to do away with the requirement of enclosing photocopies of the railway receipts with Service Tax Certificate for Transportation of Goods by Rail (STTG), as a document for availing CENVAT credit. As per the amended rule 9(1)(fa), Service Tax Certificate for Transportation of Goods by Rail issued by the Indian Railways will be an eligible document for availing CENVAT credit.

[Effective from 20.09.2016]

(d) Ethanol produced from molasses generated from cane crushed in the sugar season 2015-16 removed from the list of excisable goods which are excluded from the purview of reversal provisions under rule 6 [Rule 6(6)]

The Central Government had exempted excise duty payable on ethanol produced from molasses generated from cane crushed in the sugar season 2015-16 i.e. 1st October, 2015 onwards, for supply to the public sector oil marketing companies, namely, Indian Oil Corporation Ltd., Hindustan Petroleum Corporation Ltd. or Bharat Petroleum Corporation Ltd., for the purposes of blending with petrol.

Further, such removals of ethanol had also been excluded from the purview of reversal provisions under rule 6. For this purpose, *Notification No. 21/2015 CE (NT) dated 07.10.2015* had inserted clause (ix) in sub-rule (6) of rule 6 to provide that the provisions of sub-rules (1), (2), (3) and (4) of rule 6 would not apply to ethanol produced from molasses generated from cane crushed in the sugar season 2015-16 i.e. 1st October, 2015 onwards, for supply to the public sector oil marketing companies, namely, Indian Oil Corporation Ltd., Hindustan Petroleum Corporation Ltd. or Bharat Petroleum Corporation Ltd., for the purposes of blending with petrol. This amendment became effective from 01.10.2015 *[Refer Chapter 7: CENVAT Credit in the Supplementary Study Paper – 2016]*.

Now since the exemption to ethanol has been withdrawn from 10.08.2016, clause (ix) of sub-rule (6) of rule 6 has been omitted vide ***Notification No. 41/2016 CE (NT) dated 10.08.2016.***

[Effective from 10.08.2016]

PART – II: QUESTIONS AND ANSWERS

QUESTIONS

Residential Status and Scope of total income

1. Mr. Suhaan furnished the following particulars of his income for the year ended 31.3.2017.

	Particulars	₹
(a)	Income earned from business in France which is controlled from Mumbai (₹ 65,000 is received in India)	90,000
(b)	Pension for services rendered in India but received in France	14,000
(c)	Dividend received in France from Titanium Inc., a French company	25,000
(d)	Rent from property in France deposited in a bank in France and later on, remitted to India through approved banking channels	85,000
(e)	Dividend from Sunset Ltd., an Indian company received in France	98,000

Compute his gross total income for the assessment year 2017-18, if he is:

(i) Resident and ordinarily resident;

(ii) Resident but not ordinarily resident;

(iii) Non-resident

Income which do not form part of total income

2. State with brief reasons whether the following statements are true or false with reference to the provisions of the Income-tax Act, 1961:

   (a) Payment of ₹ 12 lakh from an approved superannuation fund made by T Ltd. by way of transfer to the account of Mr. Swayam, an employee of T Ltd., under Atal Pension Yojana is taxable in the hands of Mr. Swayam.

   (b) Mr. Arpit, a member of a HUF, received ₹ 12,000 as his share from the income of the HUF. The same is to be included in his chargeable income.

   (c) During the previous year 2016-17, Ms. Arpita received in aggregate ₹ 12 lakhs as dividend from Indian companies. The same is exempt in her hands under section 10(34).

   (d) Exemption is available to a Sikkimese individual, only in respect of income from any source in the State of Sikkim.

Income from Salaries

3. Mrs. Shakshi is a Human Resources Manager of M/s. Trumph & Co. Pvt. Ltd., based at Mumbai. She is 61 years of age and receives the following salary and perquisites from the company during the year ending 31.03.2017:

(i) Basic Salary ₹ 80,000 per month

(ii) Dearness Allowance ₹ 22,000 per month (forms part of pay for retirement benefits)

(iii) Bonus – 2 months basic pay.

(iv) Commission – 0.1% of the turnover of the company. The turnover for the F.Y. 2016-17 was ₹ 12.00 crores.

(v) Contribution of the employer and employee to the recognized provident fund Account ₹ 2,00,000 each.

(vi) Interest credited to Recognized Provident Fund Account at 9.5% - ₹ 80,000.

(vii) Rent free unfurnished accommodation provided by the company for which the company pays a rent of ₹ 84,000 per annum.

(viii) Entertainment Allowance – ₹ 35,000.

(ix) Hostel allowance for three children – ₹ 3,200 each.

She makes the following payments and investments :

(i) Premium paid to insure the life of her major daughter – ₹ 18,000.

(ii) Medical Insurance premium for self – ₹ 12,000 ; Spouse – ₹ 14,000.

(iii) Donation to a public charitable institution registered under 80G ₹ 1,50,000 by way of cheque.

(iv) LIC Pension Fund – ₹ 60,000.

Determine the tax liability of Mrs. Sakshi for the Assessment Year 2017-18.

Income from house property

4. In May, 2016, Mr. Aakarsh recovered rent of ₹ 17,000 from Ms. Gunjan, to whom he had let out his house from June 2010 to August 2012. He could not realise two months rent of ₹ 24,000 from her and to that extent his actual rent was reduced while computing income from house property for A.Y.2013-14.

From September 2012 to November 2015, he had let out his property to Mr. Sahil. In October, 2014, he had increased the rent from ₹ 13,000 to ₹ 15,000 per month and the same was a subject matter of dispute. The house remained vacant for three months from December 2015 to February 2016. In April, 2016 the matter was finally settled and Mr. Aakarsh received ₹ 28,000 as arrears of rent for the period October 2014 to November, 2015. However, in March 2016, Mr. Aakarsh had already sold this residential house property to Mr. Sagar.

Mr. Aakarsh, contends that the amount recovered as unrealised rent and arrears of rent in the P.Y.2016-17 would not be taxable in his hands in that year, since he had sold such house property in the previous year 2015-16 itself. Is the contention of Mr. Aakarsh correct? If not, under what head would such income be taxable and compute the income taxable under that head for A.Y.2017-18?

Profits and gains of business or profession

5. State, with reasons, the allowability of the following expenses under the Income-tax Act, 1961, as deduction, while computing income from business or profession for the Assessment Year 2017-18:

   (i) XYZ Credit Corporation, a non-banking finance company, made provision for bad and doubtful debts in the books of account for the year ended 31.3.2017.

   (ii) On 14.5.2017, ABC Ltd. paid ₹ 45,000 to the Indian Railways for the use of railway assets pertaining to previous year 2016-17.

   (iii) MNO Ltd. paid ₹ 55,000 as tax on non-monetary perquisite provided to an employee.

   (iv) ₹ 32,000 paid by S Ltd. in cash on 28.3.2017 to a transporter (owning 8 goods carriages throughout the previous year) for carriage of goods, without deduction of tax at source.

   (v) P Ltd. paid ₹ 80,000 in cash for purchase of wheat from a farmer on a banking day.

Capital Gains

6. Mr. Mayank, aged 55 years owned a residential house in Noida. It was acquired by Mr. Mayank on 17-12-1986 for ₹ 8,00,000. He sold it for ₹ 68,00,000 on 14-12-2016. The stamp valuation authority of the State fixed value of the property at ₹ 85,00,000. The assessee paid 2% of the sale consideration as brokerage on sale of the said property.

   Mr. Mayank acquired a residential house property at Kota on 3.3.2017 for ₹ 7,00,000 and deposited ₹ 3,50,000 on 14-5-2017 and ₹ 5,50,000 on 25-7-2017 in the capital gains bonds of the National Highway Authority of India. He deposited ₹ 4,50,000 on 16-7-2017 and ₹8,70,000 on 11-11-2017 in the capital gain deposit scheme in a Nationalized Bank for construction of an additional floor on the residential house property in Kota.

   Compute the Capital Gain chargeable to tax for the Assessment Year 2017-18 and income-tax chargeable thereon assuming Mr. Mayank has no other income.

   Cost Inflation Index for Financial Year 1986-87: 140 and Financial Year 2016-17: 1125

Income from other sources

7. During the previous year 2016-17, Mr. Gagan received ₹ 5,32,000 towards interest on enhanced compensation from State Government in respect of compulsory acquisition of his land effected during the financial year 2011-12.

   The above amount of interest include interest relating to the following financial years:

   F.Y. 2013-14: ₹ 1,58,000

   F.Y. 2014-15 ₹ 1,78,000

F.Y. 2015-16 ₹ 1,96,000

He incurred ₹ 75,000 by way of legal expenses in the F.Y.2016-17 to receive the interest on such enhanced compensation.

Determine how much of interest on enhanced compensation would be chargeable to tax for the assessment year 2017-18? Can he claim deduction in respect of legal expenses from the amount of interest on enhanced compensation chargeable to tax?

Income of Other Persons included in assessee's Total Income

8. Compute the gross total income of Mr. Abhinav & and his wife Mrs. Suhaani from the following information:

	Particulars	₹
(a)	Salary income (computed) of Mrs. Suhaani	3,25,000
(b)	Income from business of Mr. Abhinav	4,15,000
(c)	Income of minor son Chetan from fixed deposit	25,000
(d)	Income of minor daughter Shreya from music concerts given by her	28,000
(e)	Interest from bank received by Shreya on deposit made out of income derived from music concerts	7,000
(f)	Gift received by Shreya on 4.10.2016 from friend of Mrs. Suhaani	5,500

Set off and Carry Forward of Losses

9. Compute the total income of Mr. Tarun, a resident Indian, aged 57 years, from the following details for the year ended 31.3.2017. Also, show the items eligible for carry forward to the A.Y. 2018-19:

Particulars	₹
Income from salaries	2,55,000
Loss from house property	2,19,000
Loss from toys business of A.Y. 2016-17	2,45,000
Income from speculation business	28,000
Loss from specified business covered by section 35AD	46,000
Long-term capital gains from sale of urban land	2,75,500
Long-term capital loss from sale of listed shares in recognized stock exchange (STT paid)	1,32,000
Loss from card games	23,000

Income from betting (Gross)	49,000
Deposit in PPF	1,00,000

Deductions from Gross Total Income

10. State with proper reasons whether the following statements are True/False with regard to the provisions of the Income-tax Act, 1961:

    (i) Mrs. Leena, widow of Mr. Sahitya (who was an employee of M/s. ABC Ltd.), received ₹ 9 lakhs on 11.12.2016, being amount standing to the credit of Mr. Sahitya in his NPS Account, in respect of which deduction has been allowed under section 80CCD to Mr. Sahitya in the earlier previous years. Such amount received by her as a nominee on closure of the account is deemed to be her income for A.Y.2017-18.

    (ii) Mr. Gopal, a businessman, whose total income (before allowing deduction under section 80GG) for A.Y.2017-18 is ₹ 3,80,000, paid house rent at ₹ 8,000 p.m. in respect of residential accommodation occupied by him at Chennai. He is eligible to claim flat deduction of ₹ 60,000 under section 80GG for A.Y.2017-18.

    (iii) Mr. Anay purchased a residential house property for self-occupation at a cost of ₹ 40 lakh on 1.7.2016, in respect of which he took a housing loan of ₹ 32 lakh from Oriental Bank of Commerce@11% p.a. on the same date. He does not own any other house property. He is eligible to claim deduction of ₹ 2 lakh under section 24(b) out of the total interest paid or payable by him during the previous year 2016-17. He is not eligible for deduction of interest paid by him under any other provision of the Income-tax Act, 1961.

Computation of Total Income of an individual

11. From the following information, you are required to compute the total income of Mr. Dinesh (aged 52 years) for the assessment year 2017-18, based on provisions contained under section 44AE of the Income-tax Act, 1961.

    Mr. Dinesh is solely engaged in the business of plying goods vehicles since financial year 2010-11. He owned 5 heavy goods vehicles as on 01.04.2016. He acquired 3 more heavy goods vehicles on 1.7.2016.

    He did not opt for presumptive provision contained in section 44AE for the financial year 2015-16. His books were audited under section 44AB and the return of income was filed on 18.9.2016. He has unabsorbed depreciation of ₹ 95,000 and business loss of ₹ 1,28,000 for the financial year 2015-16.

    Following further information relating to P.Y.2016-17 is also provided to you:

    (i) He paid premium on life insurance policy of his married daughter ₹ 28,000. The policy was taken on 1.07.2016 and the minimum sum assured is ₹ 2,50,000.

(ii) He repaid principal of ₹ 88,000 and interest of ₹ 22,000 to Indian Bank towards education loan of his son, who completed MBA two years ago. He is employed after completion of his studies.

(iii) He deposited ₹ 55,000 in Tax Saver Deposit with Indian Bank in the name of married daughter.

(iv) He paid medical insurance premium of ₹ 31,500 for his mother, resident in India, aged 75 years by cheque.

Provisions concerning Advance Tax and Tax Deducted at source

12. State the applicability of TDS provisions and amount of tax, if any, to be deducted in the following cases:

    (a) Mr. Karthik received ₹ 2,50,000 as rent from Trip Ltd. for hire of machinery.

    (b) Dr. Sarthak performed a plastic surgery on Mr. Verma, Karta of Verma's Family. The Verma HUF paid ₹ 35,000 to Dr. Sarthak for such surgery.

    (c) Mr. Abhinav received ₹ 29,000 as director's sitting fees on 21-03-2017 from XYZ Ltd.

Provisions for filing of Return of Income

13. Mr. Vardaan earned income under the head "Salaries", "Income from House Property" and bank interest during the previous year 2016-17. He furnished his return of income on 30.11.2017 for A.Y 2017-18. Later, on 1.5.2018, he realized that he had not claimed deduction under section 80C in respect of the amount deposited by him in public provident fund (PPF). He now wants to revise his return of income. Can he do so? Explain with reference to the provisions of the Income-tax Act, 1961.

Computation of excise duty

14. Mr. Shivaay, a manufacturer, sold a machine for ₹ 4,00,000 (excluding tax and duties). Further, he furnished the following additional information with respect to said transaction:

Particulars	
Transit insurance shown separately	₹ 20,000
Packing charges	₹ 20,000
Extra charges for designing of the machine	₹ 50,000
Outward freight beyond the place of removal	₹ 30,000
Cash discount @ 2% on price of machinery was allowed as per terms of contract since full payment was received within 15 days of the dispatch of machinery	
VAT rate	2%
Excise duty rate	12.5%

Calculate the excise duty payable by Mr. Shivaay stating the reason for inclusion or exclusion for each of the items.

Computation of customs duty

15. Star Importers imports a carton of goods from China on 10.10.2016 containing 10,000 pieces valued at ₹ 2,00,000 (assessable value in terms of section 14 of the Customs Act, 1962). On the said product, customs duty @ 10% and excise duty @ 12.5% *ad valorem* is leviable.

    Similar products in India are assessable under section 4A of Central Excise Act 1944, after allowing an abatement of 30%. MRP printed on package at the time of import is ₹ 50 per piece. Special CVD under section 3(5) of the Customs Tariff Act, 1975 is also applicable on such goods. Determine the total customs duties payable on the imported goods.

Applicability of central sales tax

16. Briefly explain whether central sales tax will be applicable:-
    (i) when goods are sent by dealer outside the State to his other place of business.
    (ii) if at the time of stock transfer outside the State, dealer has an order for such sale in hand.

Computation of VAT liability

17. Mr. Maahi of Kolkata purchased goods from Mr. Vicky of Kolkata amounting to ₹ 8,55,000 including VAT @ 12.50% in the month of January, 2016. He incurred ₹ 1,00,000 as manufacturing & other expenses and added profit @ 25% on cost.

    Mr. Maahi sold 80% of the goods to Mr. Rajat of Kolkata and charged VAT @ 12.50% on 02.02.2016. Remaining 20% of the goods were transferred to his branch in Manipur on 05.02.2016.

    Compute the net VAT payable and input tax credit, if any, for the month of February, 2016 by assuming input output ratio to be 1:1.

Basic concepts of service tax

18. With reference to the provisions of service tax law, briefly examine the service tax implications in the following independent cases:-
    (a) Mr. A is working in a leading multinational company for two years. One of the clause of his employment contract provides that he would be given 3 months' notice by the said company in the event of termination of his services by such company. However, he has been terminated suddenly on account of his poor performance. He was paid termination compensation of ₹ 1,25,000.
    (b) Mr. B has entered into a contract with Zeal Technologies Ltd. for rendering legal consultancy services for one year on a lumpsum fee of ₹ 2,50,000 per month.

Point of taxation

19. With reference to the Point of Taxation Rules, 2011, determine the point of taxation in respect of following independent transactions:

    (a) A public limited company paid director's fees of ₹ 2,10,000 to one of its director for attending a Board Meeting held in the month of April. The meeting was held for taking important policy decisions for the company. Though the journal entry for the transaction was passed on the same day, actual payment was made to the director by the end of August of the next year.

    (b) XYZ Ltd. paid consultancy fees of ₹ 60,000 to its associated enterprises located in Dubai. Dubai firm raised the invoice on 27.01.2016 and the same was received by XYZ Ltd. on 06.02.2016. Though the journal entry was passed on 07.02.2016 in the books of XYZ Ltd., actual payment to Dubai firm was made on 25.02.2016.

Payment of service tax at special rates

20. Compute the service tax liability of Mr. P, an air travel agent, for the quarter ended September 30, 2016 using the following details:-

Particulars	₹
Basic air fare collected for domestic booking of tickets	40,00,000
Basic air fare collected for international booking of tickets	60,00,000
Commission received from the airlines on the sale of domestic and international tickets	5,00,000

In the above case, would the service tax liability of Mr. P be reduced if he opts for the special provision for payment of service tax as provided under rule 6 of the Service Tax Rules, 1994 instead of paying service tax at normal rates?

Notes:

1. Mr. P is not eligible for the small service providers' exemption under *Notification No. 33/2012 ST dated 20.06.2012*.
2. Service tax and cesses have been charged separately.

Computation of service tax liability

21. Compute the service tax including SBC and KKC payable on the services provided in each of the following independent cases:-

Services	₹
Sale of space for advertisement in a leading newspaper	2,15,000
Services related to preparation of advertisement	60,000
Sale of space for advertisements on internet websites	40,000

Sale of time for advertisement to be broadcast on TV Channel	1,50,000
Advertising in business directories	30,000
Advertising on film screen in theatres	1,00,000

Note: All the amounts stated above are exclusive of service tax and cesses. Ignore exemption available to small service providers.

Exemptions under service tax

22. Safe Alps Cable Car Co. runs a cable car to transport pilgrims uphill to a mountain top where a holy shrine is situated. Examine whether Safe Alps Cable Car Co. is required to pay any service tax.

23. With reference to the provisions of Finance Act, 1994 and relevant notifications issued thereunder, whether service tax is payable in the following independent cases:-

    (a) Gyan Mandal, an Educational Trust, runs a play school for providing pre-school education.

    (b) Shining Stars Public School provides educational services upto higher secondary school.

    (c) Aggarwal Classes, a coaching center, provides coaching for MBA entrance examinations to meritorious students of economically weak background.

Interest on delayed payment of service tax

24. Compute the interest payable on delayed payment of service tax by service provider where service tax has not been collected from service receivers in following cases:

Name of the service provider	ABC Ltd.	Gagan
Service tax liability	₹ 1,00,000	₹ 2,00,000
Delay in payment of service tax	10 days	20 days

Aggregate value of taxable services rendered in preceding financial year by ABC Ltd. was ₹ 35,00,000 and by Gagan was ₹ 70,00,000.

CENVAT credit

25. Compute the CENVAT credit available with Hanuman Services Ltd., an output service provider, in respect of the following services availed by it in the month of October, 2016:-

S.No.	Services availed	Service tax paid* (₹)
(i)	Accounting and auditing services	30,00,000
(ii)	Legal services	7,50,000
(iii)	Security services	60,000

(iv)	Motor vehicles taken on rent (Such motor vehicles are not eligible capital goods for the purposes of claiming CENVAT credit)	2,50,000

** including Swachh Bharat Cess (SBC) & Krishi Kalyan Cess (KKC)*

SUGGESTED ANSWERS

1. Computation of gross total income of Mr. Suhaan for the A.Y. 2017-18

	Particulars	Resident & ordinarily resident	Resident but not ordinarily resident	Non-Resident
		₹	₹	₹
(a)	Income earned from business in France which is controlled from Mumbai, out of which ₹ 65,000 is received in India	90,000	90,000	65,000
(b)	Pension for services rendered in India but received in France	14,000	14,000	14,000
(c)	Dividend received in France from a Titanium Inc., a French company	25,000	-	-
(d)	Rent from property in France deposited in a bank in France	59,500	-	-
(e)	Dividend from Sunset Ltd., an Indian Company	-	-	-
Gross Total Income		**1,88,500**	**1,04,000**	**79,000**

Notes:

(a) As per section 5(1), global income is taxable in case of a resident. However, as per section 5(2), in case of a non-resident, only the following incomes are chargeable to tax in India:

(i) Income received or deemed to be received in India; and

(ii) Income accruing or arising or deemed to accrue or arise in India.

Further, the income which accrues or arise outside India would be chargeable to tax in case of resident but not ordinarily resident in India, only if such income is derived from a business controlled in India.

Accordingly, the entire income earned from business in France which is controlled from Mumbai would be chargeable to tax in the hands of Mr. Suhaan if he is a resident in India or resident but not ordinarily resident. However, if he is non-resident then only that part of income which is received in India would be taxable in his hands.

(b) Pension for services rendered in India but received in France would be taxable in all cases, since it has accrued or arisen in India.

(c) Dividend received in France from a French company would be taxable in the hands of Mr. Suhaan, only if he is resident and ordinarily resident in India. If he is a resident but not ordinarily resident or a non-resident, the same would not be taxable in his hands in India since it has neither accrued or arisen in India nor is it received in India.

(d) Likewise, rental income from property in France would also be taxable only if he is resident in India. It has been assumed that the rental income is the gross annual value of the property. Therefore, deduction @30% under section 24, has been provided and the net income so computed is taken into account for determining the gross total income of a resident and ordinarily resident.

	₹
Rent received (assumed as gross annual value)	85,000
Less: Deduction under section 24 (30% of ₹ 85,000)	25,500
Income from house property	59,500

(e) Dividend from Indian company is exempt under section 10(34), whether the recipient is a resident, resident but not-ordinarily resident or non-resident.

2. (a) False: Any payment from an approved superannuation fund made by way of transfer to the account of an employee under a notified pension scheme referred to in section 80CCD is exempt under section 10(13). Since Atal Pension Yojana is a notified pension scheme under section 80CCD, the payment of ₹12 lakhs made by T Ltd. by way of transfer from an approved superannuation fund to Mr. Swayam's account under such scheme is exempt under section 10(13).

(b) False: Section 10(2) exempts any sum received by an individual as a member of a HUF where such sum has been paid out of the income of the family. Therefore, ₹ 12,000 would not be included in Mr. Arpit's taxable income.

(c) False: As per section 115BBDA, dividend in excess of ₹10 lakhs would be chargeable to tax @10% in the hands of, *inter alia*, an individual, resident in India. Section 10(34) exempts dividend distributed by domestic companies in the hands of the recipient, since the same has been subject to dividend distribution tax under section 115-O in the hands of the company. However, the amount of dividend which is chargeable to tax under section 115BBDA would not be exempt under section 10(34).

Accordingly, dividend received upto ₹ 10 lakh would be exempt under section 10(34) in the hands of Ms. Arpita. However, dividend in excess of ₹10 lakh i.e., ₹ 2 lakhs, would be taxable@10% in her hands.

(d) **False:** Exemption under section 10(26AAA) is available to a Sikkimese individual not only in respect of income from any source in the state of Sikkim, but also in respect of income by way of dividend or interest on securities.

3. **Computation of Total Income and tax liability of Mrs. Shakshi for A.Y. 2017-18**

Particulars	₹	₹
Income from salary		
Basic salary		9,60,000
Dearness allowance		2,64,000
Bonus		1,60,000
Commission (calculated as percentage of turnover)		1,20,000
Entertainment allowance		35,000
Children's hostel allowance	9,600	
Less : Exemption (₹ 300 x 12 x 2)	7,200	2,400
Interest credited to recognized provident fund account (exempt)		-
Rent free unfurnished accommodation (Refer Working Note 1)		84,000
Excess contribution to PF by employer (Refer Working Note 2)		38,720
Gross salary/Gross Total Income		**16,64,120**
Less **: Deduction under section 80C**		
Life insurance premium paid for insurance of major daughter	18,000	
Contribution to recognized provident fund	2,00,000	
	2,18,000	
Restricted to	1,50,000	
Deduction under section 80CCC in respect of LIC pension fund	60,000	
	2,10,000	
Deduction limited to ₹ 1,50,000 as per section 80CCE		1,50,000

Deduction under section 80D		
Medical Insurance premium in respect of self and spouse		26,000
Deduction under section 80G		
Donation to Public Charitable Trust ₹ 1,50,000 restricted to 50% of ₹ 1,48,812 (10% of adjusted total income) (Refer Working Note 3)		74,406
Total income		**14,13,714**
Total Income (Rounded Off)		**14,13,710**
Tax on total income [20,000 + 1,00,000 + (14,13,710 -10,00,000) x 30%]		2,44,113
Add : Education cess @ 2%		4,882
Add : Secondary and higher education cess @ 1%		2,441
Total tax liability		**2,51,436**
Tax Liability (rounded off)		**2,51,440**

Working Notes:

(1) Value of rent free unfurnished accommodation

Particulars	₹
Basic salary	9,60,000
Dearness allowance	2,64,000
Bonus	1,60,000
Commission@0.1% of turnover	1,20,000
Entertainment allowance	35,000
Children's hostel allowance	2,400
Gross Salary	**15,41,400**
15% of salary	2,31,210
Actual rent paid by the company	84,000
The least of the above is chargeable perquisite.	

(2) Employer's contribution to P.F. in excess of 12% of salary

Employer's contribution	₹ 2,00,000
Less : 12% of basic salary, dearness allowance & commission 12% of ₹ 13,44,000	₹ 1,61,280
	₹ 38,720

(3) Deduction@50% is allowable on donation made to public charitable trust subject to qualifying limit, which is 10% of adjusted total income i.e., ₹ 1,48,812 [i.e., Gross Total Income ₹ 16,64,120 (-) Deduction under section 80C/80CCC ₹ 1,50,000 (-) Deduction under section 80D ₹ 26,000].

Therefore, ₹ 74,406, being 50% of ₹ 1,48,812 is allowable as deduction under section 80G. In this case, since donation is made otherwise than by way of cash, it qualifies for deduction under section 80G.

4. Since the unrealised rent was recovered in the P.Y.2016-17, the same would be taxable in the A.Y.2017-18 under section 25A, irrespective of the fact that Mr. Aakarsh was not the owner of the house in that year. Further, the arrears of rent was also received in the P.Y.2016-17, and hence the same would also be taxable in the A.Y.2017-18 under section 25A, even though Mr. Aakarsh was not the owner of the house in that year. Both unrealised rent and arrears of rent would be taxable under the head "Income from house property". A deduction of 30% of unrealised rent recovered and arrears of rent would be allowed while computing income from house property of Mr. Aakarsh for A.Y.2017-18.

Computation of income from house property of Mr. Aakarsh for A.Y.2017-18

	Particulars	₹
(i)	Unrealised rent recovered	17,000
(ii)	Arrears of rent received	28,000
		45,000
Less:	Deduction@30%	13,500
Income from house property		**31,500**

5. (i) Allowable as deduction: As per section 36(1)(viia)(d), deduction is allowed to a non-banking financial company on account of provision for bad and doubtful debts of an amount not exceeding 5% of total income (before making any deduction under section 36(1)(viia) and Chapter VI-A).

Accordingly, XYZ Credit Corporation, a non-banking finance company would be eligible for deduction in respect of provision for bad and doubtful debt provided such amount does not exceed 5% of total Income (before making any deduction under section 36(1)(viia) and Chapter VI-A).

(ii) Allowable as deduction: As per section 43B, the allowability of deduction in respect of any sum payable by an assessee to the Indian Railways for use of Railway Assets is subject to actual payment of such sum on or before the due date of filing return of income under section 139(1).

Thus, in the present case, ₹ 45,000 paid by ABC Ltd. to Indian Railways for use of railway assets would be allowed as deduction while computing the business income for the previous year 2016-17, since such payment is made on or before the due date for filing return of income for the previous year 2016-17, being the year in which such liability incurred.

(iii) **Not allowable as deduction:** Income-tax paid by the employer in respect of non-monetary perquisites provided to its employees is exempt in the hands of the employee under section 10(10CC). As per section 40(a)(v), such income-tax paid by the employer is not deductible while computing business income.

Therefore, income-tax of ₹ 55,000 paid by the MNO Ltd. in respect of non-monetary perquisites provided to an employee would not be allowed as deduction while computing its business income.

(iv) **Allowable as deduction:** The limit for attracting disallowance under section 40A(3) for payment otherwise than by way of account payee cheque or account payee bank draft is ₹ 35,000 in case of payment made for plying, hiring or leasing goods carriage to a transporter.

Therefore, in the present case, no disallowance under section 40A(3) would be attracted in the hands of S Ltd. in respect of payment of ₹ 32,000 made in cash for carriage of goods to a transporter. Further, disallowance under section 40(a)(ia) for non-deduction of tax at source would also not be attracted, since the provisions for deduction of tax at source under section 194C are not applicable, in case of a transporter owning not more than 10 goods carriages at any time during the previous year.

(v) **Allowable as deduction:** As per Rule 6DD, in case the payment is made for purchase of agricultural produce directly to the cultivator, grower or producer of such agricultural produce, no disallowance under section 40A(3) is attracted even if the cash payment for the expense exceeds ₹ 20,000.

Therefore, disallowance under section 40A(3) would not be attracted in this case, since cash payment for purchase of wheat is made directly to the farmer.

6. Computation of Capital Gains chargeable to tax in the hands of Mr. Mayank for the A.Y. 2017-18

Particulars	₹	₹
Gross Sale Consideration on transfer of residential house		85,00,000
[As per section 50C, in case the actual sale consideration is lower than the stamp duty value fixed by the stamp valuation authority, the stamp duty value shall be deemed as the full value of consideration]		
Less: Brokerage @ 2% of actual sale consideration of ₹ 68,00,000		1,36,000
Net Sale Consideration		83,64,000

Less: Indexed cost of acquisition [₹ 8,00,000 x 1125/140]		64,28,571
Long-term capital gain		19,35,429
***Less:* Exemption under section 54**		
- Acquisition of residential house property at Kota on 3.3.2017 (i.e., within the prescribed time of two years from 14.12.2016, being the date of transfer of residential house at Noida).	7,00,000	
- Amount deposited in Capital Gains Accounts Scheme on or before the due date of filing return of income for construction of additional floor on the residential house property at Kota. Since Mr. Mayank has no other source of income, his due date for filing return of income is 31st July, 2017 [Therefore, ₹ 4,50,000 deposited on 16.7.2017 will be eligible for exemption whereas ₹ 8,70,000 deposited on 11.11.2017 will not be eligible for exemption under section 54]	4,50,000	11,50,000
Exemption under section 54EC		
- Amount deposited in capital gains bonds of NHAI within six months from the date of transfer (i.e., on or before 13.6.2017) would qualify for exemption. [Therefore, in this case, ₹ 3,50,000 deposited in capital gains bonds of NHAI on 14.5.2017 would be eligible for exemption under section 54EC, whereas ₹ 5,50,000 deposited on 25.7.2017 would not qualify for exemption]		3,50,000
Long-term capital gain		**4,35,429**

Computation of tax liability of Mr. Mayank for A.Y. 2017-18

Particulars	₹
Tax on ₹ 1,85,429 (i.e. Long term capital gain ₹ 4,35,429 less basic exemption limit of ₹ 2,50,000) is charged @ 20% [Section 112]	37,086
(Since long-term capital gains is the only source of income, the entire basic exemption limit can be exhausted against this income)	
Less: Rebate under section 87A	5,000
	32,086
Add: Education cess@2% and Secondary & higher education cess @ 1%	963
Total tax liability	**33,049**
Total tax liability (rounded off)	**33,050**

***Note:** As per the decision of Gauhati High Court in CIT vs Rajesh Kumar Jalan 286 ITR 274 and Haryana High Court in CIT vs Jagriti Agarwal 245 CTR 629, exemption under section 54 is allowable even if the amount of capital gain is deposited in Capital Gains Accounts Scheme within the period specified for filing a belated return under section 139(4) [i.e., on or before 31.3.2018].*

If we apply the above interpretation in this case, Mr. Mayank would be eligible for exemption under section 54 in respect of ₹ 8,70,000 deposited in Capital Gains Accounts Scheme on 11.11.2017 also, since the said date falls within the time specified under section 139(4). On the basis of this interpretation, the long term capital gain chargeable to tax in the hands of Mr. Mayank would be Nil and the consequent tax liability would also be Nil.

Long-term capital loss of ₹ 4,34,571 can be carried forward for set-off against long-term capital gains of subsequent assessment year. It can be carried forward for a maximum of eight assessment years.

7. Section 145A provides that interest received by the assessee on enhanced compensation shall be deemed to be the income of the assessee of the year in which it is received, irrespective of the method of accounting followed by the assessee and irrespective of the financial year to which it relates.

Section 56(2)(viii) states that such income shall be taxable as 'Income from other sources'.

50% of such income shall be allowed as deduction by virtue of section 57(iv) and no other deduction shall be permissible from such Income.

Therefore, he cannot claim deduction in respect of legal expenses incurred to receive the interest on enhanced compensation from such income.

Computation of interest on enhanced compensation taxable as "Income from other sources" for the A.Y 2017-18:

Particulars	₹
Interest on enhanced compensation taxable under section 56(2)(viii)	5,32,000
Less: Deduction under section 57(iv) (50% x ₹ 5,32,000)	2,66,000
Taxable interest on enhanced compensation	2,66,000

8. As per the provisions of section 64(1A) of the Income-tax Act, 1961, all the income of a minor child has to be clubbed in the hands of that parent whose total income (excluding the income of the minor) is greater. The income of Mr. Abhinav is ₹ 4,15,000 and income of Mrs. Suhaani is ₹ 3,25,000. Since the income of Mr. Abhinav is greater than that of Mrs. Suhaani, the income of the minor children have to be clubbed in the hands of Mr. Abhinav. It is assumed that this is the first year when clubbing provisions are attracted.

Income derived by a minor child from any activity involving application of his/her skill, talent, specialised knowledge and experience is not to be clubbed. Hence, the income of minor child Shreya from giving music concerts will not be included in the hands of either parent.

However, interest from bank deposit has to be clubbed even when deposit is made out of income arising from application of special talent.

The Gross Total Income of Mrs. Suhaani is ₹ 3,25,000. The gross total income of Mr. Abhinav giving effect to the provisions of section 64(1A) is as follows:

Computation of gross total income of Mr. Abhinav for the A.Y. 2017-18

Particulars	₹	₹
Income from business		4,15,000
Income of minor son Chetan from fixed deposit	25,000	
Less: Exemption under section 10(32)	1,500	23,500
Income of minor daughter Shreya		
(i) From music concerts		
[From special talent – not to be clubbed]	-	
(ii) Interest from bank	7,000	
(iii) Gift of ₹ 5,500 received from a non-relative is not taxable under section 56(2)(vii) being less than the aggregate limit of ₹ 50,000	Nil	
	7,000	
Less : Exemption under section 10(32)	1,500	5,500
Gross Total Income		**4,44,000**

9. Computation of total income of Mr. Tarun for the A.Y.2017-18

Particulars	₹	₹
Salaries		
Income from salaries	2,55,000	
Less: Loss from house property	2,19,000	36,000
Profits and gains of business or profession		
Income from speculation business	28,000	
Less: Loss from toys business set off	28,000	Nil
Capital gains		
Long-term capital gains from sale of urban land	2,75,500	
Less: Loss from toys business set off	2,17,000	58,500
Income from other sources		
Income from betting		49,000
Gross total income		**1,43,500**

Less: Deduction under section 80C (deposit in PPF)		36,000
Total income		**1,07,500**

Losses to be carried forward to A.Y. 2018-19:

Particulars	₹
(1) Loss from toys business **(₹ 2,45,000 - ₹ 28,000 - ₹ 2,17,000)**	Nil
(2) Loss from specified business covered by section 35AD	46,000

Notes:

(i) Long-term capital gains from sale of listed shares in a recognized stock exchange is exempt under section 10(38). Loss from an exempt source cannot be set off against profits from a taxable source. Therefore, long-term capital loss on sale of listed shares cannot be set-off against long-term capital gains from sale of urban land.

(ii) Loss from specified business covered by section 35AD can be set-off only against profits and gains of any other specified business as per section 73A. Therefore, such loss cannot be set off against any other income. The unabsorbed loss has to be carried forward for set-off against profits and gains of any specified business in the following year, provided the return is filed on or before the due date under section 139(1).

(iii) Loss from toys business cannot be set off against salary income. However, the balance business loss of ₹ 2,17,000 [₹ 2,45,000 – ₹ 28,000 set-off against income from speculation business as per section 70(1)] can be set-off against long-term capital gains of ₹ 2,75,500 from sale of urban land as per section 71(2). Consequently, the taxable long-term capital gains would be ₹ 58,500.

(iv) Loss from card games can neither be set off against any other income, nor can it be carried forward.

(v) For providing deduction under Chapter VI-A, gross total income has to be reduced by the amount of long-term capital gains and casual income. Therefore, the deduction under section 80C in respect of the amount deposited in PPF has to be restricted to ₹36,000 [i.e., Gross Total Income of ₹ 1,43,500 – ₹ 58,500 (LTCG) - ₹ 49,000 (Casual income)].

(vi) Income from betting is chargeable at a flat rate of 30% under section 115BB and no expenditure or allowance can be allowed as deduction from such income, nor can any loss be set-off against such income.

10. (i) False: A proviso has been inserted in section 80CCD(3) to provide that the amount received by the nominee, on closure of NPS account on the death of the assessee, shall not be deemed to be the income of the nominee.

Therefore, ₹ 9 lakhs, being the amount received by Mrs. Leena, widow of Mr. Sahitya as a nominee on closure of NPS account on his death would not be deemed as income in her hands.

(ii) **False,** as per section 80GG, least of the following is allowed as deduction:

(a) Actual rent paid *less* 10% of total income

96,000 minus $\frac{(10 \times 3,80,000)}{100}$ = ₹ 58,000

(b) 25% of total income

$\frac{25 \times 3,80,000}{100}$ = ₹ 95,000

(c) Amount calculated at ₹ 5,000 p.m.= ₹ 60,000

Thus, Mr. Gopal is eligible to claim deduction of only ₹ 58,000 under section 80GG and not a flat deduction of ₹ 60,000.

(iii) **False:** Mr. Anay has to pay ₹ 2,64,000 (₹ 32,00,000 x 11% x 9/12) towards interest on housing loan during the previous year 2016-17.

He would be eligible to claim ₹ 2,00,000 as deduction under section 24(b) under the head "Income from House Property" In addition, he can claim deduction of ₹ 50,000 under section 80EE from gross total income, in respect of the balance amount of ₹ 64,000 (₹ 2,64,000 – ₹ 2,00,000) during the P.Y. 2016-17.

11. Computation of total income of Mr. Dinesh for the A.Y. 2017-18

Particulars	₹	₹
Income from business of plying goods vehicle (Refer Note 1)		6,52,500
Less: Brought forward business loss of financial year 2015-16 (Refer Note 2 & 3)		1,28,000
Gross Total Income		**5,24,500**
Less: **Deduction under Chapter VI-A**		
Section 80C:-		
Life insurance premium paid for insurance of married daughter (Refer Note 5)	25,000	
Section 80D:-		
Medical insurance premium paid for insurance of mother (Refer Note 6)	30,000	

Section 80E:- Interest paid towards education loan taken for studies of his son (Refer Note 7)	22,000	77,000
Total Income		**4,47,500**

Working Notes:

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

Particulars	₹
5 heavy goods vehicle held throughout the year (₹ 7,500×5×12)	4,50,000
3 heavy goods vehicle – held for 9 months (₹ 7,500×3×9)	2,02,500
Income under section 44AE	6,52,500

(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 ₹ 95,000 shall not be allowed as a deduction since it is covered by section 32.

(3) Brought forward business loss of ₹ 1,28,000 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. 2016-17 was filed before the due date specified under section 139(1).

(4) Tax saver deposit in the name of married daughter 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 ₹ 28,000 paid for insurance policy of married daughter, only ₹ 25,000 (being 10% of ₹ 2,50,000) is allowable 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 ₹ 30,000. Hence, deduction of ₹ 30,000 is provided to Mr. Dinesh, as his mother is a senior citizen and the premium is paid otherwise than by way of cash.

(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.

12. (a) Since the rent paid for hire of machinery by Trip Ltd. to Mr. Kartik exceeds ₹ 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. Kartik has furnished his permanent account number to Trip Ltd.

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

= ₹ 2,50,000 x 2% = ₹ 5,000.

Note: In case Mr. Kartik has not furnished his permanent account number to Trip Ltd., tax shall be deducted @ 20% on ₹ 2,50,000, by virtue of provisions of section 206AA.

(b) 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, even if Verma (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. Sarthak is paid for a personal purpose i.e. the surgery of a member of the family.

(c) Section 194J provides for deduction of tax at source @10% from any sum paid by way of any remuneration or fees or commission, by whatever name called, to a director, which is not in the nature of salary on which tax is deductible under section 192. The threshold limit of ₹ 30,000 upto which the provisions of tax deduction at source are not attracted in respect of every other payment covered under section 194J is, however, not applicable in respect of sum paid to a director.

Therefore, in this case, tax@10% has to be deducted at source under section 194J in respect of the sum of ₹ 29,000 paid by XYZ Ltd. to its director. Thus, tax of ₹ 2,900 has to be deducted at source.

13. Since Mr. Vardaan has income only under the heads "Salaries", "Income from house property" and "Income from other sources", he does not fall under the category of a person whose accounts are required to be audited under the Income-tax Act, 1961 or any other law in force. Therefore, the due date of filing return for A.Y.2017-18 under section 139(1), in his case, is 31st July, 2017. Since Mr. Vardaan had submitted his return of income only on 30.11.2017, the said return is a belated return under section 139(4).

Section 139(5) now permits a return furnished under section 139(1) as well as a belated return furnished under section 139(4) to be revised. Thus, a belated return under section 139(4) can also be revised. The time limit for filing a revised return is one year from the end of the relevant assessment year. In this case, the time limit would expire only on 31.3.2019. He has discovered the mistake in May 2018 itself. Therefore, Mr. Vardaan can revise the belated return of income filed by him to claim deduction under section 80C, since the time limit of one year from the end of the relevant assessment year has not elapsed.

14. Computation of excise duty payable

Particulars	₹
Price of the machinery	4,00,000
Add: Packing charges [Note 1]	20,000
Add: Extra design charges [Note 1]	50,000
Total	4,70,000
Less : 2% cash discount on price of machinery [₹ 4,00,000 x 2%] [Note 2]	8,000
Assessable value	4,62,000
Excise duty @ 12.5%	**57,750**

Notes:

1. While computing assessable value, packing charges and extra designing charges have been included as such payments are in connection with sale.
2. Cash discount has been allowed as deduction since discount has been passed on to the buyer.
3. While computing assessable value, outward freight and transit insurance has not been included as they are incurred for transporting the goods beyond the place of removal.
4. State VAT does not affect excise duty payable.

15. Computation of customs duty payable

Particulars		₹
Assessable value (A)	(A)	2,00,000.00
Basic customs duty @ 10% of (A)	(B)	20,000.00
CVD [Refer note below]	(C)	43,750.00
Education cesses of customs @ 3% on [(B) + (C)]	(D)	1,912.50
Value for computing special CVD [(A) + (B) + (C) + (D)]	(E)	2,65,662.50
Special CVD @ 4% on (E) (rounded off)	(F)	10,626.50
Total custom duty payable [(B) + (C) + (D) + (F)] [Rounded off]		**76,289**

Note: If imported goods are similar to goods covered under section 4A of the Central Excise Act, 1944, CVD is payable on basis of MRP printed on the package less abatement, as permissible. Therefore, CVD is computed as under:

Particulars	₹
Maximum retail price [10,000 pieces × ₹ 50]	5,00,000
Less: Abatement @ 30%	1,50,000
Assessable value for CVD	3,50,000
CVD @ 12.5% of ₹ 3,50,000	43,750

16. **(i)** When the goods are sent by dealer outside the State to his other place of business, such movement of goods is an inter-State stock transfer and is not liable to central sales tax. The burden to prove that the inter-State movement of goods is stock transfer, lies on the dealer and not on the Department. For this purpose, the dealer has to submit a declaration obtained from his other place of business in Form F.

(ii) If at the time of stock transfer outside the State, the dealer has an order for such sale in hand; movement of such goods shall be deemed to have been occasioned as a result of sale. Therefore, such inter-State sale of goods will be liable to central sales tax.

17. **Computation of Net VAT payable and input tax credit**

Particulars	₹
Output VAT	
Purchases of raw material [excluding VAT of ₹ 95,000 (₹ 8,55,000 × 12.5/112.5)]	7,60,000
Manufacturing and other expenses	1,00,000
Cost of production	8,60,000
Cost of goods sold [80% of ₹ 8,60,000]	6,88,000
Add: Profit @ 25% on the cost of goods sold	1,72,000
Sale price	8,60,000
Output VAT payable @ 12.5% **(A)**	1,07,500
Input VAT	
Input tax credit on raw materials used in manufacture of finished goods that are sold [₹ 95,000 x 80%]	76,000
Input tax credit on raw materials used in manufacture of finished goods that are stock transferred to Manipur [₹ 7,60,000 × 20% × (12.5 – 2)%]	15,960

(In case of inter-state stock transfer of finished goods, input tax paid on inputs used in manufacture of such finished goods in excess of 2% is available as input tax credit.)	
Total input tax credit (B)	**91,960**
Net VAT payable (A) – (B)	**15,540**

18. (a) The compensation for termination of employment will not attract service tax as it is under the terms of employment. Such amount paid by the employer to the employee for premature termination of contract of employment is treatable as amounts paid in relation to services provided by the employee to the employer in the course of employment. Hence, amount so paid would not be chargeable to service tax.

(b) As per section 65B(44) of the Finance Act, 1994, only services provided by an employee to the employer are outside the ambit of services under service tax law; services provided outside the ambit of employment for a consideration would be a taxable service liable to service tax. In the present case, Mr. B is hired as a legal consultant, and hence Mr. B is liable to pay service tax.

Further, Mr. B has to register under service tax law, make quarterly payment of service tax (since he is an individual) and file half yearly returns for the half year ending on 30th September and 31st March.

19. (a) In case of taxable service provided by a director of a company to said company, service recipient is liable to pay service tax under reverse charge mechanism.

Further, rule 7 of Point of Taxation Rules, 2011, *inter alia,* provides that in respect of persons liable to pay service tax under reverse charge mechanism, the point of taxation shall be the date on which payment is made subject to the condition that payment is made within a period of three months of the date of invoice.

However, if payment is not made within a period of 3 months of date of invoice, point of taxation will be first day that occurs immediately after expiry of said 3 months.

Since, in the present case, payment is made in August end, which is beyond 3 months of the date of invoice (invoice is issued in April), the point of taxation would be the first day that occurs immediately after expiry of said 3 months.

(b) Point of taxation in case of import of service by "associated enterprises" where the person providing the service is located outside India is-

(i) date of debit in the books of account of the person receiving the service

OR

(ii) date of making the payment

whichever is earlier

Here, date of debit in XYZ Ltd.'s books of accounts is 07.02.2016 and date of payment to Dubai firm is 25.02.2016. Therefore, point of taxation is 07.02.2016.

20. As per rule 6 of the Service Tax (Determination of Value) Rules, 2006, only the commission received by the air travel agent from the airlines is included in the value of taxable service. The air fare collected by the air travel agent in respect of the service provided by him does not form part of the value of taxable service. Accordingly, the service tax liability of Mr. P would be computed as under:

Particulars	₹
Basic air fare collected for domestic booking of tickets	Nil
Basic air fare collected for international booking of tickets	Nil
Commission received from the airlines on the sale of domestic and international tickets	5,00,000
Value of taxable service	5,00,000
Service tax @ 14%	70,000
Add: Swachh Bharat Cess (SBC) @ 0.5% (₹ 5,00,000 x 0.5%)	2,500
Add: Krishi Kalyan Cess (KKC) @ 0.5% (₹ 5,00,000 x 0.5%)	2,500
Service tax payable (including SBC & KKC)	**75,000**

However, if Mr. P opts for the special provision for payment of service tax as provided under rule 6 of the Service Tax Rules, 1994, service tax liability would be computed as under:

Particulars	₹
0.7% of the basic air fare collected for domestic booking of tickets [₹ 40,00,000 × 0.7%]	28,000
1.4% of the basic air fare collected for international booking of tickets [₹ 60,00,000 × 1.4%]	84,000
Service tax	1,12,000
Add: Swachh Bharat Cess (SBC) @ 0.5% (₹ 1,12,000 x $\frac{0.5}{14}$)	4,000
Add: Krishi Kalyan Cess (KKC) @ 0.5% (₹ 1,12,000 x $\frac{0.5}{14}$)	4,000
Service tax payable (including SBC & KKC)	**1,20,000**

Therefore, as can be seen from the above two computations of service tax, the service tax liability of Mr. P would not be reduced in the aforesaid option.

21. As per section 66D(g) of the Finance Act, 1994, selling of space for advertisements in print media is included in the negative list of services. In other words, advertisement in all media except print media is liable to service tax. Therefore, sale of space for advertisements on internet websites, sale of time for advertisement to be broadcast on TV Channel and advertising on film screen in theatres are liable to service tax.

Further, definition of print media specifically excludes business directories. Therefore, advertising in business directories attracts service tax.

Services related to preparation of advertisement are liable to service tax as they are not included in the negative list.

Computation of service tax payable

Services	Value of service (₹)	Service tax @ 15% (including SBC & KKC) (₹)
Sale of space for advertisement in a leading newspaper	2,15,000	Nil
Services related to preparation of advertisement	60,000	9,000
Sale of space for advertisements on internet websites	40,000	6,000
Sale of time for advertisement to be broadcast on TV Channel	1,50,000	22,500
Advertising in business directories	30,000	4,500
Advertising on film screen in theatres	1,00,000	15,000

22. With effect from 01.04.2016, the exemption available to transportation of passengers, with or without accompanied belongings by, *inter alia,* a ropeway, cable car or aerial tramway vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* has been withdrawn.

Therefore, service tax is payable in case of transporting of pilgrims by cable car to the holy shrine situated at the mountain top. It may be noted that service tax is payable irrespective of the purpose of transport of the passengers i.e., religious or otherwise.

23. Mega exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts services provided by an educational institution to its students, faculty and staff. Further, an educational institution means an institution providing services by way of *inter alia* —

(i) pre-school education and education up to higher secondary school or equivalent;

(ii) education as a part of a curriculum for obtaining a qualification recognised by any law for the time being in force.

(a) Service tax is not payable on educational services rendered by the play school (providing pre-school education) in the given case as the Educational Trust - Gyan

Mandal - falls under the definition of 'educational institution' and services provided by it are exempt from service tax.

(b) Service tax is not payable in this case as Shining Stars Public School providing educational services upto higher secondary school is covered within the definition of educational institution and services provided by it are exempt from service tax.

(c) Since coaching given by private coaching institutes/centers is not part of a curriculum for obtaining recognized qualification, the same is not covered within the definition of educational institution. Therefore, service tax is payable by coaching center providing coaching for MBA entrance examination.

24. Computation of interest on delayed payment of service tax

Name of the service provider	ABC Ltd.	Gagan
Service tax liability	₹ 1,00,000	₹ 2,00,000
Delay in payment of service tax	10 days	20 days
Value of taxable services in previous financial year	₹ 35,00,000	₹ 70,00,000
Rate of interest	12% per annum	15% per annum
Interest (rounded off)	[₹ 1,00,000 × (12/100) × (10/365)] =₹ 329 (rounded off)	[₹ 2,00,000 × (15/100) × (20/365)] =₹ 1,644 (rounded off)

Note: As per section 75 of Finance Act, 1994 read with *Notification No. 13/2016 ST dated 01.03.2016,* in case of collection of any amount as service tax but failing to pay the amount so collected to the credit of the Central Government on or before the date on which such payment becomes due, the simple interest @ 24% p.a. is payable.

However, in all other cases, 15% simple interest p.a. is payable. Since in the above case, service tax has not been collected, so simple interest @ 15% p.a. is payable.

Further, the applicable rate gets reduced by 3% for service providers whose turnover of services does not exceed ₹ 60 lakh in the preceding financial year.

25. Computation of CENVAT credit available with Hanuman Services Ltd.:

Particulars	Service tax @ 14% (₹)	Krishi Kalyan Cess @ 0.5% (₹)
Accounting and auditing services [Note 1]	28,00,000	1,00,000
Legal services [Note 1]	7,00,000	25,000
Security services [Note 1]	56,000	2,000

Motor vehicles taken on rent [Note 2]	Nil	Nil
Total CENVAT credit available	**35,56,000**	**1,27,000**

Notes:

1. As per the definition of the input services, there is a specific inclusion with regard to the following services:-
   (a) Accounting and auditing services
   (b) Legal services
   (c) Security services

   Hence, the CENVAT credit of the service tax paid on the aforesaid services is available.
2. The definition of input services specifically excludes the services of renting of motor vehicles which are not eligible capital goods.
3. Credit of SBC is not available since it is not CENVATable. Further, since Hanuman Services Ltd. is an output service provider, credit of KKC is available.