Test Series: February, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

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

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

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

Working Notes should form part of the answer.

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

1. (a) Classify the following activities as (1) Operating Activities, (2) Investing Activities, (3) Financing Activities as per AS 3:

   a. Purchase of Machinery.

   b. Proceeds from issuance of equity share capital.

   c. Cash Sales.

   d. Proceeds from long-term borrowings.

   e. Proceeds from Debtors.

   f. Brokerage paid on purchase of investments.

   (b) On 1st December, 2011, BC Co. Ltd. undertook a contract to construct a building of ₹ 21.25 lakhs. On 31st March, 2012, the company found that it had already spent ₹ 16,24,750 on the construction. Prudent estimate of additional cost for completion was ₹ 8,00,250. What amount should be charged to revenue in the final accounts for the year ended 31st, March, 2012?

   (c) Shyam Restaurant purchased from Rang Ltd. a colour T.V set on 1st October, 2011 on the hire purchase system. The cash price of the set was ₹ 15,000. Term of payment were ₹ 1,150 down and ₹ 4,000 half yearly over two years, the first instalment was to be paid on 31st March, 2012. Rate of interest was 12% p.a. Shyam Restaurant wrote off 15% depreciation p.a. on reducing instalment basis and closed its books every year on 31st March. It could not pay the second instalment due on 30th September, 2012 and as a consequence, Rang Ltd. repossessed the T.V set. Prepare Shyam Restaurant Account in Rang Ltd.'s books of account. Assume that the estimated value of the T.V set at the time of repossession was ₹ 12,000. Also assume Rang Ltd. closes its books of accounts every year on 31st March.

(d) U.S.A Ltd. purchased raw material @ ₹ 400 per kg. Company does not sell raw material but uses in production of finished goods. The finished goods in which raw material is used are expected to be sold at below cost. At the end of the accounting year, company is having 10,000 kg of raw material in stock. As the company never sells the raw material, it does not know the selling price of raw material and hence cannot calculate the realizable value of the raw material for valuation of inventories at the end of the year. However replacement cost of raw material is ₹ 300 per kg. How will you value the inventory of raw material? *(4 x 5 = 20 Marks)*

2. (a) Following is the summarized Balance Sheet of Max Ltd. as at March 31, 2013:

Liabilities	₹	Assets	₹
Share capital:		Goodwill	20,000
Equity shares of ₹ 100 each	15,00,000	Other fixed assets	15,00,000
9% Preference shares of ₹ 100 each	5,00,000	Trade Receivables	6,51,000
General reserve	1,80,000	Inventory	3,93,000
Profit and loss account	-	Cash at bank	26,000
12% Debentures of ₹ 100 each	6,00,000	Own debenture	1,92,000
Trade Payables	4,15,000	(Nominal value 2,00,000)	
		Discount on issue of debentures	2,000
		Profit and loss account	4,11,000
	31,95,000		31,95,000

On 1.4.2013, Max Ltd. adopted the following scheme of reconstruction:

(i) Each equity share shall be sub-divided into 10 equity shares of ₹ 10 each fully paid up. 50% of the equity share capital would be surrendered to the Company.

(ii) Preference dividends are in arrear for 3 years. Preference shareholders agreed to waive 90% of the dividend claim and accept payment for the balance.

(iii) Own debentures of ₹ 80,000 were sold at ₹ 98 cum-interest and remaining own debentures were cancelled.

(iv) Debentureholders of ₹ 2,80,000 agreed to accept one machinery of book value of ₹ 3,00,000 in full settlement.

(v) Trade payables, Trade receivables and Inventories were valued at ₹ 3,50,000, ₹ 5,90,000 and ₹ 3,60,000 respectively. The goodwill, discount on issue of debentures and Profit and Loss (Dr.) are to be written off.

(vi) The Company paid ₹ 15,000 as penalty to avoid capital commitments of ₹ 3,00,000.

You are required to give Journal entries in the books of Max Ltd.

(b) Sumedha Ltd. took a loan from bank for ₹ 10,00,000 to be settled within 5 years in 10 equal half yearly instalments with interest. Normal First instalment is due on 1.6.2013 of ₹ 1,00,000. Determine how the loan will be classified for the purpose of the Financial Statements of Sumedha Ltd. for the year ended 31.3.2013 according to Revised Schedule VI. *(12 + 4 =16 Marks)*

3. (a) Ketan had accepted bills payable to Mitesh as follows:

10th April 2012	₹ 4,000	for 4 months
18th April 2012	₹ 5,000	for 3 months
25th May 2012	₹ 3,000	for 6 months
5th June 2012	₹ 6,000	for 3 months

On 1st July, it was agreed that these bills should be withdrawn and that Ketan 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 average due date.

(b) As at 31 March, 2013, the balance on the sales ledger control account of W Ltd. was ₹ 1,56,300, whilst the total of the list of balances on the sales ledger was ₹ 1,51,835. At the same time, the balance on the purchase ledger control account was ₹ 1,70,690. The total of the list of balances on the purchase ledger as at that date was ₹ 1,37,645 - this is after deducting debit balances of ₹ 900 (T Ltd.) and ₹ 16,200 (R Ltd.).

You are also given the following information:

(1) The debit balance on the account of T Ltd. arose as a result of posting a payment of ₹ 4,500 as ₹ 5,400.

(2) The debit balance on the account of R Ltd. represent a payment in advance for goods to be delivered and invoiced in April 2013.

(3) The purchase day book for 29 March 2013 had been incorrectly cast, overcastting the total by ₹ 1,260.

(4) A purchase of ₹ 7,050 from Q had not been posted to Q's account in the purchase ledger.

(5) An invoice received from M Ltd. for ₹ 15,000 had been entered in the purchase day book as ₹ 1,500.

(6) A bad debt of ₹ 3,695 written-off the S Ltd. in the sales ledger had been posted to the purchase ledger control account.

(7) Discount received amounting to ₹ 19,370 had been posted to the relevant accounts in the purchase ledger - but no posting had been made to either the purchase ledger control account or the discount received account.

(8) A contra entry of ₹ 770 between the accounts of Tisco Ltd. in the sales and purchase ledger had not been posted to either the sales ledger control account or the purchase ledger control account.

You are required to :

(a) Prepare a Sales Ledger Control Account Reconciliation and a Purchase Ledger Control Account Reconciliation as at 31 March 2013.

(b) Prepare journal entries required to reflect the information contained in (1) to (8) above. *(6 + 10= 16 Marks)*

4. (a) The premises of X Ltd. caught fire on 22nd January, 2013 and the stock was damaged. The firm made up accounts to 31st March each year and on 31st March, 2012 the stock at cost was ₹ 13,27,200 as against ₹ 9,62,200 on 31st March 2011.

Purchases from 1st April, 2012 to the date of fire were ₹ 34,82,700 as against ₹ 45,25,000 for the full year 2011-2012 and the corresponding sales figure were ₹ 49,17,000 and ₹ 52,00,000 respectively.

You are given the following further information:

(i) In July, 2012, goods costing ₹ 1,00,000 were given away for advertising purposes, no entries being made in the books.

(ii) During 2012-2013 a clerk misappropriated unrecorded cash sales. It is estimated that the defalcation averaged ₹ 2,000 per week from 1st April, 2012 until the clerk was dismissed on 18th August, 2012.

(iii) The rate of gross profit is constant.

From the above information, make an estimate of the stock in hand on the date of fire.

(b) Agra Company, incorporated on 1st April, 2013, took over running business from 1st January, 2013. The company prepares its first final accounts on 31st December, 2013. From the following information, you are required to calculate the sales ratio of pre-incorporation and post-incorporation periods:

1. Sales for January, 2013 to December, 2013 is ₹ 7,20,000,

2. The sales for the month of January is twice of the average sales; for the month of February it is equal to average sales, sales for four months from May to August is 1/4 of the average of each month; and sales for October and November is three times the average sales. *(8+8=16 Marks)*

5. The Balance Sheet of P and T who share profits & losses in the ratio of 3 : 1 as at 31st March, 2013 was as follows:

Liabilities	₹	Assets	₹	₹
Sundry creditors	60,000	Cash at bank		5,250
Employee's provident fund	6,150	Bills receivable		33,000
Profit and loss account	4,500	Debtors	25,500	
Contingency reserve	1,500	Less: Provision	1,500	24,000
General reserve	1,500	Stock		90,000
P's capital	1,10,700	Furniture and fixtures		16,500
T's capital	96,900	Land & building		1,12,500
	2,81,250			2,81,250

On 31st March, 2013, O was admitted into partnership on the following terms:

(a) The new profit sharing ratio of P, T and O will be 3 : 1 : 1.

(b) Goodwill of the firm was to be valued at two and half years' purchase of the average profits of the last three completed years. The profits were 2008-09 - ₹ 30,000, 2009-10 - ₹ 45,000, 2010-11 - ₹ 60,000, 2011-12 - ₹ 75,000, 2012-13 - ₹ 90,000.

(c) The stock was found overvalued by ₹ 9,000. Fixtures are to be brought down to ₹ 14,850. Provision for doubtful debts is to be made up to 5% on the debtors and bills receivable. Land & building was found undervalued by ₹ 22,500.

(d) The unaccrued income is ₹ 1,275.

(e) A claim on account of workmen's compensation for ₹ 225 to be provided for.

(f) Mr. X, an old customer whose account for ₹ 1,500 was written off as bad has promised in writing to pay 65% in settlement of his full debt.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of a new firm when O pays ₹ 60,000 as his capital but is unable to bring in any cash for his share of goodwill. No account for goodwill should remain in the books of new firm. The capitals of all partners will be in the same ratio as profit sharing ratio taking original capital of "O" as basis. The necessary adjustment should be made through current accounts. *(16 Marks)*

6. Mr. Hemant had ₹ 1,65,000 in the bank account on 1.1.2012 when he started his business. He closed his accounts on 31st March, 2013. His single entry books (in which he did not maintain any account for the bank) showed his position as follows:

	31.3.2012 ₹	*31.3.2013* ₹
Cash in hand	1,100	1,650
Stock in trade	10,450	15,950
Debtors	550	1,100
Creditors	2,750	1,650

On and from 1.2.2012, he began drawings ₹ 385 per month for his personal expenses from the cash box of the business. His account with the bank had the following entries:

	Deposits ₹	*Withdrawals* ₹
1.1.2012	1,65,000	-
1.1.2012 to 31.3.2012		1,22,650
1.4.2012 to 31.3.2013	1,26,500	1,48,500

The above withdrawals included payment by cheque of ₹ 1,10,000 and ₹ 33,000 respectively during the period from 1.1.2012 to 31.3.2012 and from 1.4.2012 to 31.3.2013 respectively for the purchase of machineries for the business. The deposits after 1.1.2012 consisted wholly of sale price received from the customers by cheques.

Draw up Mr. Hemant's statement of affairs as at 31.3.2012 and 31.3.2013 respectively and work out his profit or loss for the year ended 31.3.2013. *(16 marks)*

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

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

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

(b) "Recently a growing trend has developed for outsourcing the accounting functions to a third party". Analyse.

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

(d) Rajkumar Ltd. purchased a machine on 1st January 2006 for ₹ 300 lakhs. The machine was depreciated on straight line basis using a depreciation rate of 10% per annum. On 1-1-2010 the machine was revalued at ₹ 270 lakhs and the same was adopted. What will be the carrying cost of the machinery asset as on 31-12-2011? There is no change in the economic life of the asset.

(e) The details of receipts and payments for the Swaraj Club for the year ended December 31, 2012 were: Entrance fees ₹ 300; Membership Fees ₹ 3,000; Donation for Club Pavilion ₹ 10,000, Foodstuff sales ₹ 1,200; Salaries and Wages ₹ 1,200 Purchase of Foodstuff ₹ 800; Construction of Club Pavilion ₹ 11,000; General Expenses ₹ 600; Rent and Taxes ₹ 400; Bank Charges ₹ 160.

Cash in hand–Jan. 1st ₹ 200, Dec. 31st ₹ 350

Cash in Bank–Jan. 1st ₹ 400; Dec. 31st ₹ 5.

You are require to prepare Receipts and Payment Account for the period.

(4 x 4 =16 Marks)

MOCK TEST PAPER - 1

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

SUGGESTED ANSWERS/HINTS

1. (a) As per para 5 of AS 3 (Revised) "Cash Flow Statements",

Operating activities are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities.

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.

Thus, the classification will be done as:

Operating Activities: c, e,

Investing Activities: a, f,

Financing Activities: b, d.

(b)

	₹
Cost of construction till date	16,24,750
Add: Estimated future cost	8,00,250
Total estimated cost of construction	24,25,000

Percentage of completion till date to total estimated cost of construction

= (16,24,750 /24,25,000)$\times$100 = 67%

Proportion of total contract value recognised as revenue [as per AS 7 (Revised)] for the year ended 31st March, 2012 = Contract price x percentage of completion

= ₹ 21,25,000 x 67% = ₹ 14,23,750

Thus, ₹ 14,23,750 should be charged to revenue in the final accounts for the year ended 31st March, 2012.

(c) **In the books of Rang Ltd.**

Shyam Restaurant

		₹			₹
2011			2011		
Oct. 1	To Sales Account – Cash price	15,000	Oct. 1	By Bank – down payment	1,150
2012			2012		
Mar.31	To Interest A/c -on ₹ 13,850 @ 12% p.a. for six months	831	Mar.31	By Bank - First instalment	4,000
				By Balance c/d	10,681
		15,831			15,831
2012			2012		
Apr. 1	To Balance b/d	10,681	Sept. 30	By Goods Repossessed A/c –estimated value of T.V. set on repossession	12,000
Sept.30	To Interest A/c on ₹ 10,681 @ 12% p.a. for six months	641			
Sept.30	To Profit & Loss A/c – Profit on repossession of T.V. set	678			
		12,000			12,000

(d) As per AS 2 (Revised) "Valuation of Inventories", materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realizable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realizable value. Therefore, in this case, USA Ltd. will value the stock of raw material at ₹ 30,00,000 (10,000 kg. @ ₹ 300 per kg.).

2. (a) **In the Books of Max Ltd.**

Journal Entries

Particulars *01.04.2013*		*Dr. Amount* ₹	*Cr. Amount* ₹
Equity share capital A/c (₹ 100)	Dr.	15,00,000	
To Equity share capital A/c (₹ 10)			15,00,000
(Being sub-division of one share of ₹ 100			

each into 10 shares of ₹ 10 each)			
Equity share capital A/c	Dr.	7,50,000	
To Capital reduction A/c			7,50,000
(Being reduction of capital by 50%)			
Capital reduction A/c	Dr.	13,500	
To Bank A/c			13,500
(Being payment in cash of 10% of arrear of preference dividend)			
Bank A/c (800x ₹ 98)	Dr.	78,400	
To Own debentures A/c			76,800
To Capital reduction A/c			1,600
(Being profit on sale of own debentures transferred to capital reduction A/c)			
12% Debentures A/c	Dr.	1,20,000	
To Own debentures A/c			1,15,200
To Capital reduction A/c			4,800
(Being profit on cancellation of own debentures transferred to capital reduction A/c)			
12% Debentures A/c	Dr.	2,80,000	
Capital reduction A/c	Dr.	20,000	
To Machinery A/c			3,00,000
(Being machinery taken up by debentureholders for ₹ 2,80,000)			
Trade Payables A/c	Dr.	65,000	
Capital reduction A/c	Dr.	29,000	
To Trade receivables A/c			61,000
To Inventories A/c			33,000
(Being assets and liabilities revalued)			
Capital reduction A/c	Dr.	4,33,000	
To Goodwill A/c			20,000
To Discount on debentures issue A/c			2,000
To Profit and Loss A/c			4,11,000
(Being Goodwill, Discount on debentures & Profit & loss (Dr.) balance written off)			
Capital reduction A/c	Dr.	15,000	
To Bank A/c			15,000

(Being penalty paid for avoidance of capital commitments)			
Capital reduction A/c	Dr.	2,45,900	
To Capital reserve A/c			2,45,900
(Being the balance of capital reduction transferred to capital reserve account)			

(b) As per Revised Schedule VI, a liability shall be classified as current when it satisfies any of the following criteria:

(a) it is expected to be settled in the company's normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is due to be settled within twelve months after the reporting date; or

(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date.

In the given case, instalments due on 1.6.2013 and 1.12.2013 will be shown under the head 'other current liabilities' as per criteria (c). Therefore, in the balance sheet as on 31.3.2013, ₹ 8,00,000 will be shown under the heading 'Long term Borrowings' and ₹ 2,00,000 (₹ 1,00,000 x 2 instalments) will be shown under the heading 'Other Current Liabilities' as current maturities of loan from bank.

3. (a) On 1st July, it was agreed that the bills should be withdrawn. Among the four bills, the first due date is in respect of the second bill-the due date of which is 21st July. Therefore, 18.7.2012 will be taken as the base date.

Calculation of Average Due Date

Taking Base Date 21.07.2012

Date of Drawing	*Period*	*Due Date*	*Amount* ₹	*Number of Days from Base Date*	*Products* ₹
10.4.2012	4 months	13.08.2012	4,000	23	92,000
18.4.2012	3 months	21.07.2012	5,000	0	0
25.5.2012	6 months	28.11.2012	3,000	130	3,90,000
5.6.2012	3 months	8.09.2012	6,000	49	2,94,000
			18,000		7,76,000

$$\text{Average Due Date} = \text{21st July} + \frac{7,76,000}{18,000}$$

= 21.7.2007 + 43 days = 2.09.2012.

Since two new bills will be drawn, their due date will be:

First Bill- 1.7.2012 + 4 months = 1.11.2012; Second Bill- 1.7.2012+ 6 months = 1.1.2013.

(b) Reconciliation Statement of Sales Ledger Control Account

	₹	₹
Balance as per sales ledger Account		1,56,300
Less: Bad debt written off(wrongly posted)	3,695	
Tisco Ltd. (Contra)	770	4,465
Adjusted balance		1,51,835
List of balance		1,51,835

Reconciliation Statement of Purchase Ledger Control Account

	₹	₹
Balance as per Purchase ledger Account		1,70,690
Add: correction of M Ltd. invoice		13,500
		1,84,190
Less: overcastting of purchase day book total	1,260	
Bad debts wrongly posted	3,695	
Tisco Ltd.- contra	770	
Discount received not recorded in general ledger	19,370	25,095
Adjusted balance		1,59,095
List of balances		1,37,645
Correct T balance		900
Purchase from Q not posted		7,050
M Ltd. invoice of ₹ 15,000 recorded as 1,500		13,500
Adjusted list of balance		1,59,095

Journal Entries

			₹	₹
1	Purchase Ledger Control A/c To purchase A/c (Being the overcastting of purchase day book, now adjusted)	Dr.	1,260	 1,260

2	Purchase Ledger Control A/c To Discount received A/c (Being the discount received not posted in general ledger, now adjusted)	19,370	 19,370
3	Purchase Ledger Control A/c To Sales Ledger Control A/c (Being adjustment for bad debt written off)	3,695	 3,695
4	Purchase A/c To Purchase Ledger Control A/c (Being invoice of ₹ 15,000 wrongly recorded as ₹ 1,500, now rectified)	13,500	 13,500
5	Purchase Ledger Control A/c To Sales Ledger Control A/c (Being contra for Tisco Ltd. Account)	770	 770

4. (a) Trading Account for the year ended 31st March, 2012

To	Opening Stock	9,62, 200	By	Sales	52,00,000
To	Purchase	45,25,000	By	Closing Stock	13,27,200
To	Gross Profit	10,40,000			
		65,27,200			65,27,200

Rate of gross profit to sales = 10,40,000 /52,00,000 x 100 = 20%

Period from 1st April 2012 to 18th August 2012 has 140 days or 20 weeks.

Hence, amount of defalcation = ₹ 2,000 x 20 = ₹ 40,000

Memorandum Trading Account from 1st April, 2012 to 22nd January, 2013

To	Opening Stock		13,27,200	By	Sales	49,17,000
To	Purchase	34,82,700		By	Unrecorded Cash Sales	
	Less : Cost of goods used for advertising	1,00,000	33,82,700		- Defalcation	40,000
To	Gross Profit			By	Stock on 22nd January,	
	20% of recorded as well as unrecorded sales		9,91,400		2013- Balancing figure	7,44,300
			57,01,300			57,01,300

Stock in hand on date of fire = ₹ 7,44,300.

(b) Average sales per month = $\frac{7,20,000}{12 \text{ months}}$ = ₹ 60,000

Sales for the month of

		₹
January, 2013	(2 x ₹ 60,000)	1,20,000
February, 2013	(1 x ₹ 60,000)	60,000
May, 2013	($\frac{1}{4}$ x ₹ 60,000)	15,000
June, 2013	($\frac{1}{4}$ x ₹ 60,000)	15,000
July, 2013	($\frac{1}{4}$ x ₹ 60,000)	15,000
August, 2013	($\frac{1}{4}$ x ₹ 60,000)	15,000
October, 2013	(3 x ₹ 60,000)	1,80,000
November, 2013	(3 x ₹ 60,000)	1,80,000
Total sales for 8 months		6,00,000

Sales for the remaining 4 months = ₹ 7,20,000 – ₹ 6,00,000

= ₹ 1,20,000

Average sales for the remaining 4 months = $\frac{1,20,000}{4}$ = ₹ 30,000.

Sales for pre-incorporation period:

	₹
January, 2013	1,20,000
February, 2013	60,000
March, 2013	30,000
	2,10,000

Sales for post-incorporation period = ₹ 7,20,000 – ₹ 2,10,000 = ₹ 5,10,000

Sales ratio of pre-incorporation to post-incorporation period = 7: 17

5. **Revaluation Account**

Particulars	₹	Particulars	₹
To Stock	9,000	By Provision for doubtful debts	225
To Furniture & fixtures	1,650	By Land & buildings	22,500
To Provision for doubtful B/R	1,650	By Mr. X (Debtor)	975
To Unaccrued incomes	1,275		
To Workmen compensation claim	225		
To Profit on revaluation t/f to:			
P's capital A/c	7,425		
T's capital A/c	2,475		
	23,700		23,700

Capital Accounts of Partners

Particulars	P ₹	T ₹	O ₹	Particulars	P ₹	T ₹	O ₹
To P's Capital A/c	-	-	22,500	By Balance b/d	1,10,700	96,900	-
To T's Capital A/c	-	-	7,500	By Revaluation A/c	7,425	2,475	-
To Balance c/d	1,46,250	1,08,750	30,000	By P & L A/c	3,375	1,125	-
				By General Reserve	1,125	375	-
				By Contingency reserve	1,125	375	-
				By Bank A/c	-	-	60,000
				By O's Capital A/c	22,500	7,500	
	1,46,250	1,08,750	60,000		1,46,250	1,08,750	60,000
To T's Current A/c		48,750		By Balance b/d	1,46,250	1,08,750	30,000
To Balance c/d	1,80,000	60,000	60,000	By P's Current A/c	33,750	_	30,000
	1,80,000	1,08,750	60,000		1,80,000	1,08,750	60,000

Balance Sheet of M/s. P, T & O as on 31st March, 2013

Liabilities	₹	Assets	₹	₹
Sundry creditors	60,000	Cash at bank (5,250+60,000)		65,250
Employees' provident fund	6,150	Bills receivable	33,000	

Unaccrued incomes	1,275	*Less*: Provision	(1,650)	31,350
Workmen compensation claim	225	Debtors	25,500	
P's capital	1,80,000	*Less*: Provision	(1,275)	24,225
T's capital	60,000	Mr. X		975
O's capital	60,000	Stock (₹ 90,000 – ₹ 9,000)		81,000
T's current A/c	48,750	Furniture & fixtures (₹ 16,500 – ₹ 1,650)		14,850
		Land & buildings (₹ 1,12,500+ ₹ 22,500)		1,35,000
		P's current A/c		33,750
		O's current A/c		30,000
	4,16,400			4,16,400

Working Notes:

1. **Calculation of sacrificing ratio**

$$P = \frac{3}{4} - \frac{3}{5} = \frac{15-12}{20} = \frac{3}{20}$$

$$T = \frac{1}{4} - \frac{1}{5} = \frac{5-4}{20} = \frac{1}{20}$$

Therefore sacrificing ratio of P & T= 3:1

2. **Calculation of goodwill**

Total profits of last three completed years = ₹ 45,000 + ₹ 60,000 + ₹ 75,000

= ₹ 1,80,000

Average profits of last three completed years = ₹ 1,80,000/3 = ₹ 60,000

Goodwill of the firm = ₹ 60,000 ×2½ = ₹ 1,50,000

Incoming partner's share of Goodwill = ₹ 1,50,000 × 1/5= ₹ 30,000

Shared by P & T in 3:1 = ₹ 22,500 : ₹ 7,500

3. Total capital of the firm = ₹ 60,000 × 5 = 3,00,000

P's new capital = ₹ 3,00,000 x 3/5 = ₹ 1,80,000

T's new capital = ₹ 3,00,000 x 1/5 = ₹ 60,000

6. (a) **Statement of Affairs as on 31st March, 2012**

Liabilities	₹	*Assets*	₹
Capital (bal.fig.)	1,61,700	Machinery	1,10,000
Sundry creditors	2,750	Stock	10,450
		Debtors	550
		Cash at bank (W.N.1)	42,350
		Cash in hand	1,100
	1,64,450		1,64,450

(b) **Calculation of loss for 3 months (1.1.2012 to 31.3.2012)**

	₹
Capital as on 31.3.2012	1,61,700
Add: Drawings for 3 months	770
	1,62,470
Less: Capital as on 1.1.2012	(1,65,000)
Loss for 3 months	2,530

(c) **Statement of Affairs as on 31st March, 2013**

Liabilities	₹	*Assets*		₹
Capital	1,80,400	Machinery	1,10,000	
Sundry Creditors	1,650	*Add:* Additions	33,000	1,43,000
		Stock		15,950
		Debtors		1,100
		Cash at bank (W.N.2)		20,350
		Cash in hand		1,650
	1,82,050			1,82,050

(d) **Statement of Profit and Loss for the year ended 31.3.2013**

Particulars	₹
Capital as on 31.3.2013	1,80,400
Add: Drawings (₹ 385 x 12)	4,620
	1,85,020
Less: capital as on 31.3.2013	(1,61,700)
Net profit for the year ended 31.3.13	23,320

Working Notes:

	₹
1. Bank balance as on 31.3.2012	
Balance as on 1.1.2012	1,65,000
Less: Withdrawals during 1.1.2012 to 31.3.2012	(1,22,650)
Balance as on 31.3.2012	42,350
2. Bank Balance as on 31.3.2013:	
Balance as on 1.4.2012	42,350
Add: Deposits during the year	1,26,500
	1,68,850
Less: Withdrawals during the year	(1,48,500)
Bank Balance as on 31.3.2013	20,350

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

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

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

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

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

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

(b) 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. One should be well acquainted with the advantages & disadvantages of outsourcing.

Following are the advantages of outsourcing the accounting functions:

1. The organisation that outsources is able to save time to concentrate on the core area of business activity.
2. The organisation is able to utilise the expertise of the third party in undertaking the accounting work.
3. Storage and maintenance of the data is in the hands of professional people.
4. The organisation is not bothered about people leaving the organisation in key accounting positions.
5. The proposition often proves to be economically more sensible.

Following are the disadvantages of outsourcing the accounting functions:

1. *The data of the organisation is handed over to a third party:* This raises two issues, one of security and second of confidentiality. There have been instances of information leaking out of the third party data centers.
2. *Inadequate services provided*: The third party is unable to meet the standards desirable.
3. The *cost* may ultimately be higher than initially envisaged.
4. *Delay in obtaining services:* The third party service providers are catering to number of clients thereby processing as per priority basis.

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

(d) **Ascertainment of carrying cost**

	₹ in lakhs
Cost of acquisition	300
Less: Depreciation for 4 years (i.e from 1.1.2006 to 31.12.2009) @ 10% per annum (300 × 10% × 4 years)	(120)
Book value as on 1.1.2010	180

Add: Upward revaluation credited to revaluation reserve A/c	90
Revalued carrying cost as on 1.1.2010	270
Less: Depreciation at one–sixth of the revalued amount (Refer note)	(45)
Book value as on 1.1.2011	225
Less: Depreciation at one-sixth of the revalued amount	(45)
Balance to be carried forward as on 31.12.2011	180

Note:

As the depreciation rate is 10% on SLM, it is implied that the economic life of the asset is 10 years.

Since there is no change in the economic life of the machinery, the revalued amount should be written off over the remaining six year of economic life i.e ₹ 270/6 = ₹ 45 lakhs per year.

The book value of the asset on 1-1-2010 is ₹ 180 lakhs. Since it is revalued at ₹ 270 lakhs the difference of ₹ 90 lakhs is credited to revaluation reserve as per para 13 of AS 10 "Accounting for Fixed Assets".

Additional deprecation of ₹ 15 lakhs (₹ 45 lakhs – ₹ 30 lakhs) due to upward revaluation of the assets, may be charged to 'Revaluation Reserve A/c'.

(e) **Swaraj Club**

Receipts and Payments Accounts

for the year ended 31st December, 2012

	Receipts	₹		Payments	₹
To	Cash in hand b/d	200	By	Salaries and Wages	1,200
To	Cash with bank b/d	400	By	Purchase of Foodstuff	800
To	Entrance Fees	300	By	Club Pavilion (Expenditure on its construction)	11,000
To	Membership Fees	3,000			
To	Donation of Account of Club Pavilion	10,000	By	General Expenses	600
To	Sales of foodstuff	1,200	By	Rent and Taxes	400
			By	Bank Charges	160
			By	Cash in hand c/d	350
			By	Cash in bank c/d	590
		15,100			15,100

Test Series: February, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 2: BUSINESS LAWS, ETHICS AND COMMUNICATION

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

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

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

1. (a) State the nature of the contract in the following cases with reasons:

   (i) 'B' agrees to purchase the car from 'A' as per his proposal, subject to availability of valid Registration Certificate for the car.

   (ii) A threatened B to shoot if he does not lend him ₹ 2000 and B agreed to it.

   (2 ½ +2 ½ = 5 Marks)

   (b) When can a Public Company offer the new shares (further issue of shares) to persons other than the existing shareholders of the Company? Can these shares be offered to the Preference Shareholders? *(5 Marks)*

   (c) Explain the statement "Ethical behaviour creates a positive reputation that expands the opportunities for profit". *(5 Marks)*

   (d) Explain the statement 'Interpersonal communication is contextual'. *(5 Marks)*

2. (a) (i) A builder employed a labour on the daily wages for 2 months for the construction of the site on the payment of ₹ 300. Throw a light with respect to the Payment of Bonus Act, 1965 whether a labour is entitled for the bonus in the given instance. *(4 Marks)*

   (ii) Mr. X was an employee in a company for past 10 years and was assisting the director of a company in an assignment. In the mean time, he received a better opportunity from an abroad company. He put the resignation from service with prior notice and applied for the claim of gratuity. Company not accepted the resignation on the reason that assignment is incomplete and due to non acceptance of the resignation, the company also refused to pay the gratuity**.** Examine whether the contention of company is valid as per the Payment of Gratuity Act, 1972. *(4 Marks)*

   (b) In what manner the behavior of business persons towards the others in their workplace may generate ethical concerns? *(4 Marks)*

   (c) Explain how ethical communicators have a "well developed sense of social responsibility". *(4 Marks)*

3. (a) (i) P, a promoter of the company borrowed a loan on behalf of company and issued a cheque from the companies account to discharge its legal liability. P is neither a director nor a person-in-charge of the company. Subsequently the cheque was dishonoured and the compliant was lodged. State whether P is liable for an offence under section 138 of the Negotiable Instruments Act, 1881? *(5 Marks)*

(ii) Pick the correct answer:

(I) A negotiable instrument recognized by the usage or custom of trade:

(1) A promissory note

(2) A bill of exchange

(3) Hundi

(4) A cheque

(II) When the nature of the instrument is not clear, it is termed as:

(1) Inchoate

(2) Fictitious

(3) Ambiguous

(4) Escrow

(III) Endorsement which restricts the right of further negotiation of the instrument is-

(1) Special endorsement

(2) General endorsement

(3) Facultative endorsement

(4) Restrictive endorsement *(1 x 3 = 3 Marks)*

(b) State the nature of rights that are protected by the Central Consumer Protection Council. *(4 Marks)*

(c) What is meant by ‘Environmental ethics’? How does its non-adoption lead to 3 Ps Viz., Polluter, Pays and Principles? Explain. *(4 Marks)*

4. (a) What are the requirements as to the issue of the Prospectus? Under what conditions the issuing of prospectus is not necessary under the Companies Act, 1956. *(8 Marks)*

(b) State the various ethical issues that are common at the work place in an industrial organisation. *(4 Marks)*

(c) State the relevance of active listening in the business communication skill. *(4 Marks)*

5. (a) State the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 regulating the quantum of contribution to be made by the employer and employee to the provident fund. Is it possible for an employee to

increase the amount of his contribution to the provident fund more than the minimum contribution as statutorily prescribed? *(8 Marks)*

(b) State the manner in which a person may acquire membership of a public company. *(4 Marks)*

(c) Mr. P purchased the goods on the credit from Mr. S(supplier). 2 months passed and still the payment is pending. Draft a letter requesting for the payment of overdue amount. *(4 Marks)*

6. (a) (I) State whether the following statement is correct/incorrect with reasons:

(i) The Statutory meeting is required to be hold by all companies.

(ii) A promissory note given out of a wagering contract is enforceable.

(iii) Hundis are governed by the Negotiable Instruments Act, 1881.

(iv) Employees of a registered company converted from a partnership, is entitled to gratuity. *(4 x 1 = 4 Marks)*

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

(b) "Conservation looks primarily to the future". Explain. *(4 Marks)*

(c) Draft the Performa of a bond for a loan repayable in instalments. *(4 Marks)*

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

(a) Differentiate between the following:

(i) Cheque and Bill of exchange,

(ii) General Lien and Particular Lien *(2 x 2 = 4 Marks)*

(b) Who are entitled to get notice for the general meeting called by a Public Limited Company registered under the Companies Act, 1956? Does the non-receipt of a notice of the meeting by any one entitled to such notice invalidate the meeting and the resolution passed thereat? What would be your answer in case the omission to give notice to a member is only accidental omission? *(4 Marks)*

(c) State the procedure for inspection of Minutes Book of General Meetings of a company, by the members. *(4 Marks)*

(d) What safeguards may be created by a business enterprise in the work environment? *(4 Marks)*

(e) Draft a circular for employees insisting on punctuality. *(4 Marks)*

Mock Test Paper – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 2: BUSINESS LAWS, ETHICS AND COMMUNICATION

SUGGESTED ANSWERS/HINTS

1. (a) (i) As per the provision give under section 7 of the Indian Contract Act, 1872 acceptance is valid only when it is absolute and unqualified . Accordingly, in the given case where 'B' agrees to purchase the car from 'A' as per his proposal, depending on availability of valid Registration Certificate for the car, the acceptance given to the proposal of 'A' is in place though the offer contained no mention of R.C. book. This is because expecting a valid title for the car is not a condition. Therefore the acceptance given by B, in this case is unconditional. Thus agreement is valid.

(ii) The word 'Consent' generally means 'knowledge and approval' of the parties concerned. Whereas the Indian Contract Act, 1872 defines the term 'consent' as meeting of the minds on the same thing in the same sense viz *consensus ad idem*. Further such consent must be free. Consent would be considered as free consent if it is not vitiated by coercion, undue influence, fraud, misrepresentation or mistake. Wherever the consent of any party is not free, the contract is voidable at the option of that party.

Accordingly in the case, A threatened to shoot B if he (B) does not lend him ` 2000 and B agreed to it. Here the agreement is entered into under coercion and hence voidable at the option of B.

(b) Issue of Further Shares: Section 81 of the Companies Act, 1956 provides that if, at any time after the expiry of 2 years from the formation of the company or after the expiry of one year from the first allotment of shares, whichever is earlier, it is proposed to increase the subscribed capital by allotment of further shares, it should be offered to the existing equity shareholders of the company in proportion to the capital paid up on those shares.

The new shares of a company may be offered to outsiders or any persons (including the equity shareholders) if-

(i) a special resolution to that effect is passed by the company.

(ii) an ordinary resolution is passed and the approval of the Central Government is obtained. The Central Government will accord its approval if it is satisfied that the proposal is most beneficial to the company.

(iii) if any shareholder to whom the shares are offered declines to accept the shares. In such a case the Board of Directors may dispose of the shares in such a manner as they think most beneficial to the company.

(iv) if the new shares are issued within 2 years from the formation of the company or 1 year of the allotment made for the first time.

Preference Shareholders - whether (Further Issue of Capital) be offered to: From the wordings of Section 81, it is quite clear that these shares can be issued only to equity shareholders, unless procedure as stated above has been adopted for issue of these shares to outsiders, etc. Therefore, in general these shares cannot be offered to preference Shareholders.

(c) It is now a well accepted fact that ethical behaviour creates a positive reputation that expands the opportunities for profit. An organisation is not only its buildings, assets, capital or even profit. It is living and creative, evolving over time and having a vision about its future role in society, nation and the world. In the broad sense ethics in business is simply the application of everyday moral or ethical norms to business. Being ethical in business requires acting with an awareness of how the products and services of an organization, and the actions of its employees, can affect its stakeholders and society as a whole and developing codes of conduct for doing business in an ethical manner. Amongst the thinkers of modern times, an invaluable contribution to practising business ethically is provided by Mahatma Gandhi, the father of our nation. He sought to unite mankind in common interest of justice and establishment of a moral order in world-society. He advised the citizens to observe truthfulness in business and reminded them of their responsibility which was greater since their conduct would be seen as a reflection of their country.

(d) The statement 'Interpersonal communication is contextual' which means that any communication does not happen in isolation. There are following context of communications:

psychological context, which is who the communicators are and what they bring to the interaction. Their needs, desires, values, personality, etc., all form the psychological context.

Relational context, which concerns reactions to each other.

Situational context deals with the "psycho-social-where" one is communicating. For example, an interaction that takes place in a classroom will be very different from one that takes place in a Board room.

Environmental context deals with the "physical -where" one is communicating. Furniture, location, noise level, temperature, season, time of day, all are examples of factors in the environmental context.

Cultural context includes all the learned behaviours and rules that affect the interaction. If you come from a culture (foreign or within your own country) where it is considered rude to make long, direct eye contact, you will out of politeness avoid eye contact. If the other person comes from a culture where long, direct eye contact signals trustworthiness, then we have in the cultural context a basis for misunderstanding.

2. **(a)** **(i)** As per the Payment of Bonus Act, 1965, Every employee of an establishment covered under the Act is entitled to bonus from his employer in an accounting year provided he has worked in that establishment-(i) for not less than thirty working days in that year, (ii) on a salary or wage not exceeding ₹ 10,000 per mensem. [Section 2(13) read with Section 8].

The Act does not make any distinction as to whether an employee is daily wager, temporary, permanent, weekly paid, monthly paid etc. the only precondition is that he should have worked in the establishment for not less than 30 working days in an accounting year.*[Himachal Pradesh State Electricity Board and Others Vs Krishan Dutt 2010 (127) FLR 577(H.P.).]*

According to the given facts, labour who was on daily wages, have fulfilled the requirements of the above stated provisions. He has worked for the 2 months i.e., more than 30 days and on the daily wages of ₹ 300 which amounts the wages (₹ 300 x 30 days= ₹ 9000 p.m) not exceeding ₹ 10,000 p.m.

Thus it can be concluded that labour is entitled for the payment of bonus.

(ii) As per 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 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.

According to the above provision, the payability of Gratuity to the employee is his right as well as the obligation of the employer. An employee resigning from service is also entitled to gratuity; *[Texmaco Ltd. Vs Sri Ram Dhan 1992 LLR 369(Del)]* and non-acceptance of the resignation is no hurdle in the way of an employee to claim gratuity *[Mettur Spinning Mills Vs Deputy Commissioner of Labour, (1983) II LLJ 188]*.

Thus in the given case, the contention of the company is not valid. The non-acceptance of the resignation cannot the deprive Mr. X from claiming the gratuity.

(b) **Business Relationships:** The behaviour of businesspersons toward customers, suppliers, and others in their workplace may also generate ethical concerns. Ethical behaviour within a business involves keeping company secrets, meeting obligations and responsibilities, and avoiding undue pressure that may force others to act unethically.

Managers, in particular, because of the authority of their position, have the opportunity to influence employees' actions. For example, a manager can influence employees to use pirated computer software to save costs. The use of illegal software puts the employee and the company at legal risk, but employees may feel pressured to do so by their superior's authority. Customer's need should be considered most when it comes to ethical business practices. In the long run, a company will reap great profits from a customer base that feels it is being treated fairly and truthfully. Organizational pressures may encourage a person to engage in activities that he or she might otherwise view as unethical, such as invading others' privacy or stealing a competitor's secrets.

(c) Following is an ethical communication which an ethical communicators may include in communication with others:

- all relevant information,
- true in every sense and is not deceptive in any way.
- accurate and sincere. Avoids language that manipulates,, discriminates or exaggerates.
- not hide negative information behind an optimistic attitude .
- not state opinions as facts,
- portrays graphic data fairly.

In a nutshell, ethical communicators have a "well developed sense of social responsibility".

3. (a) (i) According to Section 138 of the Negotiable Instruments Act, 1881 where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from/out of that account for discharging any debt or liability, and if it is dishonoured by banker on sufficient grounds, such person shall be deemed to have committed an offence and shall be liable. However, in this case, P is neither a director nor a person-in-charge of the company and is not connected with the day-to-day affairs of the company and had neither opened nor is operating the bank account of the company. Further, the cheque, which was dishonoured, was also not drawn on an account maintained by him but was drawn on an account maintained by the company. Therefore, he has not committed an offence under section 138 of the Negotiable Instruments Act, 1881.

(ii) (I) (3)

(II) (3)

(III) (4)

(b) Central Consumer Protection Council: The objects of the Central Council shall be to promote and protect the rights of the consumers such as,-

(i) the right to be protected against the marketing of goods and services which are hazardous to life and property;

(ii) the right to be informed about the quality, quantity, potency, purity, standard and price of goods(or services, as the case may be) so as to protect the consumer against unfair trade practices;

(iii) the right to be assured, wherever possible, access to a variety of goods, and services at competitive prices;

(iv) the right to be heard and to be assured that consumer's interest will receive due consideration at appropriate terms;

(v) the right to seek redressal against unfair trade practices (or restrictive trade practices) or unscrupulous exploitation of consumers; and

(vi) the right to consumer education.

(c) Ecological ethics is based on the idea that the environment should be protected not only for the sake of human beings but also for its own sake. The issue of environmental ethics goes beyond the problems relating to protection of environment or nature in terms of pollution, resource utilization or waste disposal.

Business and Industry are closely linked with environment and resource utilization. Production process and strategy for eco-friendly technologies throughout the product life cycle and minimization of waste play major role in protecting the environment and conservation of resources. Business, Industry and multinational corporations have to recognize environmental management as the priority area and a key determinant to sustainable development. Sound management of wastes is among the major environmental issues for maintaining the quality of Earth's environment and achieving sustainable development.

If the environmental costs are properly reflected in the prices paid for goods and services then companies and ultimately the consumer would adjust market behaviour in a way that would reduce damage to environment, pollution and waste production. Price signal will also influence behaviour to avoid exploitation or excessive utilization of natural resources. Such measures would facilitate the approach of "Polluter Pays Principle". Removing subsidies that encourage environmental damage is another measure.

4. (a) Comprehensive rules and regulations have been incorporated into the Companies Act, 1956 in respect of this basic document which is the only source for the investors to ascertain the soundness or otherwise of the company. Since the prospectus is intended to save the investing public from victimisation, the

Legislature has aimed at securing the fullest disclosure of all material and essential particulars and laying the same before all the prospective buyers of shares. Briefly the rules and regulations are as follows:

(i) **Dating of prospectus -** According to Section 55, every prospectus must be dated. This requirement is designed to ensure a prima facie evidence of the date of its publication. However, this evidence may be rebutted by a contrary evidence.

(ii) **Registration of prospectus -** It is absolutely necessary for the company to deliver to the Registrar a copy of every prospectus for registration. It must be made on or before the prospectus is published. But the prospectus must not be issued more than 90 days after the date on which a copy of it is delivered to the Registrar for Registration.

(iii) **Approval of prospectus by various agencies**: The draft prospectus has to be approved by various agencies before it is filed with the ROC of the concerned State.

(iv) **The lead financial institution underwriting the issue, if applicable**: The draft prospectus is vetted by SEBI to ensure adequacy of disclosures. However, vetting by SEBI does not amount to approval of prospectus. SEBI does not take any responsibility for the correctness of the statements made or opinions expressed in the prospectus.

Non-issuing of Prospectus:

As per Section 56 of the Companies Act, 1956 the issue of prospectus is not necessary in the following cases-

(1) Where shares or debentures are offered to existing holders of shares or debentures.

(2) When the issue relates to shares or debentures uniform in all respects, with shares or debentures previously issued and dealt in or quoted in a recognized stock exchange.

(3) Where a person is bona-fide invited to enter into an underwriting agreement.

(4) Where shares are not offered to the public.

(b) Some common ethical issues faced by an individual at the workplace are:

(i) Relationship with suppliers and business partners:

- Bribery and immoral entertainment
- Discrimination between suppliers
- Dishonesty in making and keeping contracts

(ii) Relationship with customers:

- Unfair pricing
- Cheating customers
- Dishonest advertising
- Research Confidentiality

(iii) Relationship with employees:

- Discrimination in hiring and treatment of employees,
- Lack of good behaviour with employees

(iv) Management of resources:

- Misuse of organizational funds
- Tax evasion

(c) **Active Listening**: Most of us assume that listening is a natural trait, but practically very few of us listen properly. What we regularly do is-"we hear but do not listen". Hearing is through ears and listening is by mind. Listening happens when we understand and message as intended by sender. Many managers are so used to helping people solve problems that their first cause of action is transforming solutions and giving advice instead of listening with full attention directed towards understanding what the co-worker or staff member needs.

Therefore, every employer and worker needs a listening ear. If one does not learn how to listen, a great deal of what people are trying to tell you would be missed. In addition, appropriate response would not be possible. Active listening is important for several reasons.

(i) It aids the organization in carrying out its missions.

(ii) It helps individuals to advance in their careers.

(iii) It provides information that helps them to learn about important happenings in the organization, as well as assisting them in doing their own jobs well.

(iv) It also helps in building strong personal relationships.

5. **(a)** **Contribution to Provident Fund under the EPF and Miscellaneous Provisions Act, 1952:** Section 6 of the EPF and MP Act, 1952 regulates contribution to Provident Fund Scheme established under the Act. The employer's contribution shall be 10% of the basic wages, dearness allowance and retaining allowance, if any. The employee's contribution shall be equal to the contribution payable by the employer in respect of him.

Dearness allowance includes cash value of any food concession allowed to the employees. Retaining allowance means the sum paid for retaining the service, when the factory is not working. The Central Government may by notification make the employer's contribution equal to 12% for certain establishments class of establishments.

The above rule will prevail irrespective of whether the employer employs the person directly or through a contractor.

An employee can at his will voluntarily contribute, beyond 10%. But the employer shall not be under an obligation to pay any contribution over and above his contribution payable under section 6 of the said Act.

(b) The membership of a company may be acquired in the following ways:

1. **By subscribing to memorandum (Section 41):** This section provides that the subscribers of the memorandum of association shall be deemed to have agreed to become the members of the company and on its registration shall be entered as members in the register of members.
2. **By allotment**: A person may become a shareholder by agreeing to take shares in the company by allotment.
3. **By transfer**: Section 41 says that every subscribers to the memorandum of a company and every other person who agrees in writing to become a member of the company and whose name is entered in its register of members. Thus it requires two thing a) an agreement in writing to become a member and b) an entry in the register.
4. **By transmission**: Here a person may become a shareholder by transmission of shares through death, lunacy or insolvency.
5. **By estoppel**: This arises when a person holds himself out as a member or knowingly allows his name to remain on the register when he has actually parted with his shares. In the event of winding up he will be liable like other genuine members as a contributory *(Hansraj A. Ashtana).* However, he may escape liquidity by applying for removal of his name under Section 155.

(c) Letter of request for payment of overdue amount for the goods supplied

Dated:---------

To,

Mr. P,

----------------(Address)

Subject: Payment for the goods supplied on credit

This is with reference to our dealing made on ----------with respect to the purchase of goods on credit on the payment of -------------(amount). This is to remind you that above stated payment is overdue. We request you to settle the payment at your earliest.

We look forward to your response.

Yours sincerely,

S/d

(Supplier)

6. (a) (I) (i) Incorrect. According to Section 165 of the Companies Act, 156 only Public Ltd. Company with a share capital must hold Statutory Meeting. Private Companies and Government Companies are not required to hold such a Meeting.

(ii) Incorrect. As a wagering contract is *void ab initio*, it is but automatic that a promissory note given out of a wagering contract is not enforceable by way of a suit. A promissory note of this character is one without consideration and hence is null and void.

(iii) Correct: Bills of exchange drawn up in the vernacular are generally known as Hundis. The Negotiable Instruments Act ordinarily is not applicable to Hundis but, the title of the Act conveys the idea that the Act is a comprehensive enactment relating to all kinds of negotiable instruments whether negotiable by law, or by usage or custom. So, the parties to the Hundis may agree to be governed by the Negotiable Instruments Act,1881.

(iv) Correct: Wherever a partnership is converted into a registered company, there the employees are entitled to gratuity on the basis of length of service under both the establishments taken together *[Bommidala Bros. v. Authority, the Payment of Gratuity Act(1989) 1 cur LR 595 AP]*

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

(b) Conservation refers to the saving or rationing of natural resources for later uses. Conservation, therefore, looks primarily to the future: to the need to limit consumption now to have resources available for tomorrow. In a sense, pollution control is a form of conservation. Pollution "consumes" pure air and water, and pollution control "conserves" them for the future. Consequently, our concern over the depletion of resources is primarily a concern for future generations. Conservation, therefore, is the only way of ensuring a supply for tomorrow's generations.

(c) This Bond is made on the -----------day of ----------between ----------(details of party to be called as debtor) and ----------(details of the other party to be called as creditor).

Whereas the debtor has this day borrowed a sum of Rupees-------------(`………)only from the creditor with the condition to repay the same with interest at the rate of ----------percent per annum by monthly instalments. The debtor has agreed to pay the same.

Whereas in case of default in the payment of any consecutive instalments, the penalty shall be levied with double rate of interest on the remaining unpaid amount.

Signature of debtor

Signature of creditor

Witnesses:

1…………….

2…………….

7. (a) (i) Difference between Cheque and Bill of Exchange:

(1) In the case of a cheque the drawee- *i.e.,* the person on whom the bill is drawn-must always be banker whereas in the case of a bill of exchange the drawee may be any person.

(2) No days of grace are allowed in the case of a cheque, and a cheque is as a rule, payable immediately on demand, whereas three days' grace is allowed in the case of a bill which is not payable on demand.

(3) In the case of dishonour of a cheque, bank only gives the reason in writing but there is no system of Noting or Protest ,whereas in the case of a bill, there can be Noting and Protest to prove that the bill has been dishonoured.

(4) A cheque is always payable on demand, whereas a bill which is other than a cheque may be either a time bill or it may be payable on demand.

(5) Cheques do not require to be stamped in India, whereas bills must be stamped according to the law. In England and several other countries, cheques also are required to be stamped.

(6) A cheque may be crossed, whereas a bill cannot be crossed.

(ii) **Difference between the General Lien and the Particular Lien:**

General lien	Particular lien
It is a right to detain/retain any goods of the bailor for general balance of account outstanding	It is a right exercisable only on such goods in respect of which charges are due.
A general lien is not automatic but is recognized through on agreement. It is exercised by the bailee only by name	It is automatic
It can be exercised against goods even without involvement of labour or skill.	It comes into play only when some labour or skill is involved
Bankers, factors, wharfingers, policy brokers etc. are entitled to general lien	Bailee, finder of goods, pledgee, unpaid seller, agent, partner etc are entitled to particular lien

(b) Serving to notice of meeting: Notice of meeting shall be given -

(i) to every member of the company;

(ii) to the persons entitled to a share in consequence of the death or insolvency of a member;

(iii) to a auditor or auditors [Section 172(2)] and,

The company cannot take notice of the beneficial owners of shares who are, therefore, not entitled to notice, where, however, anyone is legally entitled to represent the members, such representative is entitled to receive the notice.

The private company, which is not, a subsidiary of a public company may prescribe, by its articles, persons to whom the notice should be given. The non-receipt of notice or accidental omission go given notice to any member shall not invalidate the proceedings in the meeting [Section 172(3)]. However, omission to serve notice of meeting on a member on the mistaken ground that he is not a shareholder cannot be said to be an accidental omission. Accidental omission means that the omission must be not only designed but also not deliberate. *[Maharaja Export Vs. Apparels Exports Promotion Council (1986)].*

(c) Inspection of Minutes Books of General Meetings: Following are the provisions relating to the procedure for inspection of minutes books of general meetings of a company by the members:

(1) The books containing the Minutes of the proceedings of any general meeting of a company shall-

(a) be kept at the registered office of the company, and

(b) be open, during business hours, to the inspection of any member without charge, subject to such reasonable restrictions as the company may, by its articles or in general meeting impose, so however that not less than two hours in each day are allowed for inspection.

(2) Any member shall be entitled to be furnished, within seven days after he has made a requisition in that behalf to the company, with a copy of any minutes referred to in subsection (1), on payment of such sum as may be prescribed for every one hundred words or fractional part thereof required to be copied.

(3) If any inspection required under sub-section (1) is refused, or if any copy required under sub-section (2) is not furnished within the time specified therein, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to five thousand rupees in respect of each offence.

(4) In the case of any such refusal or default, the Central Government may, by order, compel on immediate inspection of the Minute books or direct that the copy required shall forthwith be sent to the person requiring it.

(d) The following safeguards may be created by a business enterprise in the work environment:

(i) The employing organisations' systems or corporate oversight or other oversight structures.

(ii) The employing organisation's ethics and conduct programmes.

(iii) Recruitment procedures in the employing organisation emphasizing the importance of employing high caliber competent staff

(iv) Strong internal controls

(v) Appropriate disciplinary process

(vi) Leadership that stresses the importance of ethical behaviour and expectation that employees will act in an ethical manner.

(vii) Policies and procedures to implement and monitor the quality of employee performance.

(viii) Timely communication of the employing organisation's policies and procedures, including any changes to them, to all employees and appropriate training and education on such policies and procedures.

(e) Circular for employees

Jaipee Electronics Ltd.

Civil Lines, Kanpur.

Circular No: Date…………

To all employees,

Recent surprise checks have revealed that there is considerable late coming and in some cases, even the standard instructions for ensuring punctual attendance are not followed. All employees are requested to strictly adhere to the arrival, departure and lunch timing of the office. Tendency to move around in the corridors and canteen would also be viewed seriously.

Cooperation of all employees is solicited.

Sd/-

Manager – H.R

Test Series: February, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – I : COST ACCOUNTING

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

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

Working notes should form part of the answer.

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

1. Answer the followings:

(a) Aditya Ltd has calculated a predetermined overhead rate of ₹ 22 per machine hour for its Quality Check (QC) department. This rate has been calculated for the budgeted level of activity and is considered as appropriate for absorbing overheads. The following overhead expenditures at various activity levels had been estimated.

Total overheads	Number of machine hours
₹ 3,38,875	14,500
₹ 3,47,625	15,500
₹ 3,56,375	16,500

You are required to:

(i) Calculate the variable overhead absorption rate per machine hour.

(ii) Calculate the estimated total fixed overheads.

(iii) Calculate the budgeted level of activity in machine hours.

(iv) Calculate the amount of under/over absorption of overheads if the actual machine hours were 14,970 and actual overheads were ₹ 3,22,000.

(v) State the arguments for and against using departmental absorption rates as opposed to a single or blanket factory wide rate.

(b) An automobile company manufactures commercial vehicles which require engine filter E-12 DX. The following particulars are collected for the year 2013-14:

(i) Annual demand of E-12 DX 12,000 units

(ii) Cost of placing an order ₹1,200 per order

(iii) Cost per unit of E-12 DX is ₹1,740/-

(iv) Carrying cost p.a. 12%

The company has been offered a quantity discount of 5 % on the purchase of E-12 DX, provided the order size is 6,000 units at a time.

Required to:

(i) Compute the economic order quantity (EOQ)

(ii) Advise whether the quantity discount offer can be accepted. *(2 x 5 =10 Marks)*

2. Rounak Infratech Ltd. prepares its account on 31st December each year. It commenced a contract on 1st April, 2013. The costing records concerning the said contract reveal the following information on 31st December, 2013.

	(₹)
Material charged to site	2,58,100
Labour engaged	5,60,500
Foremen's salary	79,300

Plant costing ₹2,60,000 had been on site for 146 days. Working, life of the plant is estimated at 7 years and its final scrap value at ₹15,000. A supervisor, who is paid ₹4,000 per month, has devoted approximately three-fourths of his time to this contract. The administrative and other expenses amount to ₹1,40,000. Materials at site on 31st December, 2013 cost ₹25,400. Some of the materials costing ₹4,500 was found unsuitable and was sold for ₹4,000 and a part of the plant (whose written down value on 31.12.2013 was ₹5,500) was sold at a profit of ₹ 1,000 as it was unsuited to the contract.

The contract price was ₹22,00,000 but it was accepted by the contractor for ₹20,00,000. On 31st December, 2013 two-thirds of the contract was completed. Architect's certificate had been issued covering 50% of the contract price and ₹7,50,000 had so far been paid on account.

You are required to prepare Contract Account and state how much profit or loss should be taken into account for the year ended 31st December, 2013. Depreciation is charged on time basis. Also prepare the Contractee account and show how these accounts would appear in the balance sheet as on 31st December, 2013. *(8 Marks)*

3. Navya is working by employing 10 skilled workers. It is considering the introduction of some incentive scheme – either Halsey scheme (with 50% bonus) or Rowan scheme of wage payment for increasing the labour productivity to cope with the increased demand for the product by 25%. She feels that, if the proposed incentive scheme could bring about an average 20% increase over the present earnings of the workers, it would act as sufficient incentive for them to produce more and she has accordingly given this assurance to the workers.

As a result of this assurance, the increase in productivity has been observed as revealed by the following figures for the current month:

Hourly rate of wages (guaranteed)	₹ 2.00
Average time for producing 1 piece by one worker at the previous performance (this may be taken as time allowed)	2 hours
Number of working days in the month	25
Number of working hours per day for each worker	8
Actual production during the month	1,250 units

Required:

(1) Calculate effective rate of earnings per hour under Halsey scheme and Rowan scheme.

(2) Calculate the savings of Navya in terms of direct labour cost per piece under the above schemes.

(3) Advise Navya about the selection of the scheme to fulfill her assurance. *(8 Marks)*

4. From the particulars given below, compute: Material Price Variance, Material Usage Variance, Labour Rate Variance, Idle time Variance and Labour Efficiency Variance with full working details:

   1 ton of material input yields a standard output of 1,00,000 units.

   The standard price of material is ₹ 20 per kg.

   Number of employees engaged are 200.

   The standard wage rate per employee per day is ₹ 6.

   The standard daily output per employee is 100 units.

   The actual quantity of material used is 10 tons and the actual price paid is ₹ 21 per kg.

   Actual output obtained is 9,00,000 units.

   Actual number of days worked is 50 and actual rate of wages paid is ₹ 6.50 per day.

   Idle time paid for and included in above time is ½ day. *(8 Marks)*

5. Distinguish between:

   (a) Cost Allocation and Cost Absorption.

   (b) Fixed Budget and Flexible Budget *(4 x 2 = 8 Marks)*

6. Solitaire Ltd. purchased 10,000 kgs. of raw material @ ₹ 17 per kg and issued it for further processing in purifying department. In purifying department wages paid amounted to ₹ 11,000 and overhead was applied @ 150% of the labour cost. Indirect materials

costing ₹ 2,600 were introduced into the process. The normal yield from the process is 90%. 9,100 kgs of output was obtained from this purifying process. Any difference in weight between the input of raw material and output of purified material can be sold @ ₹ 2.10 per kg.

The process is operated under a licence for which royalty @ ` 0.35 per kg. of purified material produced is paid.

You are required to prepare:

(i) Purifying process Account

(ii) Normal loss Account

(iii) Abnormal loss/ gain Account

(iv) Royalty Payable Account. *(8 Marks)*

7. (a) Distinguish between Spoilage and Defectives in a manufacturing company.

(b) State the advantages of Integrated Accounting System. *(4 x 2 =8 Marks)*

Test Series: February, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 3B: FINANCIAL MANAGEMENT

All questions are compulsory.

Working notes should form part of the answer.

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

1. Answer the question, supporting the same with reasoning:

   "Determining the appropriate level of working capital for a firm requires":

   (i) Evaluating the risks associated with various levels of fixed assets and the types of debt used to finance these assets.

   (ii) Changing the capital structure and dividend policy of the firm.

   (iii) Maintaining short-term debt at the lowest possible level because it is generally more expensive than long-term debt.

   (iv) Offsetting the benefit of current assets and current liabilities against the probability of technical insolvency. *(4 × 1 = 4 Marks)*

2. (a) A machine purchased six years back for ₹ 1,50,000 has been depreciated to a book value of ₹ 90,000. It originally had a projected life of fifteen years and zero salvage value. A new machine will cost ₹ 2,50,000 and result in a reduced operating cost of ₹ 30,000 per year for the next nine years. The older machine could be sold for ₹ 50,000. The new machine shall also be depreciated on a straight-line method on nine-year life with salvage value of ₹ 25,000. The company's tax rate is 50% and cost of capital is 10%.

   Determine whether the old machine should be replaced.

   Given: Present Value of Re. 1 at 10% on 9th year = 0.424; and Present Value of an annuity of Re. 1 at 10% for 8 years = 5.335.

   (b) Gamma Limited provides the following information for your consideration:

	₹
Cost (per unit):	
Raw materials	52.0
Direct labour	19.5
Overheads	39.0

Total cost (per unit)	110.5
Profit	19.5
Selling price	130.0

Average raw material in stock is one month; average material in process is half a month. Credit allowed by suppliers is one month; credit allowed to debtors is two months. Time lag in payment of wages is one and a half weeks and Overheads is one month. One-fourth of sales are on cash basis. Cash balance is expected to be Rs 1,20,000.

You are required to prepare a statement showing the working capital needed to finance a level of activity of 70,000 units of output. You may assume that production is carried on evenly, throughout the year and wages and overheads accrue similarly. *(8 + 8= 16 Marks)*

3. (a) The following current data are available concerning Alpha Limited:

Share issued	10,000
Market price per share	₹ 20
Interest rate	12%
Tax Rate	46%
Expected EBIT	₹ 15,000

The company requires an additional ₹ 50,000 for the coming year.

You are required to determine:

(i) Which financing option (debt or equity issue) will give higher EPS for the expected EBIT?

(ii) What is indifference level of EBIT for the two alternatives?

(iii) What is EPS for that EBIT?

(b) The following data relates to Beta Limited:

	₹
Sales	2,00,000
Less: Variable Expenses (30%)	60,000
Contribution	1,40,000
Fixed operating expenses	1,00,000
EBIT	40,000
Less: Interest	5,000
EBT	35,000

(i) Using the concept of combined leverage, by what percentage will EBT increase if sales increases by 6 percent.

(ii) Using the concept of operating leverage by what percentage will EBIT increase if there is 10 per cent increase in sales?

(iii) Using the concept of financial leverage by what percentage EBT increase if EBIT increases by 6 per cent? *(9 + 9 = 18 Marks)*

4. Answer the following:

(a) Zeta Limited is now extending 1 month's credit to its selected customers. It sells its products at ₹ 100 each, and has an annual sales volume of 60,000 units. At current level of production, which matches with sales, the product has a total cost of ₹ 90 per unit and a variable cost of ₹ 80 per unit. The company is considering a plan to grant more liberal terms by extending the duration of credit from 1 month to 2 months and expects the sales to the customer group to go up by 25 per cent. In the background of a normal expectation of a 20 per cent return on investment, will this relaxation in credit standard justify itself?

(b) Critically discuss the role of IRR as an investment appraisal technique.

(8+4 = 12 Marks)

Test Series: February, 2014

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – I : COST ACCOUNTING

Suggested Answers/ Hints

1. (a) (i) Variable overhead absorption rate: $= \dfrac{\text{Difference in Total Overheads}}{\text{Difference in levels in terms of machine hours}}$

$= \dfrac{₹\,3,47,625 - ₹\,3,38,875}{15,500 \text{ hours} - 14,500 \text{ hours}}$ = ₹ 8.75 per machine hour.

(ii) Calculation of Total fixed overheads:

	(₹)
Total overheads at 14,500 hours	3,38,875
Variable overheads = ₹ 8.75 × 14,500	1,26,875
Total fixed overheads	2,12,000

(iii) Calculation of Budgeted level of activity in machine hours:

Let budgeted level of activity = X

Then, $\dfrac{(₹\,8.75\,X + ₹\,2,12,000)}{X}$ = ₹ 22

8.75X + ₹ 2,12,000 = 22X

13.25X = 2,12,000

X =16,000

Thus, budgeted level of activity = 16,000 machine hours.

(iv) Calculation of Under / Over absorption of overheads:

	(₹)
Actual overheads	3,22,000
Absorbed overheads = 14,970 hours × ₹ 22 per hour	3,29,340
Over-absorption (3,29,340 – 3,22,000)	7,340

(v) Departmental absorption rates provide costs which are more precise than those provided by the use of blanket absorption rates. Departmental absorption rates facilitate variance analysis and cost control. The application of these rates make the task of stock and work-in-process (WIP) valuation easier and more precise. However the setting up and monitoring of these rates can be time consuming and expensive.

(b) (i) Calculation of Economic Order Quantity

$$\text{EOQ} = \sqrt{\frac{2 \times \text{Annual Demand} \times \text{Ordering Cost}}{\text{Carrying cost per unit per annum}}}$$

$$= \sqrt{\frac{2 \times 12{,}000 \text{ units} \times ₹1{,}200}{₹1{,}740 \times 0.12}} = 371 \text{ units (Approx)}$$

(ii) Evaluation of Profitability of Different Options of Order Quantity

(a) When EOQ is ordered

		(₹)
Purchase Cost	(12,000 units × ₹ 1,740)	2,08,80,000.00
Ordering Cost*	[(12,000 units ÷ 371 units) i.e. 33 × ₹1,200]	39,600.00
Carrying Cost**	(371 units × ₹ 1,740 × ½ × 12/100)	38,732.40
Total Cost		2,09,58,332.40

(b) When Quantity Discount of 5% is offered.

		(₹)
Purchase Cost	(12,000 units × ₹ 1,740 × 0.95)	1,98,36,000.00
Ordering Cost*	[(12,000 units ÷ 6,000 units) × ₹1,200]	2,400.00
Carrying Cost**	(6,000 units × ₹1,653 × ½ × 12/100)	5,95,080.00
Total Cost		2,04,33,480.00

Advise – The total cost of inventory is lower if quantity discount offer is accepted. Hence, the company is advised to accept the quantity discount.

$$\text{* Ordering Cost} = \frac{\text{Annual Demand}}{\text{Order Quantity}} \times \text{Cost of placing an order}$$

$$\text{** Carrying Cost} = \frac{\text{Cost per unit} \times \text{Quantity ordered} \times \text{Carrying Cost}}{2}$$

2. Rounak Infratech Ltd.

Contract Account as on 31st December, 2013

Dr. *Cr.*

Particulars	Amount (₹)	Particulars	Amount (₹)
To Materials	2,58,100	By Bank/ Cash:	
To Labour	5,60,500	- Sale of Materials	4,000
To Foremen's salary	79,300	- Sale of Plant	6,500
To Supervisor's salary (Working Note- 1)	27,000	By Costing Profit and Loss A/c (loss on sale of materials)	500
To Costing Profit and Loss A/c (Profit on sale of plant)	1,000	By Materials at site	25,400
To Depreciation of plant (Working Note- 2)	14,000	By Work in Progress:	
To Administrative and other expenses	1,40,000	- Value of work certified (50% of ₹ 20,00,000)	10,00,000
		- Cost of work uncertified (Working Note-3)	2,60,875
To Notional Profit c/f	2,17,375		
	12,97,275		12,97,275
To Costing Profit & Loss A/c. (Working Note- 4)	1,08,688	By Notional Profit b/f	2,17,375
To Work-in-Progress (Reserve)	1,08,687		
	2,17,375		2,17,375
1st January, 2014			
To Materials at site b/f	25,400		
To Work-in-progress b/f			
-Cost of work uncertified 2,60,875			
-value of work certified 10,00,000 12,60,875 Less: Reserve 1,08,687	11,52,188		

Dr.	Contractee Account		*Cr.*
Particulars	**Amount (₹)**	***Particulars***	**Amount (₹)**
To Value of work certified	10,00,000	By Cash	7,50,000
		By Balance c/f	2,50,000
	10,00,000		10,00,000

Balance Sheet (extract) as at 31st December, 2013

Liabilities	**Amount (₹)**	***Assets***	**Amount (₹)**
Profit and Loss A/c	1,08,688	Plant at site (Working Note-5)	2,40,500
		Materials at site	25,400
		Work-in-progress 11,52,188	
		Less: Cash received	
		On account 7,50,000	4,02,188

Working Notes:

1. Supervisor's salary

   ¾ x ₹ 4,000 x 9 months = ₹ 27,000

2. Depreciation on plant

   $$\frac{₹\,2,60,000 - ₹\,15,000}{7\text{ years}} \times \frac{146\text{ days}}{365\text{ days}} = ₹\ 14,000$$

3. Cost of work uncertified:

   Cost of work completed

   [₹ (2,58,100 + 5,60,500 + 79,300 + 27,000 + 1,000 + 14,000 + 1,40,000) - ₹(4,000 + 6,500 + 500 + 25,400)]

   Or, ₹ 10,79,900 – ₹ 36,400 = ₹ 10,43,500

   ₹10,43,500 represents 2/3rd of the contract. Hence cost of full contract is : ₹10,43,500 x 3/2 = ₹ 15,65,250

   Since 50% of the contract price has been certified by the architect, the cost of work certified is : 50% of ₹ 15,65,250= ₹ 7,82,625.

   Therefore, *Cost of work uncertified = ₹ 10,43,500 - ₹ 7,82,625 = ₹ 2,60,875*

4. Profit to be transferred to Costing profit and loss account:

   $$\frac{2}{3} \times \text{Notional Profit} \times \frac{\text{Cash Received}}{\text{Work Certified}}$$

$$\frac{2}{3} \times ₹\,2,17,375 \times \frac{₹\,7,50,000}{₹\,10,00,000} = ₹\,1,08,687.50 \text{ or } ₹\,1,08,688$$

5. Plant at site on 31.12.2013

	(₹)
Cost of plant issued to site	2,60,000
Less: Depreciation	14,000
	2,46,000
Less: Written down value of plant sold	5,500
	2,40,500

3. Production during the month 1,250 units

Time allowed for 1,250 units @ 2 hours per unit (1,250 x 2 hours) 2,500 hours

Actual time taken 25 days x 8 hours x 10 workers 2,000 hours

Time saved 500 hours

Labour cost per piece under time rate scheme : 2 hours x ₹ 2 = ₹ 4

Calculation of effective hourly rate under:

Halsey Scheme:

	(₹)
Basic wages of 10 workers : 2,000 hours @ ₹ 2 per hour	4,000
Bonus 50% x (500 hours x ₹ 2)	500
Total wages for 2,000 hours	4,500

Effective hourly rate of earning = $\frac{₹\,4,500}{2,000\text{ hours}}$ = ₹ 2.25

Labour cost per piece = $\frac{₹\,4,500}{1,250\text{ units}}$ = ₹ 3.60

Saving in terms of direct labour cost per piece (₹ 4.00 – ₹ 3.60) = ₹ 0.40

Rowan Scheme:

	(₹)
Basic wages (as calculated under Halsey scheme)	4,000
Bonus : $500\text{ hours} \times \frac{2,000\text{ hours}}{2,500\text{ hours}} \times ₹\,2$	800
Total wages for 2,000 hours	4,800

Effective hourly rate of earnings $\frac{₹ 4,800}{2,000 \text{ hours}}$ = ₹ 2.40

Labour cost per piece $\frac{₹ 4,800}{1,250 \text{ units}}$ = ₹ 3.84

Saving in terms of direct labour cost per piece (₹ 4.00 – ₹ 3.84) = ₹ 0.16

Advise: Navya should introduce Halsey incentive scheme, as it gives more saving than the Rowan incentive scheme.

4. Abnormal idle time : 200 x ½ day = 100 men days

Actual time attended : 200 x 50 days = 10,000 men days

Actual time worked : 10,000 – 100 = 9,900 men days

Actual production : 9,00,000 units

Standard requirements for actual production:

Material : $\frac{9,00,000 \text{ units}}{1,00,000 \text{ units}} = 9$ tons or 9,000 kg.

Labour : $\frac{9,00,000}{100} = 9,000$ men days

	(₹)
Material Price Variance	
(Standard price – Actual price) × Actual quantity	
(₹ 20 – ₹ 21) × 10,000 kg.	10,000 (A)
Material Usage Variance	
(Standard usage – Actual usage) × Standard price	
(9,000 kg. – 10,000 kg.) × ₹ 20	20,000 (A)
Total material variance	30,000 (A)
Labour rate variance	
(Standard rate – Actual rate) × Actual man days attended	
(₹ 6 – ₹ 6.50) × 10,000 hours	5,000 (A)
Labour efficiency variance	
(Standard man days – Actual man days worked) × Standard rate	
(9,000 – 9,900) × ₹ 6	5,400 (A)

Idle time variance

Idle man days x Standard rate

100 x ₹ 6	600 (A)
Total labour variance	11,000 (A)

5. **(a)** Cost Allocation and Cost Absorption: Cost Allocation is defined as the allotment of whole items of cost to cost centres. For example, if a supervisor works exclusively for Fabrication Department in an engineering company, then the salary paid to him should be charged to Fabrication department account. This technique of charging the entire overhead expenses to a cost centre is known as cost allocation.

Cost Absorption is defined as the process of absorbing all overhead costs allocated to or apportioned over particular cost centre or production department by the units produced. For example, the overhead costs of a lathe centre may be absorbed by a rate per lathe hour.

Cost absorption can take place only after cost allocation. In other words, the overhead costs are either allocated or apportioned over different cost centres and afterwards they are absorbed on equitable basis by the output of the same cost centres.

(b) Fixed Budget and Flexible Budget: A budget can be fixed or flexible. A fixed budget assumes the most likely set of conditions and estimates are developed on the basis of only one level of future activity. Thus, a fixed budget is a sort of rigid plan under which the management attempts to forecast activities on the basis of the most likely set of conditions.

In a dynamic situation, the condition under which a business operates seldom remains fixed. The level of activity and volume of output of a company vary considerably from time to time due to many factors. Therefore, fixed budget do not serve the function of a bench mark against which actual performance can be judged. In such situations, flexible budget would be prepared. These can be defined as budgets which are designed to change in accordance with the level of activity attained. Thus, instead of estimating only one level of activity, estimates are made for the budget period on the basis of a number of possibilities. Costs are analysed according to their behavior, i.e., variable, fixed and semi-variable.

6. **(i)** **Purifying Process A/c.**

Particulars	**Qty (kg)**	**Rate (₹)**	**Amt. (₹)**	**Particulars**	**Qty (kg)**	**Rate (₹)**	**Amt. (₹)**
To Raw Material	10,000	17	1,70,000	By Normal loss (10% of 10,000	1,000	2.10	2,100

				kgs)			
To Wages			11,000	By Work in process A/c (output transferred)	9,100	22*	2,00,200
To Overheads @ 150% of ₹11,000			16,500				
To Indirect materials			2,600				
To Abnormal Gain	100	22*	2,200				
	10,100		2,02,300		10,100		2,02,300

* Cost per unit = $\frac{\text{Total cost - Realisation from normal loss}}{\text{Quantity introduced - Normal loss}}$

$= \frac{₹2,00,100 - ₹2,100}{10,000 - 1,000} = ₹\ 22$

(ii) Normal loss A/c.

Particulars	Qty (kg)	Rate (₹)	Amt. (₹)	Particulars	Qty (kg)	Rate (₹)	Amt. (₹)
To Purifying process A/c.	1,000	2.10	2,100	By Cash A/c	900	2.10	1,890
				By Abnormal Gain A/c	100	2.10	210
	1,000		2,100		1,000		2,100

(iii) Abnormal Gain A/c

Particulars	Qty (kg)	Rate (₹)	Amt. (₹)	Particulars	Qty (kg)	Rate (₹)	Amt. (₹)
To Normal loss A/c	100	2.10	210	By Purifying process A/c	100	22	2,200
To Costing P& L A/c			1,990				
	100		2,200		100		2,200

(iv) Royalty A/c

	Amt. (₹)		Amt. (₹)
		By Production A/c (9100 kgs x 0.35)	3,185

7. (a) Spoilage can be defined as the materials which are badly damaged in the course of manufacturing operations to the extent that they cannot be rectified economically and hence taken out of process, to be disposed of in some manner without further processing. Spoilage may be either normal or abnormal.

Defective products are such semi-finished or finished products produced by a manufacturing unit, which are not in conformity with laid-down standards or dimensional specifications. Defectives produced can be re-worked or reconditioned by the application of additional materials, labour and/ or processing and brought to the point of either standard or sub-standard product. The costs incurred for reconditioning are known as the "Cost of re-operations of the defectives". Defectives production may be the result of various causes such as sub-standard materials, bad-workmanship, carelessness in planning, laxity in inspection etc.

The difference between spoilage and defectives is that while spoilage cannot be repaired or reconditioned, defectives can be rectified and transformed, either back to standard production or to seconds.

(b) The main advantages of Integrated Accounting System are as follows:

(i) Since there is one set of accounts, thus there is one figure of profit. Hence the question of reconciliation of costing profit and financial profit does not arise.

(ii) There is no duplication of recording of entries and efforts in the separate set of books.

(iii) Costing data are available from books of original entry and hence no delay is caused in obtaining information.

(iv) The operation of the system is facilitated with the use of mechanized accounting.

(v) Centralisation of accounting function results in economy.

MOCK TEST PAPER – 1

IPCC: GROUP – I

PAPER – 3B: FINANCIAL MANAGEMENT

Suggested Answers/Hints

1. The requirement is to identify the factor considered in determining the appropriate level of working capital.

(i) It is incorrect because it is a consideration regarding long-term financing.

(ii) It is incorrect because it is a consideration regarding capital structure.

(iii) It is incorrect because short-term debt is generally less expensive than long-term debt.

(iv) It is correct because the main reason to retain working capital is to meet the firm's financial obligation. Therefore, the amount is determined by offsetting the benefit of current assets and current liabilities against the probability of technical insolvency.

2. (a) Cash outflow

	Rs.
Cost of new machine	2,50,000
Less: Sale of old machine	50,000
Less: Tax saving from loss due to sale of old machine Rs. 40,000 (Rs. 90,000 - Rs 50,000) × 50%	20,000
Net cash outflow	1,80,000

Cash inflow

	Amount before tax Rs.	*Amount after tax Rs.*
Cost savings	30,000	15,000
Tax savings on depreciation:		
New machine	25,000	
Old machine	10,000	
Differential depreciation	15,000	
Tax savings on Rs. 15,000 @ 50%		7,500
Cash flow after tax (1 to 8 years)		22,500

Salvage value of new machine (9th year)		25,000
Cash flow after tax (9th year)		47,500

Determination of Net Present Value

Year *(1)*	*Cash in flow after tax (Rs)* *(2)*	*Present value factor at (10%)* *(3)*	*Present value (Rs.) of cash inflows* *(4)=(2) X (3)*
1 - 8	22,500	5.335	1,20,038
9	47,500	0.424	20,140
		Total cash inflow	1,40,178
		Less: Net cash outflow	1,80,000
		Net present value	(39,822)

Decision: Since the net present value is negative, the old machine should not be replaced.

(b) Statement of Estimation of Working Capital Requirements of Gamma Limited

	Rs.
A. *Investment in Inventory*	
1. Raw Material Inventory: One month (30)days(RMC/360)x RMCP = [(70,000 x 52/360) x 30	3,03,333.33
2. Work-in-Process Inventory: Half-a-Month (15 days) (COP/360) x WIPC= {70,000x110.50/360]x15	3,22,291.67
3. Finished Goods Inventory: One Month (30 days) (COS/360)x FGCP=[(70,000x110.5)/360] x 30	6,44,583.33
	12,70,208.33
B. *Investment in Debtors:* Two Months (60 days) (Credit sale (cost)/360)x BDCP=[(52,500x110.5/360)]x60	9,66,875.00
C. *Cash Balance*	1,20,000.00
D. Investment in Current Assets (A+B+C)	23,57,083.33

E.	*Current Liabilities: Deferred Payment*	
	1. Creditors: One Month (30 days) (Purchase of raw material/360) x PDP=[(70,000x52)/360)]x30	3,03,333.33
	2. Deferred Wages: 1 ½ weeks (10 days) = [(70,000x 19.5)/360)]x10	37,916.67
	3. Deferred Overheads: One Month (30 days) = [(70,000x39)/360)] x 30	2,27,500.00
F.	*Total Current Liabilities*	5,68,750.00
G.	**Net Working Capital (D − F)**	17,88,333.33

3. (a) (i) Computation of Earnings Per Share (EPS) for the expected Earnings Before Interest and Taxes(EBIT) for the expected EBIT.

	Debt *Rs.*	*Equity* *Rs.*
Expected earnings before interest & tax	15,000	15,000
Less: Interest (12% of Rs. 50,000)	6,000	-
Earnings before tax (EBT)	9,000	15,000
Less: Tax (@ 46%) of EBT (Rs. 9000 X 46%)	4,140	6,900
Earnings available to equity shareholder: (A)	4,860	8,100
Number of shares issued : (B)	10,000	12,500
(Refer to working note)		
Earnings per shares: (A) / (B)	0.486	0.648

Recommendation: Earnings per share is higher when the company raises additional funds by issue of equity shares.

Working note

Number of new shares to be issued:

Amount required:	(i)	Rs. 50,000
Market price per share	(ii)	Rs. 20
No. of new shares to be issued:	(i) / (ii)	2,500

(ii) Computation of indifference level of EBIT for the two alternatives

$$\frac{(\text{EBIT} - ₹\,6{,}000)(1-0.46)}{10{,}000\ \text{Nos}} = \frac{\text{EBIT}\,(1-0.46)}{12{,}500\ \text{Nos}}$$

or, EBIT= Rs. 30,000

Therefore, Indifference level of EBIT for two alternatives is Rs. 30,000.

(iii) The EPS for the EBIT at the indifference level.

$$\text{EPS} = \frac{₹\,30{,}000 \times (1-0.46)}{12{,}500\ \text{Nos}}$$

= Rs. 1.296 per share

(b) (i) Increase in taxable income if sales increase by 6%.

$$\text{Composite Leverage} = \frac{\text{Contribution}}{\text{EBT}} = \frac{₹\,1{,}40{,}000}{₹\,35{,}000} = 4$$

If the sales increases by 6%, EBT will increase by 24%. ($4 \times 6\%$)

(ii) Increase in EBIT if sales increase by 10%.

$$\text{Operating Leverage} = \frac{\text{Contribution}}{\text{Earnings before interest and tax}} = \frac{₹\,1{,}40{,}000}{₹\,40{,}000} = 3.5$$

If sales increases by 10%, EBIT will increase by (3.5×10) 35%.

(iii) Increase in taxable income if EBIT increase by 6%.

$$\text{Financial Leverage} = \frac{\text{Earnings before interest and tax(EBIT)}}{\text{EBT}} = \frac{₹\,40{,}000}{₹\,35{,}000} = 1.14$$

If EBIT increases by 6%, EBT will increase by 6.8%. ($1.14 \times 6\%$)

4. (a) (i) *Profit on additional sales*

Selling price per unit	Rs. 100	
Less: variable cost per unit	80	
Marginal contribution/unit	20	
Number of additional units to be sold	× 15,000	Rs. 3,00,000

(ii) Cost of additional investment in receivables

(a) Average investments in receivables:

Present plan = (60,000 units × Rs.90)/Debtors turnover, 12(12÷1) = Rs. 4,50,000

Proposed plan : [(60,000 units × Rs.90) + (15,000 units × Rs. 80)]/6 (12÷2) = Rs. 11,00,000

(b) Additional investments in receivables = Rs. 11,00,000 – Rs. 4,50,000 = Rs. 6,50,000

(c) Cost of additional investments in receivables = 0.20 × Rs. 6,50,000 = Rs. 1,30,000.

(iii) Summary

Profits on additional sales	Rs. 3,00,000
Less: Increased cost of investments	1,30,000
Net increase in profits	1,70,000

Thus, the relaxation of credit standards is justified.

(b) The major advantage of IRR is that it does not require the identification of the 'cost of capital' to be used as a 'discount rate'. However it suffers from the following limitations,

- There is a possibility of getting multiple IRR's if the cash flows are not conventional.
- It assumes that funds can be reinvested by the company at the calculated IRR.
- It gives the rate of return per rupee which may not always be a proper yardstick for financial appraisal.

Test Series: February, 2014

MOCK TEST PAPER – 1

INTERMEIDATE (IPC): GROUP – I

PAPER – 4: TAXATION

*Question **1** is compulsory.*

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

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

1. (a) From the following details, compute the total income of Subhash of Bangalore and tax payable for the A.Y.2014-15:

Particulars	₹
Salary including dearness allowance	4,15,000
Bonus	15,000
Salary of servant provided by the employer	18,000
Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	13,000

Subhash purchased a flat in a co-operative housing society in Bangalore for ₹ 6,20,000 in September, 2008, which was financed by a loan from Life Insurance Corporation of India for ₹ 2,00,000 @ 15% interest, his own savings of ₹ 1,20,000 and a deposit from a nationalized bank for ₹ 3,00,000 to whom this flat was given on lease for ten years. The entire loan of ₹ 2,00,000 obtained from LIC, is outstanding as on 31.3.2014.

The rent payable by the bank was ₹ 5,000 per month. The following particulars are relevant:

(i) Municipal taxes paid by Mr. Subhash ₹ 3,900 (per annum)

(ii) Life Insurance for self ₹ 21,700 (per annum) [sum assured ₹ 25,00,000]

(iii) He earned ₹ 3,200 in share speculation business and lost ₹ 4,900 in cotton speculation business.

(iv) In the year 2008-09, he had gifted ₹ 50,000 to his wife and ₹ 25,000 to his son who was aged 13. The gifted amounts were advanced to Mr. Bobby, who was paying interest @ 20% per annum.

(v) Subhash received a gift of ₹ 15,000 each from four friends.

(vi) He contributed ₹ 30,000 to Public Provident Fund. *(10 Marks)*

(b) Balwantpur Post Office provided the following services to persons other than Government during the quarter ended 30.06.2013:-

Services rendered	Amount (₹)
Postal services	2,25,000
Transfer of money through money orders	4,75,000
Operation of saving accounts	1,30,000
Postal life insurance services	1,50,000
Distribution of passport applications	4,50,000
Issuance of postal orders	4,40,000
Collection of telephone and electricity bills	2,00,000
Pension payment services	69,000
Speed post services	6,00,000
Express parcel post services	3,00,000

Compute the service tax liability of Balwantpur Post Office for the quarter ended 30.06.2013.

Notes:

1. Point of taxation for all the aforesaid cases fall during the quarter ended 30.06.2013.
2. All the service charges stated above are exclusive of service tax.
3. Small service providers' exemption need not be taken into account while solving the aforesaid question. *(5 Marks)*

(c) Pulak Ltd. of Hyderabad made a total purchases of input and capital goods of ₹ 60,00,000 during the month of November, 2013 including the following purchases:-

(i) Goods worth ₹ 8,00,000 were purchased from Mysore on which C.S.T. @ 2% was paid.

(ii) Goods purchased for personal use amounted to ₹ 12,00,000 and goods purchased from unregistered dealers amounted to ₹ 18,00,000.

(iii) It purchased capital goods (not eligible for input credit) worth ₹ 9,50,000 and those eligible for input credit for ₹ 9,00,000. The input VAT credit on eligible capital goods is available in 36 equal monthly installments.

(Note: All purchases given are exclusive of tax and VAT @ 4% is paid on them)

Pulak ltd. sold goods in Hyderabad during the month of November, 2013 worth ₹ 12,00,000 on which VAT @ 12.5% is payable.

Calculate

(i) the amount of input tax credit available for the month of November, 2013

(ii) VAT payable for the month of November, 2013 and

(iii) input tax credit carried forward, if any. *(5 Marks)*

2. (a) Mr. Murad furnishes the following data for the previous year ending 31.3.2014:

(i) Unlisted Equity Shares of Batliboi Ltd., 8,000 in number were sold on 28.7.2013, at ₹ 600 for each share.

(ii) The above 8,000 shares were acquired by Murad in the following manner:

(a) Received as gift from his father on 5.10.1980 (4,000 shares) the fair market value on 1.4.1981 ₹ 40 per share.

(b) Bonus shares received from Batliboi Ltd. on 31.8.1985 (2,000 shares).

(c) Purchased 2,000 shares on 18.5.1995 at the price of ₹ 150 per share.

(iii) Purchased one residential house at ₹ 30 lakhs, on 1.5.2014 from the sale proceeds of shares.

(iv) Murad already owns a residential house, even before the purchase of above house.

You are required to compute the taxable capital gain. He has no other source of income chargeable to tax.

(Cost Inflation Index – Financial year 1995-96: 281; Financial year 2013-14: 939)

(4 Marks)

(b) M/s. Anna Ltd., a manufacturing concern, furnishes the following particulars:

		₹
(i)	Opening writing down value of plant and machinery (15% block)	50,00,000
(ii)	Purchase of plant and machinery (put to use before 10-09-2013)	1,06,00,000
(iii)	Sale proceeds of plant and machinery which became obsolete- the plant and machinery was purchased on 01-04-2011 for ₹ 5,00,000.	50,000

Further, out of plant and machinery purchased:

(i) Plant and machinery of ₹ 50,000 has been installed in office.

(ii) Plant and machinery of ₹ 20,000 was used previously for the purpose of business by the seller.

Compute the depreciation, additional depreciation and amount of deduction under section 32AC as per Income-tax Act, 1961 for the Assessment Year 2014-15. *(4 Marks)*

(c) State whether the following statements are true or false giving reasons to substantiate your answer:

(i) The rate of service tax shall be rate in force on the date of receipt of payment for the taxable services.

(ii) Services provided to RBI are not chargeable to service tax.

(iii) Provision of service by an employee to the employer in the course of employment is outside the ambit of service tax.

(iv) Auxiliary services used for gambling events are not liable to service tax.

(4 ×1 = 4 Marks)

(d) "It is said that VAT is a logical beauty. Further, the greatest advantage of the system is that it does not interfere in the choice of decision for purchases." Discuss the validity of the statement *(4 Marks)*

3. (a) State with reasons of the deductibility of the items given above under the Income-tax Act, 1961 for the Assessment Year 2014-15:

(i) Radha Ltd., engaged in manufacture of medicines (pharmaceuticals) incurred Capital expenditure on scientific research ₹ 12,00,000 which includes cost of land and building ₹ 2,20,000.

(ii) Sonu & Co. has set up a warehousing facility for storage of food grains. It commenced operations on 01.04.2013. For this purpose, Sonu & Co. incurred capital expenditure of ₹ 65 lakhs on purchase of building in February 2013.

(4 Marks)

(b) Mrs. Sharma transferred her immovable property to Arihant Co. Ltd. subject to a condition that out of the rental income, a sum of ₹ 72,000 per annum shall be utilized for the benefit of her son's wife.

Mrs. Sharma claims that the amount of ₹ 72,000 (utilized for the benefit of her son's wife) should not be included in her total income as she no longer owned the property.

State with reasons whether the contention of Mrs. Sharma is valid in law. *(4 Marks)*

(c) Mahaj Industries Ltd. (MIL) is an Indian Company. It has received taxable services from a UK based company-Bodycote Ltd. on 06.05.2013. Bodycote Ltd. raised on MIL an invoice of £ 35,000 on 23.05.2013. MIL debited its books of accounts on 06.06.2013 and made the payment on 24.07.2013.

Bodycote Ltd. and MIL are associated enterprises. Determine the point of taxation using aforesaid details. *(4 Marks)*

(d) Mr. Aaditya Singla is a trader selling raw materials to a manufacturer of finished products. He imports his stock in trade as well as purchases the same from the local markets. He sold some goods to Bharat during the month of January, 2014.

Using the following information, calculate the VAT and invoice value charged by him to Bharat, assuming the rate of input and output VAT @ 12.50%:

		₹
(1)	Cost of imported materials including import duty of ₹ 50,000	2,50,000
(2)	Cost of local materials including VAT	2,25,000
(3)	Other expenditure including storage, transport, interest and loading and unloading and profit earned by him	1,10,000

(4 Marks)

4. (a) Graham Gooch, an England cricketer visits India for 100 days in every financial year. This has been his practice for the past 10 financial years. Find out his residential status for the assessment year 2014-15. *(4 Marks)*

(b) Mr. Verma is a resident Indian. During the F.Y. 2013-14, interest of ₹ 2,02,000 was credited to his Non-resident (External) Account with the SBI. ₹ 18,000 being interest on fixed deposit with SBI was credited to his savings bank account during this period. He also earned ₹ 8,000 as interest on this savings account. Is Mr. Verma required to file return of income?

What will be your answer, if he owns a house in London? *(4 Marks)*

(c) Examine the applicability of service tax in case of following educational services during the month of August, 2013:

(i) "High Tech", an Institute provides coaching to CA students for the preparation of CA Final Examination.

(ii) 'Success Point' an industrial training centre (ITC) affiliated to the State Council Vocational Training, Delhi imparts industrial training. *(2 x 2 = 4 Marks)*

(d) Shri Laxmi & Co. purchased raw material 'A' for ₹ 60,00,000 plus VAT at 12.5%. Out of such raw material 70% was used for manufacture of taxable goods and the balance for the manufacture of exempted goods.

Another raw material 'B' was purchased for ₹ 40,00,000 on which VAT was paid @1%. Out of the raw material 'Y', 60% was used for manufacture of taxable goods and the balance for the manufacture of exempted goods.

The entire taxable goods were sold for ₹ 75,00,000 plus VAT at 12.5%. There was no opening or closing inventory of taxable goods or raw materials.

Compute the VAT liability of Shri Laxmi & Co. *(4 Marks)*

5. (a) State in brief the applicability of tax deduction at source provisions, the rate and amount of tax deduction in the following cases for the financial year 2013-14:

(i) Winning by way of jackpot in a horse race ₹ 1,20,000.

(ii) Payment made by a firm to sub-contractor (an individual) ₹ 2,50,000 on 29.03.2014. Further, there is an outstanding balance of ₹ 1,70,000 shown in the books as on 31-03-2014.

(iii) Rent paid for plant and machinery ₹ 1,75,000 by a partnership firm having sales turnover of ₹ 25,00,000 and net loss of ₹ 25,000.

(iv) Payment made to Brett Lee, an Australian cricketer, by a publishing house for contribution of articles in the Newspaper ₹ 55,000. *(4 Marks)*

(b) Examine the following, with reference to the provisions of the Income-tax Act, 1961:

(i) A charitable trust, registered under section 12AA, whose main object is "advancement of any other object of general public utility" receives ₹ 30 lakhs in aggregate during the P.Y. 2013-14 from commercial activities. The trust wants to claim benefit of exemption in respect of its income for the P.Y.2013-14 on the basis of its registration as a charitable trust under section 12AA. Can it do so?

(ii) Mr. Gurmeet held 100 unlisted shares of Alpha Ltd., a domestic company. On 10.09.2013, he received ₹ 55,000 from Alpha Ltd. for buy back of the unlisted shares held by him. Is the amount chargeable to tax in the hands of Mr. Gurmeet? *(2 x 2 = 4 Marks)*

(c) (i) Vasu Electronics Ltd. exported some air conditioners to Integrated Inc. of USA. It received US $ 10,000 as consideration for the same and sold it @ ₹60 per US dollar. Compute the value of taxable service under rule 2B of the Service Tax (Determination of Value) Rules, 2006 in the following cases:-

(a) RBI reference rate for US dollar at that time is ₹ 62 per US dollar.

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

(ii) What would be the value of taxable service if US $ 10,000 are converted into UK £ 5,000. RBI reference rate at that time for US $ is ₹ 61 per US dollar and for UK £ is ₹ 100 per UK Pound. *(4 Marks)*

(d) Compute the VAT payable at each stage using 'invoice method' from the particulars given below:-

Stage	Particulars	Profit (as % of cost price)
I	Lifeline Medicaids Ltd. sold the medicines manufactured by it	--

	to the distributors of medicines- Healers Pharmacy - at ₹ 80,000.	
II	Healers Pharmacy sold the medicines to the wholesalers- All Well Medicos.	15%
II	All Well Medicos sold the medicines to the retailers- Cure Medicines.	20%
IV	Cure Medicines sold the medicines to the ultimate consumers	25%

Assume that the VAT rate is 4% and that there was no value addition at various stages of sale except profit margin. *(4 Marks)*

6. (a) Mr. Sagar submits the following information for the financial year ending 31st March, 2014. He desires that you should:

(i) Compute the total income and

(ii) Ascertain the amount of losses that can be carried forward.

	Particulars	₹
(i)	He has two houses :	
	(a) House No. I – Income after all statutory deductions	54,000
	(b) House No. II – Current year loss	(15,000)
(ii)	He has three proprietary businesses :	
	(a) Textile Business :	
	(i) Discontinued from 31st August, 2013 – Current year loss	55,000
	(ii) Brought forward business loss of A.Y.2011-12	87,500
	(b) Chemical Business :	
	(i) Discontinued from 1st February, 2012 – hence no profit/loss	Nil
	(ii) Bad debts allowed in earlier years recovered during this year	48,500
	(iii) Brought forward business loss of A.Y. 2012-13	57,000
	(c) Leather Business : Profit for the current year	1,25,000
	(d) Share of profit in a firm in which he is partner since 2003	21,450
(iii)	(a) Short-term capital gain	75,000
	(b) Long-term capital loss	45,000
(iv)	Contribution to LIC towards premium	18,000

(8 Marks)

(b) "Mrs. Nirmal Aggarwal, a life insurer wants to pay service tax at a rate different than 12%". Can she do so? Critically examine the contention of Mrs. Nirmal Aggarwal.

(4 Marks)

(c) State whether the following are true or false giving reasons to substantiate your answer:

(i) Under VAT, the tax is payable on the first sale price.

(ii) VAT would increase the working capital requirements and the interest burden.

(2 × 2 = 4 Marks)

7. (a) Smt. Shobha reports the following transactions to you:

(i) Received cash gifts on the occasion of her marriage on 25-12-2013 of ₹ 2,20,000. It includes gift of ₹ 40,000 received from non-relatives.

(ii) On 10-09-2013, being her birthday, she received a gift by means of cheque from her mother's maternal uncle, the amount being ₹ 45,000.

(iii) On 01-01-2014, she acquired a vacant site from her friend for ₹ 2,05,000. The State stamp valuation authority fixed the value of site at ₹ 2,80,000 for stamp duty purpose.

(iv) She bought 120 equity shares of a listed company from another friend for ₹ 72,000. The value of shares in the stock exchange on the date of purchase was ₹ 1,27,000.

Determine the income chargeable to tax under the head "Income from Other Sources" in the hands of Smt. Shobha for the A.Y. 2014-15.Your answer should be supported by reasons. *(6 Marks)*

(b) How will you calculate the period of holding in case of transfer of the following assets?

(i) Shares received by Mr. A from his friend without consideration, having FMV of ₹ 75,000.

(ii) Bonus shares *(2 Marks)*

(c) Ceridian Private Limited is engaged in providing the taxable services. Compute the value of taxable service and the service tax payable by it in the month of July, 2013 from the information furnished below:-

Receipts	**Amount (₹)**
Advances received from clients for which no service has been rendered so far	9,00,000
Demurrage charges recovered for use of the services beyond the agreed period	40,000

Advance forfeited for cancellation of an agreement to provide a service	4,00,000
Security deposits forfeited for damages done by service receiver owing to his negligence in the course of receiving a service	6,00,000

Besides, the above receipts, one of the clients-Extron Ltd. made a payment of ₹ 2,00,000 (out of which ₹ 35,000 were paid extra by mistake). However, Ceridian Private Limited refused to return the excess payment received.

Note: Ceridian Private Limited is not eligible for small service providers' exemption under *Notification No. 33/2012 – ST dated 20.06.2012.* *(4 Marks)*

(d) An auditor plays an important role to ensure that the tax payers discharge their tax liability properly under the VAT system. Discuss the validity of the statement.

(4 Marks)

MOCK TEST PAPER – 1

INTERMEDIATE (IPC): GROUP – I

PAPER – 4: TAXATION

SUGGESTED ANSWERS / HINTS

1. (a) Computation of total income and tax liability of Subhash for the A.Y. 2014-15

Particulars		₹	₹
Salary Income			
Salary including dearness allowance			4,15,000
Bonus			15,000
Value of perquisites:			
(i) Salary of servant		18,000	
(ii) Free gas, electricity and water		13,000	31,000
			4,61,000
Income from house property			
Gross Annual Value (GAV) (Rent receivable is taken as GAV in the absence of other information) (₹ 5,000 × 12)		60,000	
Less: Municipal taxes paid		3,900	
Net Annual Value (NAV)		56,100	
Less: Deductions under section 24			
(i) 30% of NAV	₹ 16,830		
(ii) Interest on loan from LIC @15% of ₹ 2,00,000	₹ 30,000	46,830	9,270
Income from speculative business			
Income from share speculation business		3,200	
Less: Loss from cotton speculation business		4,900	
Net Loss [See Note 1]		(1,700)	
Income from Other Sources			
(i) Income on account of interest earned from advancing money gifted to his son [See Note 2]		-	
(ii) Interest income earned from advancing money gifted to wife has to be clubbed with the income of the assessee as per section 64(1)		10,000	
(iii) Gift received from four friends (taxable under section 56(2)(vii) as the aggregate amount received			

during the year exceeds ₹ 50,000)	60,000	70,000
Gross Total Income		**5,40,270**
Less: Deduction under section 80C		
- Life insurance premium for self (fully allowable, since premium paid is less than 10% of sum assured)	21,700	
- Contribution to Public Provident Fund	30,000	51,700
Total Income		**4,88,570**

Particulars	₹
Tax on total income @10% on ₹ 2,88,570 (i.e. ₹ 4,88,570-₹ 2,00,000)	28,857
Less: Rebate under section 87A, as total income does not exceed ₹ 5,00,000	2,000
	26,857
Add: Education cess@2%	537
Add: Secondary and higher education cess@1%	269
	27,663
Tax liability (rounded off)	**27,660**

Notes:

(1) Net loss from speculative business has to be carried forward as it cannot be set off against any other head of income.

(2) Interest earned from advancing money gifted to his son during the year 2008-09 when he was 13 years old is not includible in the hands of Subhash, since Subhash's son turned major during the P.Y. 2013-14. Clubbing provisions are not attracted where the child is major.

(b) Services provided by the Government or a local authority are not chargeable to service tax as they are included in the negative list. However, following services provided to a person other than Government, by the Department of Posts are excluded from the negative list:-

(i) Speed post

(ii) Express parcel post

(iii) Postal Life Insurance

(iii) Agency services which include distribution of passport applications, collection of telephone and electricity bills, etc.

Hence, the aforesaid services are taxable.

Thus, the amount of service tax payable by Balwantpur Post Office for the quarter ended 30.06.2013 would be as follows:-

Particulars	Amount (₹)
Postal services	Nil
Transfer of money through money orders	Nil
Operation of saving accounts	Nil
Postal life insurance services	1,50,000
Distribution of passport applications	4,50,000
Issuance of postal orders	Nil
Collection of telephone and electricity bills	2,00,000
Pension payments	Nil
Speed post services	6,00,000
Express parcel post	3,00,000
Value of taxable service	17,00,000
Service tax @ 12% [17,00,000×12%]	2,04,000
Education cess @ 2% [2,04,000×2%]	4,080
Secondary and higher education cess @ 1% [2,04,000×1%]	2,040
Service tax liability	2,10,120

(c)

	Particulars	₹	₹
A.	Purchases made in November, 2013		60,00,000
	Less: (i) Inter-State purchases (input tax credit not available)	8,00,000	
	(ii) Goods purchased for personal use (input tax credit not available)	12,00,000	
	(ii) Purchase from unregistered dealer (input tax credit not available)	18,00,000	
	(iii) Capital goods (not eligible for input tax credit)	9,50,000	47,50,000
	Total purchases eligible for input tax credit		12,50,000
B.	Input tax credit available		
	VAT credit on inputs @ 4%		
	4% of (₹ 12,50,000 –₹ 9,00,000)		
	i.e. 4% of ₹ 3,50,000		14,000

	VAT credit on eligible capital goods		
	(4% of ₹ 9,00,000) x $\frac{1}{36}$		1,000
	Input tax credit available for November, 2013		15,000
C.	VAT on sales @ 12.5% of ₹ 12,00,000		1,50,000
	Less: Input tax credit		15,000
	Net VAT payable		1,35,000
	Input tax credit carried forward to December,2013		Nil

2. (a) Computation of taxable capital gain of Mr. Murad for A.Y. 2014-15

Particulars	₹	₹
Sale consideration received on sale of 8,000 shares @ ₹ 600 each		48,00,000
Less: Indexed cost of acquisition		
- 4,000 shares received as gift from father on 5.10.1980 Indexed cost (4,000 x ₹ 40 x 939/100)	15,02,400	
- 2,000 bonus shares received from Batliboi Ltd	Nil	
(Bonus shares are acquired on 31.8.1985 i.e. after 01.04.1981. Hence, the cost is Nil.)		
- 2000 shares purchased on 18.5.1995 @ ₹ 150 per share. (2000 x ₹ 150 x 939/281)	10,02,491	25,04,891
Long term capital gain		**22,95,109**
Less : Exemption under section 54F (See Note below)		
₹ 22,95,109 x ₹ 30,00,000 / ₹ 48,00,000		14,34,443
Taxable long term capital gain		**8,60,666**

Note:

Exemption under section 54F can be availed by the assessee subject to fulfillment of the following conditions:

(a) The assessee should not own more than one residential house on the date of transfer of the long-term capital asset;

(b) The assessee should purchase a residential house within a period of 1 year before or 2 years after the date of transfer or construct a residential house within a period of 3 years from the date of transfer of the long-term capital asset.

In this case, the assessee has fulfilled the above mentioned conditions. Therefore, he is entitled to exemption under section 54F.

(b) Computation of written down value of Plant and Machinery of M/s. Anna Ltd. for the A.Y. 2014-15

Particulars	₹
Opening written down value (as on 01.04.2013)	50,00,000
Add: Purchase of plant and machinery during the previous year	1,06,00,000
	1,56,00,000
Less: Sale proceeds of obsolete plant and machinery sold during the year	50,000
Closing Written Down Value (as on 31.03.2014)	**1,55,50,000**

Computation of Depreciation and Additional Depreciation for A.Y. 2014-15 as per section 32 of the Income-tax Act, 1961

Particulars	₹
Normal Depreciation (₹1,55,50,000 x 15%)	23,32,500
Additional Depreciation (Refer Note 2) (₹ 1,06,00,000 – ₹ 50,000 - ₹ 20,000) x 20%	21,06,000
Depreciation on Plant and Machinery	**44,38,500**

Notes:-

(1) Since the new plant and machinery was purchased and put to use before 10.09.2013, it was put to use for more than 180 days in the year. Hence, full depreciation is allowable for A.Y. 2014-15.

(2) As per section 32(1)(iia), additional depreciation is allowable in the case of any new machinery or plant acquired and installed after 31.3.2005 by an assessee engaged, *inter alia,* in the business of manufacture or production of any article or thing, at the rate of 20% of the actual cost of such machinery or plant.

However, additional depreciation shall not be allowed in respect of, *inter alia*, –

(i) any machinery or plant which, before its installation by the assessee, was used either within or outside India by any other person;

(ii) any machinery or plant installed in office premises, residential accommodation or in any guest house.

In view of the above provisions, additional depreciation cannot be claimed in respect of -

(i) Plant and machinery of ₹ 20,000 used previously for the purpose of business by the seller.

(ii) Plant and machinery of ₹ 50,000, installed in office.

Therefore, in the given case additional depreciation has to be provided only on ₹ 1,05,30,000 (i.e., ₹ 1,06,00,000 – ₹ 70,000).

(3) As per section 32AC, manufacturing companies would be entitled to deduction @ 15% of aggregate amount of actual cost of new plant and machinery acquired and installed during the F.Y. 2013-14 and F.Y. 2014-15, if the same exceeds ₹ 100 crore.

In this case, the company would not be entitled to deduction under section 32AC for the F.Y.2013-14, since the investment is less than ₹ 100 crore.

(c) (i) The statement is false. As per section 67A of the Finance Act, 1994 the rate of service tax will be the rate in force at the time when the taxable service has been provided or agreed to be provided.

(ii) The statement is false. Services provided to RBI are chargeable to service tax as they are neither included in the negative list of services nor covered in any of the exemptions.

(iii) The statement is true. Provision of service by an employee to the employer in the course of employment is outside the ambit of service tax because it has been specifically excluded from the definition of service. Hence, service tax cannot be levied on it.

(iv) The statement is false. Negative list of services, inter alia, includes services of gambling. However, auxiliary services used for gambling events are not covered in the negative list of services. Hence, they are liable to service tax.

(d) The statement is valid. Under the VAT system, credit of duty paid is allowed against the liability on the final product manufactured or sold. Therefore, unless proper records are kept in respect of various inputs, it is not possible to claim credit. Hence, suppression of purchases or production will be difficult because it will lead to loss of revenue. A perfect system of VAT is a perfect chain where tax evasion is difficult. Hence, it is said that VAT is a logical beauty.

Further, it is truly said that the greatest advantage of the system is that it does not interfere in the choice of decision for purchases. This is because the system has anti-cascading effect. How much value is added and at what stage it is added in the system of production/distribution is of no consequence. The system is neutral with regard to choice of production technique, as well as business organisation. All other things remaining the same, the issue of tax liability does not vary the decision about the source of purchase. VAT facilitates precise identification and rebate of the tax on purchases and thus ensures that there is no cascading effect of tax. In short, the allocation of resources is left to be decided by the free play of market forces and competition.

3. (a) (i) Weighted deduction@200% is available under section 35(2AB) in respect of expenditure incurred by a company on scientific research on in-house research and development facility as approved by the prescribed authority. However, cost of land or building is not eligible for deduction.

Deduction under section 35(2AB) = 200% of ₹ 9,80,000 = ₹ 19,60,000.

Note: It is presumed that the in-house research and development facility is approved by the prescribed authority and is hence, eligible for weighted deducted@200% under section 35(2AB).

(ii) As per section 35AD, investment linked tax deduction is available in respect of any of the specified businesses defined thereunder. Further, as per section 35AD(1A) a weighted deduction of 150% of the capital expenditure (including expenditure incurred before commencement of operations) is available in respect of certain specified businesses which include *inter alia* business of warehousing facility for storage of agricultural produce. Therefore, in this case, Sonu and Co. would be eligible for deduction of ₹ 97,50,000 (150% of ₹ 65 lakhs), in the year in which it commenced operations i.e., P.Y. 2013-14, provided it has capitalised the amount in its books of accounts on 1.4.2013, being the date of commencement of operations. No other deduction is allowable in respect of the said sum under any other provision of the Income-tax Act, 1961.

(b) The clubbing provisions under section 64(1)(viii) are attracted in case of transfer of any asset, directly or indirectly, otherwise than for adequate consideration, to any person to the extent to which the income from such asset is for the immediate or deferred benefit of son's wife. Such income shall be included in computing the total income of the transferor-individual.

Therefore, income of ₹ 72,000 p.a meant for the benefit of daughter-in-law is chargeable to tax in the hands of transferor i.e., Mrs. Sharma in this case.

The contention of Mrs. Sharma is, hence, not valid in law.

(c) In case of "associated enterprises", where the person providing the service is located outside India, the point of taxation shall be:-

(i) the date of debit in the books of account of the person receiving the service

or

(ii) date of making the payment

whichever is earlier.

Hence, in the given case, the point of taxation shall be earlier of the following two dates:-

(i) the date of debit in the books of account of MIL i.e. 06.06.2013

or

(ii) date of making the payment i.e. 24.07.2013

Thus, the point of taxation is 06.06.2013.

(d) Computation of VAT and invoice value:-

Particulars		₹
Imported material cost		2,50,000
[Since, input tax credit of import duty of ₹ 50,000 is not available, it will form part of cost of input]		31,250
Add: Cost of local materials	2,25,000	
Less:VAT@12.5%	25,000	
[Since, credit of ₹ 25,000 would be available, it will not be included in cost of input]		2,00,000
Add: Other expenses and profit		1,10,000
Sales Price of goods		5,91,250
Add: Output VAT on the above @12.5%		73,906.25
Invoice value charged by Mr. Aaditya to Bharat		6,65,156.25

VAT charged by Mr. Aaditya Singla is ₹ 73,906.25.

4. (a) Determination of Residential Status of Mr. Graham Gooch for the A.Y. 2014-15:-

Period of stay during previous year 2013-14 = 100 days.

Calculation of period of stay during 4 preceding previous years (100 x 4=400 days)

2012-13	100 days
2011-12	100 days
2010-11	100 days
2009-10	100 days
Total	400 days

Mr. Graham Gooch has been in India for a period more than 60 days during previous year 2013-14 and for a period of more than 365 days during the 4 immediately preceding previous years. Therefore, since he satisfies one of the basic conditions under section 6(1), he is a resident for the assessment year 2014-15.

Computation of period of stay during 7 preceding previous years = 100 x 7=700 days

2012-13	100 days
2011-12	100 days
2010-11	100 days
2009-10	100 days
2008-09	100 days
2007-08	100 days
2006-07	100 days
Total	**700 days**

Since his period of stay in India during the past 7 previous years is less than 730 days, he is a not-ordinarily resident during the assessment year 2014-15. (See Note below)

Therefore, Mr. Graham Gooch is a resident but not ordinarily resident during the previous year 2013-14 relevant to the assessment year 2014-15.

Note: A not-ordinarily resident person is one who satisfies any one of the conditions specified under section 6(6), i.e.

(i) If such individual has been non-resident in India in any 9 out of the 10 previous years preceding the relevant previous year, or

(ii) If such individual has during the 7 previous years preceding the relevant previous year been in India for a period of 729 days or less.

(b) Computation of total income of Mr. Verma for A.Y. 2014-15

Particulars	₹
Income from other sources	
Interest earned from Non-resident (External) Account ₹ 2,02,000 [Exempt under section 10(4)(ii), assuming that Mr. Verma has been permitted by RBI to maintain the aforesaid account]	Nil
Interest on bank fixed deposit	18,000
Interest on savings bank account	8,000
Gross Total Income	**26,000**
Less: Deduction under section 80TTA – Interest on saving bank account	8,000
Total Income	**18,000**

An Individual is required to furnish a return of income under section 139(1) if his total income exceeds the maximum amount not chargeable to tax i.e. ₹ 2,00,000 (for A.Y. 2014-15). Hence, Mr. Verma is not required to file a return of income as his total income is below ₹ 2,00,000.

However, as per section 139(1), every person who is a resident, other than not-ordinarily resident in India, having –

(i) any asset (including financial interest in any entity) located outside India or

(ii) signing authority in any account located outside India

is required to file a return of income in the prescribed form compulsorily on or before the due date of filing the return of income whatever be the amount of income chargeable to tax.

Since, Mr. Verma owns a house in London, he has to compulsorily file his return of income for A.Y 2014-15 on or before the due date of filing return of income irrespective of the fact that his total income does not exceed the taxable limit.

(c) 1. 'High Tech', an Institute providing coaching to CA students for the preparation of CA Final Examination is liable to pay service tax on its services as such coaching does not lead to grant of a recognized qualification. Since, only education as a part of a curriculum for obtaining a qualification recognized by law is included in the negative list of services and thus, training given by private coaching institutes would not be covered.

2. 'Success Point' – an industrial training centre (ITC) affiliated to the State Council for Vocational Training, Delhi (SCVTs) have been included in the definition of approved Vocational Education course (VEC) vide the Finance Act, 2013. Thus, the same are included in the negative list and hence service tax is not payable.

(d) Computation of VAT liability of Shri Laxmi & Co.

Particulars	**₹**	**₹**
Output VAT (75,00,000 x 12.5%) (A)		9,37,500
Input VAT (B)		
Raw material 'A' (60,00,000 x 70% x 12.5%) (Refer Note 1)	5,25,000	
Raw material 'B' (40,00,000 x 60% x 1%) (Refer Note 2)	24,000	5,49,000
Net VAT payable by Shri laxmi & Co. (A) – (B)		3,88,500

Notes:

(1) In respect of the raw material 'A', input tax credit is allowed only to the extent raw material 'A' is used in manufacture of taxable goods and hence the same is restricted to the extent of 70%.

(2) In respect of the raw material 'B', input tax credit is allowed only to the extent

raw material 'B' is used in manufacture of taxable goods and hence the same is restricted to the extent of 60%.

5. **(a)** (i) Provisions for tax deduction at source under section 194BB @ 30% are attracted if the amount exceeds ₹ 5,000 in respect of income arising by way of winning a jackpot in horse races.

Tax to be deducted = ₹ 1,20,000 x 30% = ₹ 36,000

(ii) Provisions of tax deduction at source under section 194C are attracted in respect of payment by a firm to a sub-contractor. Under section 194C, tax is deductible at the time of credit or payment, whichever is earlier @ 1% if the payment is made to an individual or HUF and 2% for others.

As the sub-contractor is an individual and the aggregate amount credited/paid during the year is ₹ 4,20,000 hence, tax is deductible @ 1% on ₹ 4,20,000.

Tax to be deducted = ₹ 4,20,000 x 1% = ₹ 4,200

(iii) As per section 194-I, tax is to be deducted @ 2% on payment of rent for plant and machinery, only if the payment exceeds ₹ 1,80,000 during the financial year. Since rent of ₹ 1,75,000 paid by a partnership firm does not exceed ₹ 1,80,000, tax is not deductible.

(iv) Under section 194E, the person responsible for payment of any amount to a non-resident sportsman for contribution of articles relating to any game or sport in India in a newspaper shall deduct tax @ 20%. Further, since Brett Lee is a non-resident, education cess @2% and secondary and higher education cess @ 1% on TDS would also be added.

Therefore, tax to be deducted = ₹ 55,000 x 20.60% = ₹ 11,330.

(b) (i) A charitable trust having "advancement of any other object of general public utility" as its main object, will lose its status as a charitable trust for the previous year in which its receipts from commercial activities exceed ₹ 25 lakhs and therefore, would not be entitled to get benefit of exemption in respect of its income for that previous year, whether or not its registration is cancelled. When the receipts from commercial activities exceed ₹ 25 lakhs in any previous year, the denial of exemption for that year is compulsory by operation of law and is not dependent on cancellation of registration.

Since, in this case, the receipts of the charitable trust is ₹ 30 lakhs (which is in excess of ₹ 25 lakhs), it cannot claim the benefit of exemption in respect of its income.

(ii) The buyback of unlisted shares would attract additional income-tax under section 115QA in the hands of the domestic company, i.e., Alpha Ltd. in this case. Consequently, the income arising to Mr. Gurmeet in respect of such buyback of unlisted shares by Alpha Ltd. would be exempt under section 10(34A).

(c) (i) (a) For a currency, when exchanged from, or to, Indian Rupees (INR), the value shall be equal to the difference in the buying rate or the selling rate, as the case may be, and the Reserve Bank of India (RBI) reference rate for that currency at that time, multiplied by the total units of currency.

Hence, in the given case, value of taxable service would be as follows:-

(RBI reference rate for $ – Selling rate for $) × Total units of US $

= ₹ (62-60) × 10,000

= ₹ 20,000

(b) If the RBI reference rate for a currency is not available, the value shall be 1% of the gross amount of Indian Rupees provided or received, by the person changing the money.

Hence, in the given case, value of taxable service would be as follows:-

1% of ₹ (60 × 10,000)

= ₹ 6,000

(ii) Where neither of the currencies exchanged is Indian Rupee, the value shall be equal to 1% of the lesser of the two amounts the person changing the money would have received by converting any of the two currencies into Indian Rupee on that day at the reference rate provided by RBI.

Hence, in the given case, value of taxable service would be 1% of the lower of the following:-

(a)	US dollar converted into Indian rupees	= $ 10,000× ₹ 61
		= ₹ 6,10,000
(b)	UK pound converted into Indian rupees	= £ 5,000 × ₹ 100
		= ₹ 5,00,000
	Value of taxable service	= 1% of ₹ 5,00,000 = ₹ 5,000

(d) Computation of VAT payable:-

Stage	Particulars	VAT Liability	Less VAT Credit	Tax to Government
I	Medicines sold by Lifeline Medicaids Ltd. to Healers Pharmacy at ₹ 80,000	=80,000 × 4% = 3,200	--	3,200
II	Medicines sold by Healers Pharmacy to All Well Medicos at ₹ 92,000 (₹ 80,000 × 115%)	=92,000 × 4% = 3,680	3,200	480

III	Medicines sold by All Well to Cure Medicines at ₹ 1,10,400 (₹ 92,000 × 120%)	=1,10,400 × 4% = 4,416	3,680	736
IV	Medicines sold by Cure Medicines to ultimate consumers at ₹ 1,38,000 (₹ 1,10,400 ×125%)	=1,38,000 × 4% = 5,520	4,416	1,104

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

Particulars	₹	₹
1. Income from house property		
- House No.1	54,000	
- House No.2	(-) 15,000	39,000
2. Profits and gains of business or profession		
Profit from leather business	1,25,000	
Add: Bad debts recovered taxable under section 41(4)	48,500	
	1,73,500	
Less: Current year loss of textile business	(-) 55,000	
	1,18,500	
Less:- Brought forward business loss of textile business for A.Y.2011-12 set off against the business income of current year	87,500	
- Brought forward business loss of chemical business for A.Y.2012-13 set off against the business income of current year (upto the limit of profits available for set off)	31,000	Nil
3. Capital Gains		
Short-term capital gain		75,000
Gross Total Income		**1,14,000**
Less: Deduction under Chapter VI-A		
- Under section 80C – LIC premium paid		18,000
Total Income		**96,000**

Statement of losses to be carried forward to A.Y. 2015-16

Particulars	₹
Business loss of A.Y. 2012-13 to be carried forward under section 72	26,000
Long term capital loss of A.Y. 2014-15 to be carried forward under section 74	45,000

Notes:

(1) Share of profit from firm of ₹ 21,450 is exempt under section 10(2A).

(2) Long-term capital loss cannot be set-off against short-term capital gains. Therefore, it has to be carried forward to the next year to be set-off against long-term capital gains of that year.

(b) The contention of Mrs. Nirmal Aggarwal is valid in law. Yes, she can do so. An insurer carrying on life insurance business has the option to pay tax:

(i) on the gross premium charged from a policy holder reduced by the amount allocated for investment, or savings on behalf of policy holder, if such amount is intimated to the policy holder at the time of providing of service;

(ii) Where amount of the gross premium allocated for investment or savings on behalf of policy holder is not intimated to the policy holder at the time of providing of service:-

First year	on 3% of the gross amount of premium charged
Subsequent year	on 1.5% of the gross amount of premium charged

towards the discharge of his service tax liability instead of paying service tax at the rate of 12%.

However, such option shall not be available in cases where the entire premium paid by the policy holder is only towards risk cover in life insurance.

Hence, Mrs. Nirmal Aggarwal has the option to calculate service tax at a rate other than 12% as per the above provisions.

(c) **(i)** False, VAT is a multi-point tax where tax is imposed at each and every stage of sales and tax paid at the earlier stage is allowed as set-off.

(ii) True, VAT increases the working capital requirements and the interest burden. The tax is imposed or paid at various stages and not on last stage only. It increases the requirement of working capital and also the interest element as compared to single stage-last point taxation system.

7. (a) Computation of income chargeable to tax under the heads "Income from Other Sources" in hands of Smt. Shobha for A.Y. 2014-15

	Particulars	₹
(i)	Cash gifts of ₹ 2,20,000 received on the occasion of her marriage is not taxable since gifts received by an individual on the occasion of marriage is excluded under section 56(2)(vii), even if the same are from non-relatives.	Nil
(ii)	Even though mother's maternal uncle does not fall within the	Nil

	definition of "relative" under section 56(2)(vii), gift of ₹ 45,000 received from him by cheque is not chargeable to tax since the aggregate sum of money received by Smt. Shobha without consideration from non-relatives(other than on the occasion of marriage) during the previous year 2013-14 does not exceed ₹ 50,000.	
(iii)	Purchase of land for inadequate consideration on 01.01.2014 would attract the provisions of section 56(2)(vii). Where any immovable property is received for a consideration which is less than the stamp duty value of the property by an amount exceeding ₹ 50,000, the difference between the stamp duty value and consideration is chargeable to tax in the hands of Individual. Therefore, in the given case ₹ 75,000 is taxable in the hands of Smt. Shobha.	75,000
(iv)	Since shares are included in the definition of "property" and difference between the purchase value and fair market value of shares is ₹ 55,000 (₹ 1,27,000 - ₹ 72,000) i.e. it exceeds ₹ 50,000, the difference would be taxable under section 56(2)(vii).	55,000
Amount chargeable to tax		**1,30,000**

(b) **(i)** **Shares received without consideration from a friend, having FMV of ₹ 75,000 -** The period of holding shall be reckoned from the date on which the asset is received by Mr. A. The period of holding of the previous owner i.e. A's friend will not be included, since this case is covered under section 49(4) and not under section 49(1).

(ii) **Bonus shares -** The period of holding shall be reckoned from the date of allotment of bonus shares.

(c) **Computation of the value of taxable service and the service tax payable:**

Particulars	Amount ₹
Advances received from clients for which no service has been rendered so far (Note-1)	9,00,000
Demurrage charges recovered for use of the services beyond the agreed upon period (Note-2)	40,000
Advance forfeited for cancellation of an agreement to provide a service (Note-3)	4,00,000
Security deposits forfeited for damages done by service receiver owing to his negligence in the course of receiving a service (Note-2)	6,00,000
Payment received from Extron Ltd. (Note-4)	2,00,000
Total	21,40,000

Value of taxable service=₹ $21,40,000 \times \frac{100}{112.36}$	19,04,592
Service tax liability = =₹ $21,40,000 \times \frac{12.36}{112.36}$	2,35,408

Notes:

1. Advances received in July, 2013 shall be taxable in the month of receipt of advance only [Explanation to rule 3 of the Point of Taxation Rules, 2011].
2. As per rule 6 of the Service Tax Valuation (Determination of Value) Rules, 2006, following charges are includible in the value of taxable service:-
   (a) Demurrage charges recovered for use of the services beyond the period agreed upon.
   (b) Security deposits forfeited for damages done by service receiver in the course of receiving a service. However, if the forfeited deposits relate to accidental damages due to unforeseen actions not relatable to provision of service, then such forfeited deposits would be excluded.
3. Since service becomes taxable on an agreement to provide a service such forfeited deposits would represent consideration for the agreement that was entered into for provision of service. Hence, entire ₹ 4,00,000 would form part of taxable value.
4. Excess payment made as a result of a mistake, if not returned and retained by the service provider, becomes a part of the taxable value. Hence, entire ₹ 2,00,000 would form part of taxable value.

(d) The statement is valid. Under the VAT system, trust has been reposed on tax payers, as there will be no regular assessment of all VAT returns, but only a few VAT returns will be taken up for scrutiny assessment. In other cases, the return filed by the trader will be accepted. It will also not be seen whether proper records have been maintained by the trader. As a consequence, a check on compliance becomes essential. Chartered Accountants can ensure tax compliance by:-

(i) helping the client in systematic record keeping.

(ii) helping the client in interpretation of the provisions of VAT law, and

(iii) performing audit of VAT accounts.

(iv) reporting the under-assessment, if any, made by the dealer requiring additional payment or

(v) reporting any excess payment of tax warranting refund to the tax payers.