Test Series: April, 2014

MOCK TEST PAPER – 2

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

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

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

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

Working Notes should form part of the answer.

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

1. (a) A plant was depreciated under two different methods as under:

Year	S.L.M (₹ in lakhs)	W.D.V. (₹ in lakhs)
1	39.00	106.90
2	39.00	79.00
3	39.00	58.40
4	39.00	43.20
	156.00	287.50
5	39.00	31.90

What should be the amount of resultant surplus/deficiency, if the company decides to switch over from W.D.V. method to S.L.M for first four years?

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

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

(c) Bell Co. Ltd. submits the following information pertaining to year 2012-2013. Using the given data, you are required to prepare Cash Flow Statement for the year ended 31st March, 2013 by indirect method.

	(₹ in millions)
Opening balance of cash and cash equivalents	1.55
Additional shares issued	6.50
Capital expenditure	9.90
Proceeds from assets sold	1.60
Dividend paid	0.50
Loss from disposal of assets	1.20
Net profit for the year	3.30
Increase in Accounts Receivable	1.50
Redemption of 4.5% debentures	2.50
Depreciation and Amortization	0.75

(d) Dox owes Wax ₹ 2,000 on 1st April, 2012. From 1st April, 2012 to 30th June, 2012 the following further transactions took place between Dox and Wax:

April 10 Dox buys goods from Wax for ₹ 5,000

May 16 Dox receives cash loan of ₹ 10,000 from Wax

June 9 Dox buys goods from Wax for ₹ 3,000

Dox pays the whole amount, together with interest @ 15% per annum, to Wax on 30th June, 2012. Calculate the interest paid by Dox on 30th June, 2012 by the average due-date method. *(4 x 5 = 20 Marks)*

2. The shareholders of Maitri Ltd. decided on a corporate restructuring exercise necessitated because of economic recession. From the given summarised balance sheet as on 31-3-2012 and the information supplied, you are required to prepare (i) Journal entries reflecting the scheme of reconstruction, (ii) Capital reduction account, (iii) Cash account in the books of Maitri Ltd.

Summarised Balance Sheet of Maitri Ltd. as on 31.3.2012

Liabilities	₹	*Assets*	₹
Share Capital		Fixed Assets	
30,000 Equity shares of ₹ 10 each	3,00,000	Trademarks and Patents	1,10,000
40,000 8% Cumulative Preference shares ₹ 10 each	4,00,000	Goodwill at cost	36,100
		Freehold Land	1,20,000
Reserves and Surplus		Freehold Premises	2,44,000
Securities Premium Account	10,000	Plant and Equipment	3,20,000

Profit and Loss Account	(1,38,400)	Investment (marked to market)	64,000
Secured Borrowings		Current Assets	
9% Debentures (₹100) 1,20,000		Inventories:	
Accrued Interest 5,400	1,25,400	Raw materials and	
Current liabilities		packing materials 60,000	
Trade payables	1,20,000		
Vat payable	50,000	Finished goods 16,000	76,000
Temporary bank overdraft	2,23,100	Trade receivables	1,20,000
	10,90,100		10,90,100

Note: Preference dividends are in arrears for 4 years.

The scheme of reconstruction that received the permission of the Court was on the following lines:

(1) The authorized capital of the Company to be re-fixed at ₹ 10 lakhs (preference capital of ₹ 3 lakhs and equity capital of ₹ 7 lakhs). Both classes of shares are of ₹ 10 each.

(2) The preference shares are to be reduced to ₹ 5 each and equity shares reduced by ₹ 3 per share. Post reduction, both classes of shares to be re-consolidated into ₹ 10 shares.

(3) Trade Investments are to be liquidated in open market.

(4) One fresh equity shares of ₹ 10 to be issued for every ₹ 40 of preference dividends in arrears (ignore taxation).

(5) Expenses for the scheme were ₹ 10,000.

(6) The debenture holders took over freehold land at ₹ 2,10,000 and settled the balance after adjusting their dues.

(7) Unprovided contingent liabilities were settled at ₹ 54,000 and a pending insurance claim receivable settled at ₹ 12,500.

(8) The intangible assets were all to be written off along with ₹ 10,000 worth obsolete packing material and 10% of the receivables.

(9) Remaining cash available as a result of the above transactions is to be utilized to pay off the bank overdraft to that extent.

(10) The Equity shareholders agree that they will bring in necessary cash to liquidate the balance outstanding on the overdraft account by subscribing the fresh shares. The equity shares will be issued at par for this purpose. *(16 Marks)*

3. (a) Shyam keeps his books of account by single entry system. However, he is able to give you the following lists of his assets and liabilities in the beginning as well as at the end of the year ended 31st March, 2013:

	On 1st April, 2012 ₹	On 31st March, 2013 ₹
Cash in hand	1,750	1,400
Cash at bank	20,000	-
Bank Overdraft	-	1,800
Bills Receivable	15,000	25,000
Stock	93,500	98,700
Debtors	60,000	70,000
Furniture and Fittings	65,000	65,000
Creditors	45,000	31,000
Bills Payable	5,000	Nil

Shyam introduced ₹ 10,000 as fresh capital on 1st October, 2012. He also withdrew ₹ 5,000 every month for his household expenses.

During the year, there was no sale or fresh purchase of furniture and fittings. Ascertain the profit earned by Shyam during the year ended 31st March, 2013 after depreciating furniture and fittings @ 10% per annum and creating a provision for bad debts @ 5% on debtors.

(b) How will you disclose the following in the Financial Statements of a Non-Profit Organisation?

Salaries paid during 2012 were ₹ 42,00,000. The following further information is available.

	₹	
Salaries unpaid on 31st Dec. 2011	1,70,000	
Salaries prepaid on 31st Dec. 2011	65,000	
Salaries unpaid on 31st Dec. 2012	2,30,000	
Salaries prepaid on 31st Dec. 2012	95,000	*(10 + 6= 16 Marks)*

4. The following is the Trial Balance of Omega Limited as on 31.3.2012:

(Figures in ₹ '000)

	Debit		*Credit*
Land at cost	220	Equity Capital (Shares of ₹ 10 each)	300

Plant & Machinery at cost	770	10% Debentures	200
Trade Receivables	96	General Reserve	130
Inventories (31.3.12)	86	Profit & Loss A/c	72
Bank	20	Securities Premium	40
Adjusted Purchases	320	Sales	700
Factory Expenses	60	Trade Payables	52
Administration Expenses	30	Provision for Depreciation	172
Selling Expenses	30	Suspense Account	4
Debenture Interest	20		
Interim Dividend Paid	18		
	1670		1670

Additional Information:

(i) The authorised share capital of the company is 40,000 shares of ₹ 10 each.

(ii) The company on the advice of independent valuer wish to revalue the land at ₹ 3,60,000.

(iiii) Proposed final dividend @ 10%.

(iv) Suspense account of ₹ 4,000 represents cash received for the sale of some of the machinery on 1.4.11. The cost of the machinery was ₹ 10,000 and the accumulated depreciation thereon being ₹ 8,000.

(v) Depreciation is to be provided on plant and machinery at 10% on cost.

You are required to prepare Omega Limited's Balance Sheet as on 31.3.2012 and Statement of Profit and Loss for the year ended 31.3.2012 as per Revised Schedule VI. Ignore previous years' figures & taxation. . *(16 Marks)*

5. (a) The following information is extracted from a set of books of Mr. Vasu for the year ended 31st December, 2012:

	₹
Sales	11,26,000
Purchases	6,44,000
Returns outward	15,200
Cash received from debtors	3,68,400
Bills payable accepted	2,40,000

Returns inward	33,600
Cash paid to creditors	3,60,000
Bills receivable received	3,20,000
Discounts received	8,400
Bad debts written off	24,000
Discount allowed	21,600

The total of the sales ledger balances on 1st Jan, 2012 was ₹ 6,41,600 and that of the purchases ledger balances on the same date was ₹ 3,72,800.

Prepare Sales Ledger and Purchases Ledger Adjustment Accounts in the General Ledger from the above information.

(b) On 1.4.2012, Ms. Priya purchased 2,000 equity shares of ₹ 100 each in TELCO Ltd. @ ₹ 120 each from a Broker, who charged 2% brokerage. She incurred 50 paise per ₹ 100 as cost of shares transfer stamps. On 31.1.2013 Bonus was declared in the ratio of 1 : 2. Before and after the record date of bonus shares, the shares were quoted at ₹ 175 per share and ₹ 90 per share respectively. On 31.3.2013 Ms. Priya sold bonus shares to a Broker, who charged 2% brokerage.

Show the Investment Account in the books of Ms. Priya, who held the shares as Current assets and closing value of investments shall be made at Cost or Market value whichever is lower. *(8 + 8 = 16 Marks)*

6. X, Y and Z are in partnership sharing Profits and Losses in the ratio 2 : 2: 1. Partnership deed provides that all the partners are entitled to interest @ 9% per annum on fixed capital of ₹ 2,00,000 contributed in profit sharing ratio. Z is entitled for 10% commission of net profit after such commission, for special performance.

On 1.9.2012, it was decided to retire X on health grounds and admit A, son of X, as a partner with 1/5th share in Profit and Loss. Other decisions taken on this date were as follows:

(a) Firm's fixed capital to be raised to ₹ 3,00,000 and partners to maintain fixed capital in profit sharing ratio. Hence forth, interest on capital shall be paid @ 10% per annum.

(b) No commission to be paid to Z from 1.9.2012.

(c) Goodwill is assessed at ₹ 60,000 not to be shown in the books.

(d) X was paid ₹ 50,000 in cash on retirement.

(e) Balance claim payable to X was to be credited to A's fixed capital account and current account.

(f) Profit for the accounting year 2012-13 before interest on capital, Z's commission and depreciation was ₹ 1,80,000. Depreciation for the year amounted to ₹ 18,500 (inclusive of depreciation of ₹ 6,000 upto 1.9.2012).

You are required to prepare:

(i) Profit and Loss Appropriation account of the firm for the year ended 31st March, 2013.

(ii) Partners' Current accounts. *(16 Marks)*

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

(a) In the financial statements of the financial year 2011-12, Alpha Ltd. has mentioned in the notes to accounts that during financial year, 24,000 equity shares of ₹ 10 each were issued as fully paid bonus shares. However, the source from which these bonus shares were issued has not been disclosed. Is such non-disclosure a violation of the Revised Schedule VI to the Companies Act? Comment.

(b) Mr. A gives you the following information:

	₹
Turnover in last financial year	6,00,000
Standing charges in last financial year	1,20,000

Net profit earned in last year was 15% of turnover and the same trend expected in subsequent year. Increase in turnover is expected at the rate of 30%. To achieve additional sales, Mr. A will have to incur additional expenditure of ₹ 77,000.

He intends to take a loss of profit policy with indemnity period of 6 months. Advise him the policy amount which will be necessary to cover loss of profits.

(c) "Spread sheet is a very valuable accounting tool." Explain the significance of spread sheets keeping in view the current business requirements.

(d) M/s Omega & Co. (a partnership firm), had a turnover of ₹ 1.25 crores (excluding other income) and borrowings of ₹ 0.95 crores in the previous year. It wants to avail the exemptions available in application of Accounting Standards to non-corporate entities for the year ended 31.3.2013. Advise the management of M/s Omega & Co in respect of the exemptions of provisions of ASs, as per the directive issued by the ICAI.

(e) Following items appear in the trial balance of Bharat Ltd. as on 31st March, 2012:

	₹
40,000 Equity shares of ₹ 10	4,00,000

Capital Reserve (including 30,000 being profit on sale of machinery)	75,000
Capital Redemption Reserve	25,000
Securities Premium	30,000
General Reserve	1,05,000
Surplus i.e. credit balance of Profit and Loss Account	50,000

The company decided to issue to equity shareholders bonus shares at the rate of 1 share for every 4 shares held and for this purpose, it decided that there should be the minimum reduction in free reserves. Pass necessary journal entries.

(4 x 4 =16 Marks)

Test Series: April, 2014

MOCK TEST PAPER - 2

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

SUGGESTED ANSWERS/HINTS

1. (a) As per para 15 of AS 6 on 'Depreciation Accounting', when a change in the method of depreciation is made, depreciation should be recalculated in accordance with the new method from the date of the asset coming into use. The deficiency or surplus arising from retrospective re-computation of depreciation in accordance with the new method should be adjusted in the accounts in the year in which the method of depreciation is changed.

In the given case, a surplus of ₹ 131.5 i.e. (287.50 – 156) on account of change in method of depreciation from WDV to SLM, will be credited to Statement of Profit and Loss.

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

(c) **Bell Co. Ltd.**

Cash Flow Statement for the year ended 31st March, 2013

	₹ in millions	₹ in millions
Cash flows from operating activities		
Net profit	3.30	
Add: Depreciation and amortization	0.75	
Loss from disposal of assets	1.20	
Operating profit before working capital changes	5.25	
Less: Increase in accounts receivables	(1.50)	
Net cash generated from operating activities		3.75

Cash flows from investing activities		
Capital expenditure	(9.90)	
Proceeds from sale of fixed assets	1.60	
Net cash used in investing activities		(8.30)
Cash flows from financing activities		
Proceeds from issue of additional shares	6.50	
Dividend paid	(0.50)	
Redemption of 4.5% debentures	(2.50)	
Net cash generated from financing activities		3.50
Net decrease in cash and cash equivalents		(1.05)
Cash and cash equivalents at beginning of the period		1.55
Cash and cash equivalents at end of the period (Balancing figure)		0.50

(d) Calculation of Average Due Date taking base date as April 1, 2012

Due dates	Amount ₹	No. of days from April 1, 2012	Products ₹
2012			
April 1	2,000	0	0
April 10	5,000	9	45,000
May 16	10,000	45	4,50,000
June 9	3,000	69	2,07,000
	20,000		7,02,000

Average due date = Base date +Days equal to $\frac{\text{Total of products}}{\text{Total amount}}$

Average due date = 1st April + $\frac{7,02,000}{20,000}$ =1st April + 35 days = 6th May, 2012

Interest payable on 30th June, 2012

Interest can be calculated on ₹ 20,000 from 7th May, 2012 to 30th June 2012. i.e. for 55 days @ 15% per annum.

Interest=20,000 x 15/100 x 55/366* = ₹ 451 (approx.)

* Year 2012 is a leap year.

2. **In the books of Maitri Ltd.**

Journal Entries

				Dr.	*Cr.*
	2012			₹	₹
1	March 31	Equity Share Capital A/c (₹ 10)	Dr.	3,00,000	
		To Capital Reduction A/c			90,000
		To Equity Share Capital A/c (₹ 7)			2,10,000
		(Being reduction of equity shares of ₹ 10 each to shares of ₹ 7 each as per Reconstruction Scheme dated...)			
2.		8% Cum. Preference Share Capital A/c (₹ 10)	Dr.	4,00,000	
		To Capital Reduction A/c			2,00,000
		To Preference Share Capital A/c (₹ 5)			2,00,000
		(Being reduction of preference shares of ₹ 10 each to shares of ₹ 5 each as per reconstruction scheme)			
3.		Equity Share Capital A/c (30,000 x ₹ 7)	Dr.	2,10,000	
		Preference Share Capital A/c (40,000 x ₹ 5)	Dr.	2,00,000	
		To Equity Share Capital A/c (21,000 x ₹ 10)			2,10,000
		To Preference Share Capital A/c (20,000 x ₹ 10)			2,00,000
		(Being post reduction, both classes of shares reconsolidated into ₹ 10 each) s			
4.		Cash Account	Dr.	64,000	
		To Trade Investments			64,000
		(Being trade investments liquidated in the open market)			
5.		Capital Reduction Account	Dr.	32,000	
		To Equity Share Capital Account			32,000
		(Being arrears of preference dividends of 4 years satisfied by the issue of 3,200 equity shares of ₹ 10 each)			

6.		Capital Reduction Account	Dr.	10,000	
		To Cash Account			10,000
		(Being expenses of reconstruction scheme paid in cash)			
7.		9% Debentures Account	Dr.	1,20,000	
		Accrued Interest Account	Dr.	5,400	
		To Debenture holders Account			1,25,400
		(Being amount due to debenture holders)			
8.		Debenture holders Account	Dr.	1,25,400	
		Cash Account (2,10,000 – 1,25,400)	Dr.	84,600	
		To Freehold Land			1,20,000
		To Capital Reduction Account (2,10,000 – 1,20,000)			90,000
		(Being Debenture holders took over freehold land at ₹ 2,10,000 and settled the balance)			
9.		Capital Reduction Account	Dr.	54,000	
		To Cash Account			54,000
		(Being contingent liability of ₹ 54,000 paid)			
10.		Cash Account	Dr.	12,500	
		To Capital Reduction Account			12,500
		(Being pending insurance claim received)			
11.		Capital Reduction Account	Dr.	1,68,100	
		To Trademarks and Patents			1,10,000
		To Goodwill			36,100
		To Raw materials & Packing materials			10,000
		To Trade receivables			12,000
		(Being intangible assets written off along with raw materials and packing materials worth ₹10,000 and 10% of trade receivables)			
12.		Cash Account	Dr.	1,26,000	
		To Equity Share Capital Account			1,26,000

		(Being 12,600 shares issued to existing shareholders)			
13.		Bank Overdraft Account	Dr.	2,23,100	
		To Cash Account			2,23,100
		(Being cash balance utilized to pay off bank overdraft)			
14.		Capital Reduction Account	Dr.	1,28,400	
		To Capital reserve Account			1,28,400
		(Being balance of capital reduction account transferred to capital reserve account)			

(ii) Capital Reduction Account

Particulars	₹	*Particulars*	₹
To Equity share capital	32,000	By Preference share capital	2,00,000
To Cash (contingent liability settled)	54,000	By Equity share capital	90,000
To Trademarks and Patents	1,10,000	By Freehold land	90,000
To Goodwill	36,100	By Cash (insurance claim)	12,500
To Raw material and Packing materials	10,000		
To Trade receivables	12,000		
To Cash account	10,000		
To Capital reserve account	<u>1,28,400</u>		
	<u>3,92,500</u>		<u>3,92,500</u>

(iii) Cash Account

Particulars	₹	*Particulars*		₹
To Investment	64,000	By Capital reduction (Contingent liability)		54,000
To 9% Debenture holders (2,10,000-1,25,400)	84,600	By Expenses		10,000
To Capital reduction (insurance claim)	12,500	By Temporary bank overdraft - From available cash (64,000+84,600+12,500 -54,000-10,000)	97,100	

To Equity share capital 12,600 shares @ ₹ 10 each	1,26,000	- From proceeds of equity share capital (2,23,100–97,100) 1,26,000	2,23,100
	2,87,100		2,87,100

Note: Shares issued to existing equity shareholders for bringing cash for payment of balance of bank overdraft = ₹ 2,23,100 – ₹ 97,100 = ₹ 1,26,000

3. (a) Statement of Affairs as on 1st April, 2012

	₹		₹
Creditors	45,000	Cash in Hand	1,750
Bills Payable	5,000	Cash at Bank	20,000
Capital (bal.fig.)	2,05,250	Bills Receivable	15,000
		Stock	93,500
		Debtors	60,000
		Furniture and Fittings	65,000
	2,55,250		2,55,250

Statement of Affairs as on 31st March, 2013

Liabilities	₹	*Assets*	₹	₹
Creditors	31,000	Cash in Hand		1,400
Bank Overdraft	1,800	Bills Receivable		25,000
Capital (bal.fig.)	2,17,300	Stock		98,700
		Debtors	70,000	
		Less: Provision for doubtful debts	(3,500)	66,500
		Furniture and fittings	65,000	
		Less: Depreciation	(6,500)	58,500
	2,50,100			2,50,100

Statement of Profit

	₹
Capital as on 31st March, 2013	2,17,300
Add: Drawings (₹ 5,000 x 12)	60,000
	2,77,300
Less: Additional capital	(10,000)
	2,67,300
Less: Capital as on 1st April, 2012	(2,05,250)
Profits during the year	62,050

(b) Calculation of Salary Expense

Particulars	₹
Salaries Paid	42,00,000
Add: Outstanding Salaries for 2012	2,30,000
Less:Unpaid Salaries of 2011 included in current year payment	(1,70,000)
Add: Prepaid Salaries as on 31st Dec. 2011	65,000
Less:Prepaid Salaries as at end of 2012	(95,000)
Salary Expense as per Income and Expenditure A/c	42,30,000

Disclosure in the Financial Statements

Income & Expenditure A/c (An extract) for the year ended 31st December, 2012

	₹		₹
To Salaries	42,30,000		

Balance Sheet as on 31st December, 2012 (An extract)

Liabilities	₹	*Assets*	₹
Outstanding salaries	2,30,000	Prepaid salaries	95,000

4. **Omega Limited**

Balance Sheet as at 31st March, 2012

Particulars	*Note No.*	*(` in 000)*
Equity and Liabilities		
1. Shareholders' funds		
a Share capital	1	300
b Reserves and Surplus	2	500
2. Non-Current liabilities		
a Long term borrowings	3	200
3. Current liabilities		
a Trade Payables		52
b Short-term provisions	4	30
Total		**1082**

Assets		
1. Non-current assets		
a Fixed assets		
i Tangible assets	5	880
2. Current assets		
a Inventories		86
b Trade receivables		96
c Cash and cash equivalents		20
Total		**1082**

Omega Limited

Statement of Profit and Loss for the year ended 31st March, 2012

	Particulars	*Notes*	*(` in 000)*
I.	Revenue from operations		700
II.	Other Income	6	2
III	**Total Revenue**		**702**
IV	Expenses:		
	Purchases		320
	Finance costs	7	20
	Depreciation (10% of 760)		76
	Other expenses	8	120
	Total Expenses		**536**
V.	**Profit (Loss) for the period** (III – IV)		**166**

Notes to accounts

			(₹ in 000)
1.	**Share Capital**		
	Equity share capital		
	Authorized		
	40,000 shares of ₹ 10 each		400
	Issued & subscribed & called up		
	30,000 shares of ₹ 10 each		300
	Total		**300**
2.	**Reserves and Surplus**		
	Securities Premium Account		40

	Revaluation reserve			140
	General reserve			130
	Profit & loss Balance			
	Opening balance	72		
	Profit for the period	166	238	
	Less: Appropriations			
	Interim Dividend		(18)	
	Proposed Final Dividend		(30)	190
				500
3.	**Long term borrowing**			
	10% Debentures			200
4.	**Short term provision**			
	Proposed Final Dividend			30
5.	**Tangible assets**			
	Land			
	Opening balance		220	
	Add: Revaluation adjustment		140	
	Closing balance			360
	Plant and Machinery			
	Opening balance		770	
	Less: Disposed off		(10)	
			760	
	Less: Depreciation (172-8+76)		(240)	
	Closing balance			520
	Total			880
6.	**Other Income**			
	Profit on sale of machinery:			
	Sale value of machinery		4	
	Less: Book value of machinery (10-8)		(2)	2
7.	**Finance costs**			
	Debenture interest			20
8.	**Other expenses:**			
	Factory expenses		60	

	Selling expenses	30	
	Administrative expenses	30	120

5. (a) Sales Ledger Adjustment Account

2012		₹	2012		₹
Jan. 1	To Balance b/d	6,41,600	Dec. 31	By General ledger adjustment A/c-	
Dec. 31	To General ledger adjustment A/c-	11,26,000		Cash	3,68,400
				Returns inward	33,600
	Sales			Bills receivable	3,20,000
				Bad debts	24,000
				Discounts allowed	21,600
			Dec. 31	By Balance c/d	10,00,000
		17,67,600			17,67,600

Purchases Ledger Adjustment Account

2012		₹	2012		₹
Dec. 31	To General ledger		Jan. 1	By Balance b/d	3,72,800
	adjustment A/c: Cash	3,60,000	Dec. 31	By General ledger adjustment A/c:	
	Returns outward	15,200		Purchases	6,44,000
	Bills payable	2,40,000			
	Discounts received	8,400			
Dec. 31	To Balance c/d	3,93,200			
		10,16,800			10,16,800

(b) **In the books of MS. Priya**

Investment Account

for the year ended 31st March, 2013

(Scrip: Equity Shares of TELCO Ltd.)

Date		*Particulars*	*Nominal Value (₹)*	*Cost (₹)*	*Date*	*Particulars*	*Nominal Value (₹)*	*Cost (₹)*
1.4.2012	To	Bank A/c	2,00,000	2,46,000	31.3.2013	By Bank A/c	1,00,000	88,200
31.1.2013	To	Bonus shares	1,00,000	–	31.3.2013	By Balance c/d	2,00,000	1,64,000
31.3.2013	To	Profit & loss A/c [(W.N.(iii)]	–	6,200				
			3,00,000	2,52,200			3,00,000	2,52,200

Working Notes:

(i) Cost of equity shares purchased on 1.4.2012 = 2,000 × ₹ 120 + 2% of ₹ 2,40,000 + ½% of ₹ 2,40,000 = ₹ 2,46,000

(ii) Sale proceeds of equity shares(bonus) sold on 31st March, 2013 = 1,000 × ₹ 90 – 2% of ₹ 90,000 = ₹ 88,200.

(iii) Profit on sale of bonus shares on 31st March, 2013

= Sales proceeds – Average cost

Sales proceeds = ₹ 88,200

Average cost = ₹ (2,46,000 × 1,00,000)/3,00,000 = ₹ 82,000

Profit = ₹ 88,200 – ₹ 82,000 = ₹ 6,200.

(iv) Valuation of equity shares on 31st March, 2013

Cost = (₹ 2,46,000 × 2,00,000)/3,00,000 = ₹ 1,64,000)

Market Value = 2,000 shares × ₹ 90 = ₹ 1,80,000

Closing balance has been valued at ₹ 1,64,000 being lower than the market value.

6. **Profit & Loss Appropriation Account**

for the year ended 31st March, 2013

	For the period			For the period	
	1.4.12 to 31.8.12	1.9.12 to 31.3.13		1.4.12 to 31.8.12	1.9.12 to 31.3.13
	₹	₹		₹	₹
To Interest on capital (W.N.3)	7,500	17,500	By Net Profit	75,000	1, 05,000
To Depreciation	6,000	12,500			
To Z's Commission (W.N.4)	5,591	-			
To Transfer to current A/c					
X	22,364	-			
Y	22,363	40,000			
Z	11,182	20,000			
A	-	15,000			
	75,000	1,05,000		75,000	1,05,000

Partners' Current Accounts

(From 1.4.12 to 31.8.12)

	X	Y	Z		X	Y	Z
	₹	₹	₹		₹	₹	₹
To X	-	16,000	8,000	By X's capital A/c (Transfer)	80,000	-	-
To Cash	50,000	-	-	By Interest on Capital	3,000	3,000	1,500
To A's Capital A/c	60,000	-	-	By Commission	-	-	5,591
To A's Current A/c	19,364	-	-	By Y	16,000	-	-
To Balance c/d		9,363	10,273	By Z	8,000		
				By P/L Appropriation Account	22,364	22,363	11,182
	1,29,364	25,363	18,273		1,29,364	25,363	18,273

Partners' Current Accounts

(From 1.9.12 to 31.3.13)

	Y ₹	Z ₹	A ₹		Y ₹	Z ₹	A ₹
To Y	-	-	8,000	By Balance b/d	9,363	10,273	
To Z	-	-	4,000	By X's Current A/c	-	-	19,364
To Balance c/d	66,696	38,940	25,864	By Interest on Capital	9,333	4,667	3,500
				By A	8,000	4,000	-
				By P/L Appropriation A/c	40,000	20,000	15,000
	66,696	38,940	37,864		66,696	38,940	37,864

Working Notes:

1. **New Profit sharing ratio and proportionate partners' capital as per new ratio:**

Fixed capital of the firm ₹ 3,00,000

New profit sharing ratio:

A is given 1/5 share

Balance share $1 - \frac{1}{5} = \frac{4}{5}$

$$\text{Y's share} = \frac{4}{5} \times \frac{2}{3} = \frac{8}{15}$$

$$\text{Z's share} = \frac{4}{5} \times \frac{1}{3} = \frac{4}{15}$$

New ratio

Y		Z		A	
$\frac{8}{15}$	:	$\frac{4}{15}$	:	$\frac{3}{15}$	or 8:4:3

Fixed capital of partners in profit sharing ratio will be

$$Y = \frac{3,00,000 \times 8}{15} = 1,60,000$$

$$Z = \frac{3,00,000 \times 4}{15} = 80,000$$

$$A = \frac{3,00,000 \times 3}{15} = 60,000$$

2. Goodwill adjustment at the time of retirement of X

	X ₹	Y ₹	Z ₹
Goodwill as per old ratio 2:2:1	24,000	24,000	12,000
Less : Goodwill in new ratio 2:1	—	(40,000)	(20,000)
	24,000	(16,000)	(8,000)

Goodwill adjustment at the time of admission of A

	Y ₹	Z ₹	A ₹
Goodwill in 2:1 (before admission)	40,000	20,000	——
Less : Goodwill in 8:4:3	(32,000)	(16,000)	(12,000)
	8,000	4,000	(12,000)

3. Interest on partners' capital

For the period from 1.4.2012 to 31.8.2012 (5 months)

X's capital ₹ 80,000 x 9% x $\frac{5}{12}$ = ₹ 3,000

Y's capital ₹ 80,000 x 9% x $\frac{5}{12}$ = ₹ 3,000

Z's capital ₹ 40,000 x 9% x $\frac{5}{12}$ = ₹ 1,500

Total = ₹ 7,500

For the period from 1.9.2012 to 31.3.2013 (7 months)

Y's capital ₹ 1,60,000 x 10% x $\frac{7}{12}$ = ₹ 9,333

Z's capital ₹ 80,000 x 10% x $\frac{7}{12}$ = ₹ 4,667

A's capital ₹ 60,000 x 10% x $\frac{7}{12}$ = ₹ 3,500

Total = ₹ 17,500

4. Commission payable to Z

Profit for the period 01.04.2012 to 31.8.2012 = 1,80,000 x $\frac{5}{12}$ = ₹ 75,000

Less: Depreciation for the period	₹ 6,000	
Interest on capital for the period	₹ 7,500	(₹ 13,500)

₹ 61,500

Commission to Z @ 10%

Net profit before commission	=	₹ 61,500
Profit after 10% commission	=	$\frac{61,500 \times 100}{110}$
	=	₹ 55,909
Commission @ 10%	=	₹ 5,591

7. **(a)** Revised Schedule VI has come into force for the Balance Sheet and Profit and Loss Account prepared for the financial year commencing on or after 1st April, 2011. As per Part I of the Revised Schedule VI, a company shall, inter alia, disclose in notes to accounts for the period of 5 years immediately preceding the balance sheet date (31st March, 2012 in the instant case) the aggregate number and class of shares allotted as fully paid-up bonus shares. Revised Schedule VI does not require a company to disclose the source from which bonus shares have been issued. Therefore, non-disclosure of source from which bonus shares have been issued does not violate the Revised Schedule VI to the Companies Act, 1956.

(b) **Calculation of policy amount to cover loss of profit**

	₹
Turnover in the last financial year	6,00,000
Add: 30% increase in turnover	1,80,000
	7,80,000
Gross profit on increased turnover (7,80,000 x 35%)	2,73,000
Add: Additional standing charges	77,000
Policy Amount	3,50,000

Therefore, the trader should take a loss of profit policy of ₹ 3,50,000.

(c) Spread sheets are used in various areas of current business requirements. Some of its important advantages as an accounting tool are as follows:

1. **Simple:** It is simple to use and easy to understand.
2. **Convenience:** Most of the common functions like doing calculations, setting formulas, macros, replication of cell contents, etc. can be easily done in a spread sheet.
3. **Grouping of heads:** Grouping and regrouping of accounts can be done.
4. **Presentations:** Presentation can be made in various forms including graphical presentations like bar diagram, histogram, pie-chart, etc.
5. **Security of data:** Basic protection like restricted access and password

protection of cell can be used to give security to the spread sheet data.

From the above discussion, it may be concluded spread sheet is a very valuable accounting tool.

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

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

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

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

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

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

(e) **Journal Entries in the books of Bharat Ltd.**

		Dr.	Cr.
		₹ in lakhs	*₹ in lakhs*
Capital Reserve A/c	Dr.	30,000	
Capital Redemption Reserve A/c	Dr.	25,000	
Securities Premium A/c	Dr.	30,000	
General Reserve A/c	Dr.	15,000	
To Bonus to Shareholders A/c			1,00,000
(Bonus issue of one share for every four shares			

held, by utilising various reserves as per Board's resolution dated…….)			
Bonus to Shareholders A/c	Dr.	1,00,000	
To Equity Share Capital A/c			1,00,000
(Capitalisation of profit)			

Note: Capital reserve amounting ₹ 30,000 realised in cash can only be used for bonus issue.

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)*

Test Series: April, 2014

Mock Test Paper – 2

INTERMEDIATE (IPC): GROUP – I

PAPER – 2: BUSINESS LAWS, ETHICS AND COMMUNICATION

SUGGESTED ANSWERS/HINTS

1. (a) The problem asked in the question is related to Cross offer which can be understood as, when two parties exchange identical offers in ignorance at the time of each other's offer, the offers are called cross offers.

According to the provisions given in the Indian Contract Act, 1872, when a person to whom proposal (offer) is made signifies his assent, the proposal is said to be accepted. Thus, assent can be only to a 'proposal'. If there was no proposal, question of its acceptance cannot arise.

Accordingly in the given case, H making a proposal to G to sell his car on the payment of ₹ 3 lacs and G, without knowing of the proposal of H, makes a proposal to G to purchase the same car at the price specified in the proposal of H. Thus, it is not an acceptance, as G was not aware of proposal made by H. It is only cross proposal (cross offer). And when two persons make offer to each other in this situation, it cannot be treated as mutual acceptance. Hence, there can be no binding contract in such a case.

Thus, the contention of G in the above case, is not tenable.

(b) According to the provisions of the Companies Act, 1956, a company may pay underwriting commission to any person who agrees to subscribe or procure subscription for an agreed number of shares or debentures of the company. Such commission may be paid to the underwriters who offer guarantee to procure applications for certain number of shares and guarantee to purchase the balance quantity of shares in case there is under subscription from the public. For this, the underwriter gets underwriting commission. Maximum total commission payable cannot exceed 5% of the price of shares or the underwriter may be paid a lower rate if so prescribed by articles. In case of debentures, it is 2½ % or a lower rate if so prescribed in the articles.

In the given problem the articles of Honest Automobiles Ltd., has prescribed 3% underwriting commission but the directors decided to pay 4% underwriting commission. The directors cannot do so because as aforesaid in the provision, such commission cannot be more than that prescribed in the articles. Therefore, the directors are not empowered to do so. Further, such amount of commission payable must be authorized by articles. The agreed commission should be disclosed in the prospectus or the statement in lieu of prospectus. Copy of the contract for payment of commission must be filed with Registrar of Companies at the time of the delivery of the prospectus or letter of offer. An underwriter must be also registered with SEBI.

(c) Group conflict : Group conflict is an 'express struggle' between two inter-dependent parties who perceive incompatible goals, scarce resources and interference from the other party in achieving their goals. There are two aspects in relation to conflict :

1. Expression : The two sides must communicate / express about the problem for there to be conflict.
2. Perception : Conflict evolves perceptions in the two sides may only perceive that their goals, resources and interference are incompatible with each other's.

Managing conflicts : The climate in which conflict is managed is important. It is essential to plan communications to foster a supportive climate, marked by emphasis on

i. Presenting ideas or options

ii. Problem orientation – focusing attention the task

iii. Spontaneity – Communicating openly and honestly

iv. Empathy – understanding another person's thoughts

v. Equality – asking for opinions

vi. Willing to listen to the ideas of others

Successfully managed conflicts can be constructive and can strengthen relationships in an organization.

(d) Environmental consideration has become a part of corporate strategy, which means incorporating environmental issues in the process of developing a product, in new investments and in the organizational set up. A good environmental practice improves corporate performance. In many industries it has been found that environmental friendly practices have resulted in more saving; for example the process of recycling the waste.

Thus, environmental considerations play a key role in corporate strategy. Markets of new millennium will be able to create wealth if they respond to the challenges sustainable development, as unsustainable products will become obsolete.

Thus, 'A good environmental practice improves corporate performance".

2. (a) (i) Recovery of the bonus due from an employer : As per the provisions of the Payment of Bonus Act, 1965, where an amount of bonus is due to an employee from his employer under a settlement or an award or agreement and it is not paid, there in such a case, the employee is to make an application for the recovery of the amount to the Appropriate Government.

This application can be made even by his assignee or heirs when the employee is dead. The application is to be made within one year from the date on which the money (Bonus) becomes due but it may be entertained even after the expiry of the said period of one year, if the Appropriate Government is satisfied that the applicant had sufficient cause for not making the application within the said period.

On receipt of the aforesaid application for the recovery of the bonus amount, the appropriate Government or such authority as it may specify in this connection is to be satisfied that the money is so due. On being thus satisfied, it must issue a certificate for that amount to the Collector. Thereupon, Collector shall proceed to recover the same in the same manner as an arrear of land revenue.

(ii) According to the Payment of Gratuity Act, 1972, where as soon as gratuity becomes payable, the employer shall, whether the application for the payment of gratuity has been given or not by the employee, determine the amount of gratuity and give notice in writing to the person to whom the gratuity is payable and also the controlling officer specifying the amount of gratuity so determined. The employer shall arrange to pay the amount of gratuity within 30 days from the date of its becoming due/ payable to the person to whom it is payable.

Provision of interest on gratuity amount : If the amount of gratuity is not paid by the employer within period specified i.e. 30 days, the employer shall pay, from the date on which the gratuity becomes payable to the date on which it is paid, simple interest at such rate, not exceeding the rate notified by the Central Government from time to time for repayment of long term deposits, as the Government may, by notification specify.

Thus, according to the above provisions, P will succeed to get the amount of gratuity along with the interest due.

(b) The term 'discrimination' generally means to distinguish one object from another or treating people differently. It is usually intended to refer to the wrongful act of making a difference in treatment or favour on a basis other than individual merit. Such discrimination may also be related in employment in business organization. The practices which create discrimination in a business organization may be summarized as follows :-

i. If the decision against one or more employees is taken which is not based on individual merit, such as the ability to perform a given job, seniority or other morally legitimate qualification.

ii. If the decision has been derived solely from racial or sexual prejudice, false stereotypes other kind of morally unjustified attitude against members of which the employee belongs.

iii. If the decision has a harmful or negative impact on the interests of the employees, perhaps costing them jobs, promotions or better pay.

(c) **(i)** The given statement is i**ncorrect**

Reason : In addition to oral communication, people can also relate and understand the non-verbal, by observing facial expressions, eye contact, gestures, postures etc., to understand the message better.

(ii) The given statement is **correct**

Reason : Communication is so fundamental that without it no organization can exist and function effectively towards achieving its objectives. Communication is the principal means by which members of an organisation work together.

(iii) The given statement is **correct**

Reason : An office order is a circular prepared and circulated for interdepartmental information to all the employees of the organization. Thus, it is correct that office order is meant for internal use.

(iv) The given statement is **correct**

Reason : A group is composed of individuals who interact verbally and non-verbally, occupy certain roles with respect to one another and co-operate to accomplish a definite goal. Thus, a group is like a tune, it is not constituted of individual sounds but the resulting symphony. Just like individuals, group also develops personality.

3. **(a)** As per the Negotiable Instruments Act, 1881, an alteration can be called a material alteration if it alters or attempts to alter the character of the instrument and affects or is likely to affect the contract which the instrument contains or is evidence of. Thus, it totally alters the business effect of the instrument. It makes the instrument speak a language other than that was intended.

The following material alterations have been authorized by the Act and do not require any authentication :

i. Filling blanks of inchoate instruments

ii. Conversion of a blank endorsement into an endorsement in full

iii. Crossing of cheque

As per the facts given in the question, B stated that he had paid the principal amount of ₹ 3,000/- to A and made endorsement on the back of the pronote which A erased and did a material alteration (total outstanding amount being ₹ 5,000/- that included a sum of ₹ 3,000/- as principal and the balance as interest).

The pronote consists of the principal and the interest amount which are important components of the debt. Erasure of the principal amount would alter the character of the instrument and affect the contract which the instrument contains or is evidence of. Thus, the erasure would be treated as material alteration.

Some of the grounds whereby the alteration will not be vitiate the pronote under Negotiable Instruments Act, 1881 are :

1. Conversion of instrument payable to bearer
2. Conversion of instrument payable to bearer into order
3. Elimination of the words 'or order' from an endorsement
4. Addition of the words 'or demand' to a note in which no time or payment is expressed.

(b) Following are the ancestry following different approaches of Ethical standards:

The Utilitarian Approach : The ethical corporate action is the one that produces the greatest good and does the least harm for all who are affected - customers, employees, shareholders, the community, and the environment. The utilitarian approach deals with consequences; it tries both to increase the good done and to reduce the harm done.

The Rights Approach (The Deontological Approach) : This approach starts from the belief that humans have a dignity based on their human nature per se or on their ability to choose freely what they do with their lives. On the basis of such dignity, they have a right to be treated as ends and not merely as means to other ends. The list of moral rights -including the rights to make one's own choices about what kind of life to lead, to be told the truth, not to be injured, to a degree of privacy, and so on. Also, it is often said that rights imply duties-in particular, the duty to respect others' rights.

The Fairness or Justice Approach : Aristotle and other Greek philosophers have contributed the idea that all equals should be treated equally. Today we use this idea to say that ethical actions treat all human beings equally-or if unequally, then fairly based on some standard that is defensible. We pay people more based on their harder work or the greater amount that they contribute to an organization, and say that is fair.

The Common Good Approach : This approach suggests that the interlocking relationships of society are the basis of ethical reasoning and that respect and compassion for all others-especially the vulnerable-are requirements of such reasoning. This approach also calls attention to the common conditions that are important to the welfare of everyone. This may be a system of Laws, effective police and fire departments, health care, a public educational system, or even public recreational areas.

The Virtue Approach : A very ancient approach to ethics is that ethical actions ought to be consistent with certain ideal virtues that provide for the full development of our humanity. These virtues are dispositions and habits that enable us to act according to the highest potential of our character and on behalf of values like truth and beauty. Honesty, courage, compassion, generosity, tolerance, love, fidelity, integrity, fairness, self-control, and prudence are all examples of virtues.

(c) Communication is a two-way process in which there is an exchange of ideas or thoughts linking the sender and receiver towards a mutually accepted direction or goal consisting of 7 elements which are as under:

1. **Sender:** The process of communication begins with a sender, the person who has an idea and desires to exchange it.
2. **Encoding:** The sender puts his/her ideas or facts into words, symbols, pictures or gestures that the receiver can understand.
3. **Message:** A message refers to what is being communicated. It may be verbal or non-verbal.
4. **Channel:** Channel is the medium through which message is transmitted to the sender. Channel may be in oral or written forms.
5. **Receiver:** It is any person who notices and attaches some meaning to a message.
6. **Decoding:** The receiver translates the words and symbols used in the message into ideas and interpret it to attain its meaning.
7. **Feedback:** Ultimately receiver reacts or responds to the communication sent by the sender. It could be based on clear interpretation of the symbols sent or misunderstanding or misinterpretation of the symbols sent.

4. (a) Return of Allotment (Section 75, Companies Act, 1956): Within thirty days of allotment of shares, a company is required to send the Registrar a report, known as the "return as to allotment". It must contain the following particulars:

1. The number of nominal amount of shares allotted; the names, addresses, the occupation of the allottees; the amount, if any, paid or payable on each share. No share should be shown as allotted for cash unless cash has actually been received in respect of the allotment.
2. Contracts in writing under which shares have been allotted for any consideration other than cash, must be produced for examination of the Registrar.
3. Where bonus shares have been issued, the returns must show the nominal amount of the shares allotted; names and addresses and occupations of the allottees and a copy of the resolution authorizing the issue of such shares.
4. Where the shares have been issued at a discount, the return must include a copy of the resolution authorizing such an issue, a copy of the Tribunal's order

sanctioning the issue, and where the rate of discount is more than ten percent, a copy of the order of the Central government permitting the issue.

(b) Economic growth has to be environmentally sustainable. There is no economic growth without ecological costs. Industrialization and rapid development have affected the environment. Everybody should realize that such development is related to environmental damage and resource depletion.

Therefore, an element of resource regeneration and positive approach to environment has to be incorporated in development programs. Sustainable development refers to maintaining development over time. Sustainable development is development that meets the needs of the present without comprising the ability of future generations to meet their own needs. A nation or society should satisfy its social, economic and other requirement without jeopardizing the interest of future generations.

High economic growth means high rate of extraction, transformation and utilization of non-renewable resources. Therefore it is suggested that economic growth has to be environmentally sustainable because it is sure that there is no economic growth without ecological cost.

(c) Personal Competencies Associated with Emotional Intelligence:

Personal Competencies – How You Manage Yourself

- *Emotional self-awareness*: Reading your own emotions and recognizing their impact; using 'gut sense' to guide decisions
- *Accurate self-assessment*: Knowing your strengths and weaknesses
- *Self-confidence:* A sound sense of your self-worth and capabilities
- *Self-Management*
- *Emotional self-control*: Keeping disruptive emotions and impulses under control
- *Transparency*: Displaying honesty and integrity; trustworthiness
- *Adaptability*: Flexibility in adapting to changing situations or overcoming obstacles
- *Achievement*: The drive to improve performance to meet inner standards of excellence
- *Initiative:* Readiness to act and seize opportunities
- *Optimism*: Seeing the upside in events

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

The officer can himself review the order on his own motion. [Section 7B(1)]. The officer can either reject the application for review if there are not sufficient grounds for review, or he can grant the review. [Section 7B(4)]. Appeal cannot be filed against order rejecting the application for review. However, if fresh order is passed after the review, appeal can be filed against such order [Section 7B(5)].Application for review should be made within 45 days in form 9. [Para 79A of EPF Scheme].

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

(b) **Mode of registration/incorporation of company:** In the case of a public company with or without limited liability any 7 or more persons can form a company by subscribing their names to memorandum and otherwise complying with the requirements of the Companies Act, 1956. In exactly the same way, 2 or more persons can form a private company [Section 12]. Persons who form the company, who conceive the idea of forming the company are known as promoters. They take all necessary step for its registration.

- **Lawful purpose:** The essence of validly incorporated company is that it must consist of a particular number of persons and be an association for a lawful purpose.
- **Applying for the name:** The promoters of the company should decide upon at least three suitable names in order of preference to afford flexibility to the Registrar to decide the availability of the name.
- **Documents to be filed:** After getting the name approved, the certain documents along with the application and prescribed fees, are to be filed with the Registrar.
- **Subscribing their names:** Section 15 stipulates that the Memorandum should be signed by each subscriber who should add his address, description and occupation in the presence of one witness.
- **Commencement of business**
- **Statement in Lieu of Prospectus: If** a public company does not issue a prospectus inviting the public to purchase its share because, the directors think they can sell the shares even without the issue of the prospectus, it can do so.
- **Certificate of incorporation:** Upon the registration of the documents mentioned earlier under the head “Documents to be filed for registration of the

company" and the payment of the necessary fees, the Registrar of Companies issues a certificate that the company is incorporated.

(c) Indemnity Bond

Mr. X, son of ………….resident of…………do hereby agree to indemnify the ABC bank Ltd., New Delhi for any loss that may occur on issuing a duplicate Demand Draft for a sum of ₹ 5,000/- (Rupees five thousand only).

I further declare that personally I have not encashed the Demand Draft in question.

Date : Signature

Place :

6 (a) (i) Period within which first and the subsequent AGM must be held :

(1) In accordance with the provisions of the Companies Act, 1956, the first Annual General Meeting of the company should be held within 18 months of incorporation of the company and so long as the company hold its first annual general meeting within that period, the company need not hold any general meeting in the year of incorporation or in the following year. Further, the date of the first AGM must be within 9 months from the date of the financial year for which profit and loss account has been made.

(2) Any subsequent AGM must be held not later than 6 months from the close of the financial year of the company. The gap between the two consecutive AGMs must not be more than 15 months. Further, the Registrar may, for any special reason, extend the time within which any AGM (not being the first AGM) shall be held by a period not exceeding 3 months.

(ii) Every AGM shall be called for a time during business, on a day that is not a public holiday, and shall be held either at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situate.

The Central Government may exempt any class of companies from the provisions of this subsection subject to such conditions as it may impose. Further, a public company or a private company which is a subsidiary of a public company, may by its articles fix the time for its AGM and may also by a resolution passed in one AGM fix the time for its subsequent AGMs.

(b) The dynamic environment in which businesses operate today may usher a broad range of circumstances because of which compliance the fundamental principles may potentially be threatened. Such threats may be classified as follows:

- Self-interest threats, which may occur as a result of the financial or other interests of a finance and accounting professional or of an immediate or close family member;
- Self-review threats, which may occur when a previous judgment needs to be re-evaluated by the finance and accounting professional responsible for that judgment;
- Advocacy threats occur when a professional promotes a position or opinion to the point that subsequent objectivity may be compromised;
- Familiarity threats occur when a finance and accounting professional has close relationships in the work environment and such relationships impair his selfless attitude towards work.
- Intimidation threats occur when a professional may be prohibited from acting objectively by threats, actual or perceived.

(c) A number of elements that can be used to describe or influence Organizational Culture:

- **The Paradigm:** What the organization is about; what it does; its mission; its values.
- **Control Systems**: The processes in place to monitor what is going on.
- **Organizational Structures**: Reporting lines, hierarchies, and the way that work flows through the business.
- **Power Structures**: Who makes the decisions and how power is distributed across the organization.
- **Symbols:** These include the logos and designs, but would extend to symbols of power, such as car parking spaces and executive washrooms!
- **Rituals and Routines:** Management meetings, board reports and so on may become more habitual than necessary.
- **Stories and Myths:** build up about people and events, and convey a message about what is valued within the organization.

Communicating the corporate culture effectively is paramount. For example, at General Electric (GE), corporate values are so important to the company, that Jack Welch, the former legendary CEO of the company, had them inscribed and distributed to all GE employees at every level of the company.

7. (a) (i) Incorrect : A company is a juristic person with a perpetual succession. It never dies, nor does its life depend upon the life of its members. It is created by a process of law and can be put to an end only by the process of law. Members may come and go but the company can go on forever (until dissolved).

(ii) **Incorrect :** 'Shelf Prospectus' means a prospectus issued by any financial institution or bank for one or more issues of the securities or class of securities specified in that prospectus. Thus, banks other than scheduled banks may also issue shelf prospectus.

(iii) **Incorrect :** Though, a minor is not competent to contract, nothing in the Contract Act prevents him from making the other party bound to the minor. Thus, a promissory note duly executed in favour of a minor is not void and can be sued upon by him, because he though incompetent to contract, may yet accept a benefit.

(iv) **Correct :** The test to decide whether a statement is an 'offer' or 'invitation to offer' is to see the 'intention'. If a person who makes the statement has the intention to be bound by it as soon as the other accepts, he is making an offer. If he however intends to do some other act, he is making only an invitation to offer. Thus, the intention to be bound is the important thing, which is to be seen.

(b) Alteration of Share Capital : A limited company having a share capital may, if so authorized by its articles, alter its share capital in the following manner :-

i. by increasing its nominal capital by issuing new shares;

ii. by consolidating and dividing all or any of its share capital into shares of larger denomination;

iii. by converting fully paid-up shares into stock or vice versa;

iv. by sub-dividing its shares or any of them into shares of smaller amount;

v. by cancelling shares which have not been taken up and diminishing the amount of its share capital by the amount of the shares so cancelled.

The powers conferred by above points shall be exercised by passing an ordinary resolution of the company in a general meeting and shall not require to be confirmed by the Court.

(c) Quorum : In this case, the quorum for a general meeting is 7 members to be personally present. For the purpose of quorum, only those members are counted who are entitled to vote on resolution proposed to be passed in the meeting.

Some points to be considered while calculating the quorum are :

1. Only members present in person and not by proxy are to be counted. Hence, proxies whether they are members or not will have to be excluded, for the purpose of quorum.

2. If a company is a member of another company, it may authorize a person by resolution to act as its representative at a meeting of a latter company, then

such a person shall be deemed to be a member present in person and counted for the purpose of quorum.

3. Where two or more companies which are members of another company, appoint a single person as their representative then each such company will be counted as quorum at a meeting of the latter company.

4. The President of India or Governor of a State, if he is a member of a company, may appoint such a person as he thinks fit, to act as its representative at any meeting of the company. A person so appointed shall be deemed to be a member of such a company and thus considered as member personally present.

With respect to the question, the following may be considered :

i. 'A' will be included for the purpose of quorum

ii. D will have three votes for the purpose of quorum as he represents three companies P. Ltd. Q. Ltd. and R. Ltd.,

iii. E will have two votes for the purpose of quorum as he represents two companies S. Ltd. and T. Ltd.

iv. F, G, H and I are not to be included as they are not members but representing as proxies for the members.

Thus, the number of persons being personally present would be as follows :-

Present Personally	Number
Mr. A	1
Mr. B & Mr. C	Nil
Mr. D	3
Mr. E	2
Proxies	Nil
Total	6

Thus, it can be said that a valid quorum for the Extra-ordinary General Meeting was not present.

(d) Letter of acknowledging the acceptance of the cheque book

The Manager,

-----------------bank,

---------New Delhi Date------------

Dear sir,

This is to acknowledge the acceptance of the Cheque book containing 20 cheques from no. 123450 to 123470 which I found to be correct.

Yours faithfully,

XYZ

(Customer)

(e) Legal drafting is of great importance to a person for entering into various types of agreements with different parties and in executing various types of documents in favour of the other.

This Legal drafting is a technical writing used by lawyers, judges, legislators and others in law to express legal analysis and legal rights, privileges, functions, status and duties.

Drafting is of importance for the three reasons:

(i) For obtaining legal consultations

(ii) For carrying out documentation

(iii) For interpretation of the documents

Legal Drafting have been catagorised into three forms-

1. Document
2. Instrument
3. Deed

MOCK TEST PAPER – 2

INTERMEDIATE (IPC): GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – I : COST ACCOUNTING

Suggested Answers/ Hints

1. (a) (i) Standard input (kg.) of Material SW:

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

Or, ₹ 600 Adverse = ₹ 30 (SQ – 140)

Or, -600 = 30 SQ – 4,200

Or, SQ = 120 kgs.

(ii) Actual Input (kg.) of Material MW:

Let, the actual input for Material MW is X kg.

(We also assume that proportion between the two materials required for production is 1:1)

Material Mix Variance = Std. Price (Actual Quantity in Std. mix – Actual Quantity)

Material Mix Variance (MW+SW) = Material Mix Variance for Material MW + Material Mix Variance for Material SW

$$\text{Or,}\quad -90 = [₹24\{(\frac{X+140\text{kg.}}{2})-X\}]+[₹30\{(\frac{X+140\text{kg.}}{2})-140\text{kg.}\}]$$

$$\text{Or,}\quad -90 = [₹24\{\frac{X+140-2X}{2}\}]+[₹30\{\frac{X+140-280}{2}\}]$$

$$\text{Or,}\quad -90 = [₹24\{\frac{140-X}{2}\}]+[₹30\{\frac{X-140}{2}\}]$$

$$\text{Or,}\quad -90 = [-12X+1,680]+[\frac{30X-4,200}{2}]$$

$$\text{Or,}\quad -90 = [\frac{-24X+3,360+30X-4,200}{2}]$$

$$\text{Or,}\quad -180 = 6X-840$$

Or, X $= \frac{660}{6} = 110$ kg.

(iii) (a) Material Price Variance of MW = Actual Quantity (Std. Rate – Actual Rate)

= 110 kg. (₹ 24 – ₹ 30) = ₹ 660 Adverse

(b) Material Price Variance of SW = 140 kg. (₹ 30 – ₹ 40) = ₹ 1,400 Adverse

(iv) Material Usage Variance of MW = Std. Rate (Std. Quantity – Actual Quantity)

= ₹ 24 (100 kg. – 110 kg.) = ₹ 240 Adverse

(v) (a) Material Cost Variance of MW = Standard Cost – Actual Cost

= (100 kg. × ₹ 24) – (110 kg. × ₹ 30)

= 2,400 – 3,300 = ₹ 900 Adverse

(b) Material Cost variance of SW = (120 kg. × ₹ 30) – (140 kg. × ₹ 40)

= 3,600 – 5,600 = ₹ 2,000 Adverse

(b) (i) **Computation of Break-even Point (BEP) for each factory.**

Sl. No.		Factory A (₹)	Factory B (₹)
A	Selling Price per packet	80	80
B	Variable Cost per packet	65	68
C	Contribution per packet [A - B]	15	12
D	P/V ratio [C ÷ A x 100] (%)	18.75	15
E	Fixed Cost	3,60,000	3,00,000
F	BEP (units) [E ÷ C]	24,000	25,000
G	BEP (Sales) [E ÷ D]	19,20,000	20,00,000

(ii) Cash BEP (units) $= \frac{\text{Fixed Cost} - \text{Depreciation}}{\text{Contribution per unit}}$

Factory A $= \frac{₹3,60,000 - ₹60,000}{₹15}$ = 20,000 packets

Factory B $= \frac{₹3,00,000 - ₹30,000}{₹12}$ = 22,500 packets

(iii) Computation of Combined Break-even Point (units)

$$= \frac{\text{Combined Fixed Cost}}{\text{Combined Contribution per unit}}$$

$$= \frac{₹3,60,000 + ₹3,00,000}{₹15\frac{2}{5} + ₹12\frac{3}{5}}$$

$$= \frac{₹6,60,000}{₹13.20} = 50,000 \text{ packets}$$

2. **Raw Material Control Account**

	(₹)		(₹)
To Balance b/d	42,000	By WIP control A/c (Material issued to production)	21,000
To Cost Ledger Control A/c (Material purchased)	32,400	By Cost Ledger Control A/c (Credit note issued by supplier)	1,200
		By Cost Ledger Control A/c (Loss of materials)	1,000
		By Balance c/d	51,200
	74,400		74,400

Work in Progress Control Account

	(₹)		(₹)
To Balance b/d	16,000	By Finished Goods Control A/c	38,800
To Cost Ledger Control A/c (Factory overhead allocated)	11,500	By Cost Ledger Control A/c (Rejection of production)	1,300
To Cost Ledger Control A/c (Direct wages allocated)	19,300	By Balance c/d	27,700
To Raw Material Control A/c	21,000		
	67,800		67,800

Finished Goods Control Account

	(₹)		(₹)
To Balance b/d	24,000	By Cost Ledger Control A/c (Cost of goods sold)	46,000
To WIP Control A/c	38,800	By Balance c/d	20,200
To Cost Ledger Control A/c (Return inward)	3,400		
	66,200		66,200

Cost Ledger Control Account

	(₹)		(₹)
To Raw Material Control A/c (Credit note issued by supplier)	1,200	By Balance b/d	82,000
To Finished Stock Control A/c (Cost of goods sold)	46,000	By Raw Material Control A/c	32,400
To Raw Material Control A/c (Loss of stock)	1,000	By WIP Control A/c	11,500
To WIP Control A/c (Rejection of production)	1,300	By WIP Control A/c	19,300
To Balance c/d	99,100	By Finished Stock Control A/c (Return inward)	3,400
	1,48,600		1,48,600

3. Schedule of costs

	Amount (₹)	Amount (₹)
Cost incurred: Opening balance		8,00,000
During the year Material consumed:		
Opening Stock	80,000	
Add: Material delivered during the year	15,90,000	
	16,70,000	
Less: Closing stock	40,000	16,30,000
Wages		14,95,000
Hire of plant		2,86,000
Other expenses		2,30,000
Material discrepancy (Actual)		15,000
General overheads 5% of ₹ 57,20,000	2,86,000	
Less: Absorbed at the beginning of the year	35,000	2,51,000
		47,07,000
Estimated further cost to complete		5,72,000
Estimated Total Cost		52,79,000
Contract Price		65,00,000
Estimated Total Profit		12,21,000

(i) Profit to be transferred to Profit and loss account:

$$\text{Estimated Profit x } \frac{\text{Value of work certified}}{\text{Contract price}} \text{ x } \frac{\text{12 months}}{\text{15 months}}$$

$$= ₹\ 12{,}21{,}000 \times \frac{57{,}20{,}000}{65{,}00{,}000} \times \frac{12}{15} = ₹\ 8{,}59{,}584$$

(ii) If contract price was ₹ 80 lakhs and if no estimate has been made of costs to completion

Value of work certified at the end of year is ₹ 57,20,000 which is 71.5% of the contract price. In such case notional profit has to be calculated instead of estimated profit.

Value of work certified	₹ 57,20,000
Add: Cost of work not certified	₹ 1,20,000
	58,40,000
Less: Cost of work upto the end of year	47,07,000
Notional Profit	11,33,000

Recommendation in (i) above would be affected as follows:

The following formula is to applied for the profit to be credited to Costing Profit & loss A/c. for the year just ended.

$$\frac{2}{3} \times \text{Notional profit} \times \frac{12 \text{ months}}{15 \text{ months}} \times \frac{\text{Cash received}}{\text{Value of work certified}}$$

$$\frac{2}{3} \times 11{,}33{,}000 \times \frac{12}{15} \times \frac{90}{100} = ₹\ 5{,}43{,}840$$

4. Primary Distribution of Overheads

Item	Basis	Total Amount (₹)	Production Departments			Service Departments	
			X (₹)	Y (₹)	Z (₹)	A (₹)	B (₹)
Indirect Material	Actual	1,25,000	20,000	30,000	45,000	25,000	5,000
Indirect Labour	Actual	2,60,000	45,000	50,000	70,000	60,000	35,000
Superintendent's Salary	Actual	96,000	-	-	96,000	-	-
Fuel & Heat	Radiator Sections {2:4:6:5:3}	15,000	1,500	3,000	4,500	3,750	2,250
Power	Kilowatt Hours {7:8:6:3:-}	1,80,000	52,500	60,000	45,000	22,500	-
Rent & Rates	Area (Sq. ft.) {22:20:15:12:6}	1,50,000	44,000	40,000	30,000	24,000	12,000

Insurance	Capital Value of Assets {4:6:5:1:2}	18,000	4,000	6,000	5,000	1,000	2,000
Meal Charges	No. of Employees {6:7:12:3:2}	60,000	12,000	14,000	24,000	6,000	4,000
Depreciation	Capital Value of Assets {4:6:5:1:2}	2,70,000	60,000	90,000	75,000	15,000	30,000
Total overheads		11,74,000	2,39,000	2,93,000	3,94,500	1,57,250	90,250

Re-distribution of Overheads of Service Department A and B

Total overheads of Service Departments may be distributed using simultaneous equation method

Let, the total overheads of A = a and the total overheads of B= b

a = 1,57,250 + 0.10 b (i)

or, 10a - b = 15,72,500 [(i) x10]

b = 90,250 + 0.20 a (ii)

or, -0.20a + b = 90,250

$$\begin{aligned} 10a - \cancel{b} &= 15,72,500 \\ -0.20a + \cancel{b} &= 90,250 \\ \hline 9.8a &= 16,62,750 \end{aligned}$$

a = 1,69,668

Putting the value of 'a' in equation (ii), we get

b = 90,250 + 0.20 x 1,69,668

b = 1,24,184

Secondary Distribution of Overheads

	Production Departments		
	X (₹)	**Y (₹)**	**Z (₹)**
Total overhead as per primary distribution	2,39,000	2,93,000	3,94,500
Service Department A (80% of 1,69,668)	50,900	50,900	33,934
Service Department B (90% of 1,24,184)	31,046	49,674	31,046
Total	3,20,946	3,93,574	4,59,480

5. (a)

Bills of Material	Material Requisition Note
1. It is document by the drawing office/ planning department.	1. It is prepared by the foreman of the consuming department.
2. It is a complete schedule of component parts and raw materials required for a particular job or work order.	2. It is a document authorizing Store-Keeper to issue material to the consuming department.
3. It often serves the purpose of a Store Requisition as it shows the complete schedule of materials required for a particular job i.e. it can replace stores requisition.	3. It cannot replace a Bill of Material.
4. It can be used for the purpose of quotation	4. It is useful in arriving historical cost only.
5. It helps in keeping a quantitative control on materials draw through stores requisition.	5. It shows the material actually drawn from stores.

(b) Difference between Cost Control and Cost Reduction

(1) Cost control aims at maintaining the costs in accordance with the established standards. While cost reduction is concerned with reducing costs.

(2) Cost control seeks to attain lowest possible cost under existing conditions, while cost reduction recognizes no condition as permanent, since a change will result in lower cost.

(3) In case of cost control, emphasis is on past and present, while in case of cost reduction, it is on present and future.

(4) Cost control is a preventive while cost reduction is corrective.

(5) Cost control ends when targets are achieved, while cost reduction has visible end.

6. (i) **Production Budget for the year 2014 by Quarters**

		I	II	III	IV	Total
	Sales demand(Unit)	24,000	26,000	28,000	31,000	1,09,000
I	Opening Stock	8,000	8,600	9,200	10,100	35,900
II	70% of Current Quarter 's Demand	16,800	18,200	19,600	21,700	76,300

III	30% of Following Quarter's Demand	7,800	8,400	9,300	8,200*	33,700
IV	Total Production(II &III)	24,600	26,600	28,900	29,900	1,10,000
V	Closing Stock (I+IV-Sales)	8,600	9,200	10,100	9,000	36,900

*Balancing Figure

(ii) Break Even Point = Fixed Cost* ÷ PV Ratio#

= ₹ 2,40,000 ÷ 10.71% = ₹ 22,40,896

Or, Break Even Point = Fixed Cost ÷ Contribution per unit

= ₹ 2,40,000 ÷ ₹ 7.50 = 32,000 Units

*Fixed Cost = 1,20,000 hours × ₹ 2 = ₹ 2,40,000

#P/V Ratio = Contribution per unit ÷ Selling Price per unit

= ₹ 70 - ₹ 62.50 = ₹ 7.50) ÷ ₹ 70 × 100 =10.71%

Cumulative sales in the quarter II is 50,000 units which is more than BEP of 32,000 units, BEP achieved in II quarter.

7. (a) CVP Analysis:-Assumptions

(i) Changes in the levels of revenues and costs arise only because of changes in the number of products (or service) units produced and sold.

(ii) Total cost can be separated into two components: Fixed and variable

(iii) Graphically, the behaviour of total revenues and total cost are linear in relation to output level within a relevant range.

(iv) Selling price, variable cost per unit and total fixed costs are known and constant.

(v) All revenues and costs can be added, subtracted and compared without taking into account the time value of money.

(b) ABC analysis exercises discriminating control over different items of stores classified on the basis of investment involved in the inventory.

'A' category items consists of only a small proportion i.e. approximately 10% of total items of stores but needs huge investment. Say about 70% of inventory value, because of their high prices or heavy requirement.

'B' category items are relatively 20% of the total items of the stores. The proportion of investments requires is also approximately 20% of total inventory investment.

'C' category items do not require much investment. It may be about 10% total inventory value but they are nearly 70% of the total items of stores.

Test Series: April, 2014

MOCK TEST PAPER – 2

IPCC: GROUP – I

PAPER – 3B: FINANCIAL MANAGEMENT

Suggested Answers/Hints

1. (a) The requirement is to identify the definition of Eurobonds.

(i) The statement is incorrect because Eurobonds are not always denominated in Eurodollars, which are US dollars deposited outside the US.

(ii) The statement is correct because Eurobonds are always sold in some country other than the one in whose currency the bond issue is denominated. The advantage of Eurobonds is that they are less regulated than other bonds and the transaction costs are lower.

(iii) The statement is incorrect because foreign bonds are denominated in the currency of the country in which they are sold.

(iv) The statement is incorrect because Eurobonds are usually issued not as registered bonds, but as bearer bonds.

(b) The requirement is to calculate the conversion period. The inventory conversion period is calculated as:

Inventory Conversion Period = Average Inventory / Sales per day

= ₹ 50,00,000 / (₹ 3,00,00,000 / 365)

= 60.83 days.

2. (a) Determination of Earnings per Share (EPS) in each alternative *(in ₹ Lakhs)*

Additional fund of ₹ 20 lakhs raised through	*Proposal (i) ordinary shares*	*Proposal (ii) ₹10 lakhs by ordinary shares & ₹ 10 lakhs by long-term loan @ 8% interest per annum*	*Proposal (iii) ₹ 5 lakhs by ordinary shares and ₹ 15 lakhs by long-term borrowing at 9% interest per annum*	*Proposal (iv) ₹ 10 lakhs by ordinary shares & ₹ 10 lakhs by preference shares with 5% dividend*
Earnings before interest and tax	8.00	8.00	8.00	8.00
Less: Interest		0.80	1.35	
Earnings before tax	8.00	7.20	6.65	8.00
Less: Tax @ 50%	4.00	3.60	3.33	4.00
Earnings after tax	4.00	3.60	3.32	4.00
Less: Preference				0.50

Shares dividend				
Earnings available for ordinary shareholders (A)	4.00	3.60	3.32	3.50
No. of Ordinary Shares (New Shares plus existing 25,000 shares): (B)	45,000	35,000	30,000	35,000
Earnings per share: (A)/(B)	8.89	10.29	11.07	10.00

Comment: The above analysis shows that Proposal (iii) gives the highest earning per share. It is on account of the following reasons:

(i) Rate of interest on loan is fixed and independent of the profit or loss and is treated as an expense by the Income Tax Authorities. Thus, the company's profit is taxed after deduction of this interest charge.

(ii) Dividend per share is more. It will, therefore, attract shareholders for further investment.

(iii) The borrowers are not the owners; hence there will be least interference from them in the management of the company.

(b) (i) **Liquidity ratios**

(a) Current ratio = CA/CL= ₹ 25,88,000/₹ 6,40,000 = 4.04 : 1 (previous year); ₹ 30,52,000/₹ 8,00,000 = 3.82 : 1 (current year)

(b) Acid test ratio = (₹ 25,88,000 – ₹18,68,000)/₹ 6,40,000 = 1.125 : 1 (previous year); (₹ 30,52,000 – ₹ 21,72,000)/₹ 8,00,000 = 1.1 : 1 (current year)

(ii) **Solvency ratios**

(a) *Debt-equity ratios*

(1) Total outside debts/Equity funds = ₹ 22,40,000/₹ 24,68,000 = 0.91 (previous year) ; ₹ 24,00,000/₹ 28,12,000 = 0.85 (current year)

(2) Long-term debts/Equity funds = ₹ 16,00,000/₹ 24,68,000 = 0.65 (previous year); ₹ 16,00,000/₹ 28,12,000 = 0.57 (current year)

(b) *Interest coverage ratio*

= EBIT/Interest charges = ₹12,00,000/₹1,60,000 =7.5 times (current ye *(iii)* **Profitability ratios (current year)**

(a) Gross profit ratio = (Gross profit/sales) × 100 = (₹ 12,00,000/₹ 40,00,000) × 100 = 30 per cent

(b) Net profit ratio = (Net profit/sales) × 100 = (₹ 6,76,000/₹ 40,00,000) × 100 = 16.9 per cent

(c) Return on total resources = (EAT + Interest – Tax savings on interest)/Total assets) × 100 = [(₹6,76,000 + ₹ 1,60,000 – ₹ 56,000)/₹ 64,00,000] × 100 = 12.2 per cent

(d) Return on capital employed = [(EAT + Interest – Tax savings on interest)/Total assets] × 100 = [(₹ 6,76,000 + ₹ 1,60,000 – ₹ 56,000)/44,12,000] × 100 = 17.7 per cent

(e) Return on equity funds = (Net profit after taxes/Equity funds) × 100 = (₹ 6,76,000/₹ 28,12,000) × 100 = 24 per cent.

Note : Ratios (c), (d) and (e) can also be determined by taking average total assets/capital employed/equity funds.

(iv) **Activity ratios**

(a) Debtors turnover = ₹ 40,00,000/₹ 3,60,000 = 11.1 times

(b) Stock turnover = ₹ 28,00,000/₹ 20,00,000 = 1.4 times

(c) Total assets turnover = ₹ 28,00,000/₹ 64,00,000 = 0.44 times

Comment: The company's position is quite sound from the point of view of liquidity, solvency and profitability. However, its activity ratios, particularly in terms of utilisation of total assets and holding of stocks, do not seem to be satisfactory.

3. (a)

Factor 10%	*Factor 20%*	*Project A*	*PV 10% ₹ lakhs*	*PV 20% ₹ lakhs*	*Project B*	*PV 10% ₹ lakhs*	*PV 20% ₹ lakhs*
1.00	1.00	(200)	(200.00)	(200.00)	(200)	(200.00)	(200.00)
0.91	0.83	35	31.85	29.05	218	198.38	180.94
0.83	0.69	80	66.40	55.20	10	8.30	6.90
0.75	0.58	90	67.50	52.20	10	7.50	5.80
0.68	0.48	75	51.00	36.00	4	2.72	1.92
0.62	0.40	20	12.40	8.00	3	1.86	1.20
		NPV	29.15	(19.55)	NPV	18.76	(3.24)

@10% NPV Project A = ₹ 29.15 lakhs

@10% NPV Project B = ₹ 18.76 lakhs

@20% NPV Project A = (₹19.55 lakhs)

@20% NPV Project B = (₹ 3.24 lakhs)

IRR Project A = 16%

IRR Project B = 18.5%

(i) **Recommendation:** Zeta Limited is advised to undertake Project A for the following reasons:

- ✓ It has a positive NPV, indicating that it exceeds the company's cost of capital
- ✓ Assuming that the company's objective is to maximise the present value of future cash flows A offers the higher NPV.

'A' offers a higher NPV, whereas 'B' offers a higher IRR. Where such conflicting indications appear it is generally appropriate to accept the NPV result, NPV being regarded as technically more sound than IRR.

(ii) The two projects have radically different time profiles. A's cash inflows are grouped in the middle three years of the project, while nearly 90 percent of B's inflows come in the first year of the project. This leads to B showing a higher IRR.

(b) (1) **Statement showing weighted average cost of capital**

(as per the existing capital structure)

Particulars	*₹*	*After-tax Cost*	*Weights*	*Weighted Cost*
Equity Share Capital	40,00,000	0.17	0.500	0.0850
Preference Share Capital	10,00,000	0.06	0.125	0.0075
Debentures	30,00,000	0.04	0.375	0.0150
Weighted Average Cost of Capital (K_0)				0.1075 or 10.75%

*The cost of equity shares is:

$$Ke = \frac{D}{MP} + g = \frac{₹\ 2}{₹\ 20} + 0.07 = 0.17 \text{ or } 17\%$$

(2) **Statement showing weighted average cost of capital**

(as per the proposed capital structure)

Particulars	*₹*	*After-tax Cost*	*Weights*	*Weighted Cost*
Equity Share Capital	40,00,000	0.27	0.40	0.108

6% Preference Share Capital	10,00,000	0.06	0.10	0.006
8% Debentures	30,00,000	0.04	0.30	0.012
10% Debentures	20,00,000	0.05	0.20	0.010
Weighted Average Cost of Capital (K_0)				0.136 or 13.60%

The cost of equity shares is:

$$Ke = \frac{D}{MP} + g = \frac{₹\ 3}{₹\ 15} + 0.07 = 27\%$$

(3) **Statement showing weighted average cost of capital**

Particulars	*₹*	*After-tax Cost*	*Weights*	*Weighted Cost*
Equity Share Capital	40,00,000	0.30	0.40	0.120
6% Preference Share Capital	10,00,000	0.06	0.10	0.006
8% Debentures	30,00,000	0.04	0.30	0.012
10% Debentures	20,00,000	0.05	0.20	0.010
Weighted Average Cost of Capital (K_0)				0.148 or 14.8%

$$\text{Cost of Equity Share} = \frac{D}{MP} + g = 0.20 + 0.10 = 30\%$$

4. **(a)** The requirement is to calculate the effective interest rate on a loan with a compensating balance requirement. The interest rate is calculated as follows:

$$\frac{\text{Interest cost}}{\text{Funds available}} = \frac{10\% \times ₹\ 5{,}00{,}000}{₹\ 5{,}00{,}000 - 50{,}000} = 11.1\%$$

(b) Calculation of Number of Days' Sales Outstanding

One-third of the customers take advantage of the 5% cash discount and pay on day ten. The remaining two-thirds of the customers pay on day 20. Average days' sales outstanding are calculated as:

Days' sales outstanding = (1/3) (10 days) + (2/3) (20 days) = 17 days.

MOCK TEST PAPER – 2

INTERMEDIATE (IPC): GROUP – I

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART – I : COST ACCOUNTING

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

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

Working notes should form part of the answer.

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

1. Answer the followings:

(a) The management accountant of MJ Pvt. Ltd. has found some data related with its two products 'MW' and 'SW'. With the help of data collected by the management accountant, compute the missing data indicated by the question marks:

Particulars	MW	SW
Standard Price per unit	₹ 24	₹ 30
Actual Price per unit	₹ 30	₹ 40
Standard Input (kg.)	100	?
Actual Input (kg.)	?	140
Material Price Variance	?	?
Material Usage Variance	?	₹ 600 Adverse
Material Cost Variance	?	?

Material Mix Variance for both products i.e. MW and SW together is ₹ 90 Adverse.

(b) Baby Care Ltd. has two factories for producing baby diapers of identical quality. The figures of year 2013-14 are as follows:

	Factory-A	Factory-B
Selling price per packet (₹)	80	80
Variable cost per packet (₹)	65	68
Fixed cost (₹)	3,60,000	3,00,000
Sales (packets)	70,000	80,000
Production capacity (packets)	80,000	90,000

Fixed cost includes depreciation on plant and machinery in factory A and factory B ₹ 60,000 and ₹ 30,000 respectively. You are required to calculate:

(i) Break-even Point (BEP) in sales and units for each factory separately.

(ii) Cash BEP in units for each factory separately.

(iii) BEP in units for company as a whole. Current product mix of factory A and factory B is 2:3. *(2 x 5 =10 Marks)*

2. The following balances were extracted from the cost books of M/s. ISBN Ltd. as on 31st Dec 2013.

	Dr. (₹)	Cr. (₹)
Raw materials control account	42,000	
Work-in-progress control account	16,000	
Finished stock control account	24,000	
Cost ledger control account		82,000
	82,000	82,000

Further transactions took place during the following quarter as follows:

	(₹)
Factory overhead-allocated to WIP	11,500
Goods finished-at cost	38,800
Raw materials purchased	32,400
Direct wages-allocated to WIP	19,300
Cost of goods sold	46,000
Raw materials-issued to production	21,000
Raw materials-Credit Note issued by supplier	1,200
Raw material losses detected by the Stock Auditor	1,000
WIP rejected (with no scrap value)	1,300
Customer's returns(at cost) of finished goods	3,400

Prepare all the Ledger Accounts in Cost Ledger *(8 Marks)*

3. NM Construction Ltd. has been constructing a flyover for 15 months and is under progress. The following information relating to the work on the contract has been prepared for the period ended 31st March, 2014.

	Amount (₹)
Contract price	65,00,000
Value of work certified at the end of the year	57,20,000
Cost of work not yet certified at the end of the year	1,20,000
Opening balances: Cost of work completed	8,00,000

Materials on site	80,000
Costs incurred during the year: Material delivered to site	 15,90,000
Wages	14,95,000
Hire of plant	2,86,000
Other expenses	2,30,000
Closing balance: Material on site	40,000

As soon as materials are delivered to the site, they are charged to the contract account. A record is kept on actual use basis, periodically a stock verification is made and any discrepancy between book stock and physical stock is transferred to a general contract material discrepancy account. The stock verification at the year end revealed a stock shortage of ₹ 15,000.

In addition to the direct charges listed above, general overheads are charged to contracts at 5% of the value of work certified. General overheads of ₹ 35,000 had been absorbed into the cost of work completed at the beginning of the year.

It has been estimated that further costs to complete the contract will be ₹ 5,72,000. This estimate includes the cost of materials on site at the end of the year (31.3.2014) and also a provision for rectification.

Required:

(i) Determine profitability of the above contract and recommend how much profit should be taken for the year just ended. (Provide a detailed schedule of costs).

(ii) State how your recommendation in (i) would be affected if the contract price was ₹ 80,00,000 (rather than ₹ 65,00,000), cash received is 90% of the value of work certified and if no estimate has been made of costs to completion. *(8 Marks)*

4. The following account balances and distribution of indirect charges are taken from the accounts of a manufacturing concern for the year ending on 31st March, 2014:

Item	**Total Amount**	**Production Departments**			**Service Departments**	
	(₹)	**X (₹)**	**Y (₹)**	**Z (₹)**	**A (₹)**	**B (₹)**
Indirect Material	1,25,000	20,000	30,000	45,000	25,000	5,000
Indirect Labour	2,60,000	45,000	50,000	70,000	60,000	35,000
Superintendent's Salary	96,000	-	-	96,000	-	-
Fuel & Heat	15,000					
Power	1,80,000					
Rent & Rates	1,50,000					
Insurance	18,000					

Meal Charges	60,000					
Depreciation	2,70,000					

The following departmental data are also available:

	Production Departments			Service Departments	
	X	Y	Z	A	B
Area (Sq. ft.)	4,400	4,000	3,000	2,400	1,200
Capital Value of Assets (₹)	4,00,000	6,00,000	5,00,000	1,00,000	2,00,000
Kilowatt Hours	3,500	4,000	3,000	1,500	-
Radiator Sections	20	40	60	50	30
No. of Employees	60	70	120	30	20

Expenses charged to the service departments are to be distributed to other departments by the following percentages:

	X	Y	Z	A	B
Department A	30	30	20	-	20
Department B	25	40	25	10	-

Prepare an overhead distribution statement to show the total overheads of production departments after re-apportioning service departments' overhead by using simultaneous equation method. Show all the calculations to the nearest rupee. *(8 Marks)*

5. Distinguish between:

   (a) Bill of Material and Material Requisition Note.

   (b) Cost Control and Cost Reduction. *(4 x 2 = 8 Marks)*

6. Arnav Limited produces and sells a single product. Sales budget for calendar year 2014 by a quarters is as under:

Quarters	I	II	III	IV
No. of units to be sold	24,000	26,000	28,000	31,000

The year is expected to open with an inventory of 8,000 units of finished products and close with inventory of 9,000 units. Production is customarily scheduled to provide for 70% of the current quarter's sales demand plus 30% of the following quarter demand. The budgeted selling price per unit is ₹ 70. The standard cost details for one unit of the product are as follows:

Variable Cost ₹ 62.50 per unit

Fixed Overheads 2 hours 30 minutes @ ₹ 2 per hour based on a budgeted production volume of 1,20,000 direct labour hours for the year. Fixed overheads are evenly distributed through-out the year.

You are required to:

(i) Prepare Quarterly Production Budget for the year.

(ii) In which quarter of the year, company expected to achieve break-even point.

(8 Marks)

7. (a) Discuss basic assumptions of Cost Volume Profit analysis.

   (b) Discuss ABC analysis as a system of inventory control *(4 x 2 =8 Marks)*

Test Series: April, 2014

MOCK TEST PAPER – 2

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 following:

   (a) Which of the following are characteristics of Euro-bonds? Answer supporting the same with reasons for each part below:

   (i) Are always denominated in Eurodollars.

   (ii) Are always sold in some country other than the one in whose currency the bond is denominated.

   (iii) Are sold outside the country of the borrower but are denominated in the currency of the country in which the issue is sold.

   (iv) Are generally issued as registered bonds.

   (b) Alpha Limited has ₹ 50,00,000 of average inventory and sales of ₹ 3,00,00,000. Using a 365 days year, you are required to calculate the firm's inventory conversion period. *(4+2 = 6 Marks)*

2. (a) Beta Limited has currently an ordinary share capital of ₹ 25 lakhs consisting of 25,000 shares of ₹ 100 each. The management is planning to raise another ₹ 20 lakhs to finance a major expansion programme through one of four possible financing plans. The plans are:

   (i) Entirely through ordinary shares.

   (ii) ₹ 10 lakhs through ordinary shares and ₹ 10 lakhs through long-term borrowings at 8 per cent interest per annum.

   (iii) ₹ 5 lakhs through ordinary shares and ₹ 15 lakhs through long-term borrowings at 9 per cent interest per annum.

   (iv) ₹ 10 lakhs through ordinary shares and ₹ 10 lakhs through preference shares with 5 percent dividend.

   The company's Earnings before Interest and Tax (EBIT) will be ₹ 8 lakhs. Assuming a corporate tax rate of 50 per cent, determine the earnings per share (EPS) in each alternative and comment on the implications of financial leverage.

(b) Gamma Limited's financial statements contain the following information:

	Previous year	*Current year*
Cash	₹ 2,00,000	₹ 1,60,000
Sundry debtors	3,20,000	4,00,000
Temporary investments	2,00,000	3,20,000
Stock	18,40,000	21,60,000
Pre-paid expenses	28,000	12, 000
Total current assets	25,88,000	30,52,000
Total assets	56,00,000	64,00,000
Current liabilities	6,40,000	8,00,000
10% Debentures	16,00,000	16,00,000
Equity share capital	20,00,000	20,00,000
Retained earnings	4,68,000	9,04,000

Statement of profit for the current year

Sales	₹ 40,00,000
Less : Cost of goods sold	28,00,000
Interest	1,60,000
Net profit	10,40,000
Less : Taxes (0.35)	3,64,000
Profit after taxes	6,76,000
Dividends declared on equity shares	2,20,000

From the above, appraise the financial position of Gamma Limited from the point of view of (i) liquidity, (ii) solvency (iii) profitability, and (iv) activity. *(12 + 8 = 20 Marks)*

3. (a) Two projects 'A' and 'B' having the same initial cash outflows and length of life are being evaluated by Zeta Limited. The projects are mutually exclusive and only one shall be undertaken by the company. The finance manager feels that the project with the higher NPV should be accepted whereas the managing director is of the opinion that the one with a higher IRR should be undertaken. The cost of capital for the company is 10 percent and the net cash flows of the project are as follows:

Year	*Project 'A' (₹ in lakhs)*	*Project 'B' (₹ in lakhs)*
0	(200)	(200)
1	35	218
2	80	10
3	90	10
4	75	4
5	20	3

You are required to:

(ii) Calculate the NPV and IRR of the two projects and recommend with reasons, which project you would undertake.

(ii) Explain the inconsistency in ranking of the two projects in view of the remarks by the finance manager and the managing director.

(b) Theta Limited has the following capital structure:

Equity Share Capital (2,00,000 shares)	₹ 40,00,000
6% Preference shares	10,00,000
8% Debentures	30,00,000
	80,00,000

The market price of the Theta Limited's equity share is ₹ 20. It is expected that it will pay a current dividend of ₹ 2 per share which will grow at 7 per cent forever. The tax rate may be presumed at 50 percent. You are required to compute the following:

(1) A weighted average cost of capital based on existing capital structure.

(2) The new weighted average cost of capital if the company raises an additional ₹ 20,00,000 debt by issuing 10 percent debentures. This would result in increasing the expected dividend to ₹ 3 and leave the growth rate unchanged but the price of share will fall to ₹ 15 per share.

(3) The cost of capital if in *(2)* above, growth rate increases to 10 percent.

(9+9= 18 Marks)

4. (a) If Mahalaxmi Limited borrows ₹ 5,00,000 at 10 percent and is required to maintain ₹ 50,000 as a minimum compensating balance at the bank. Calculate the effective interest rate on the loan?

(b) Ganpati Limited offers its customers credit terms of 5/10 net 20. One-third of the customers take the cash discount and the remaining customers pay on day 20. On average 20 units are sold per day, priced at ₹ 10,000 each. The rate of sales is uniform throughout the year. Using 360 days per year, compute Ganpati Limited's sales outstanding in accounts receivable, to the nearest full day. *(3+3 =6 Marks)*

Test Series: April, 2014

MOCK TEST PAPER – 2

INTERMEDIATE (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) Mr. Rakesh, a Deputy Manager (Production cell) working in Shriram Ltd., New Delhi, receives the following emoluments during the previous year 2013-14:

	₹		₹
Basic salary	2,25,000	Bonus	12,000
D.A. (not forming part of salary)	1,85,000	Medical allowance	8,000
Commission on extra production	15,000	Special allowance	14,000

Education Allowance (including allowance for hostel expenditure) for two sons who are engineering students at Mumbai - ₹ 18,000.

(i) His employer has provided rent free house to him in New Delhi. The house is owned by the employer.

(ii) Electricity bills paid by Shriram Ltd. for him during the previous year are of ₹ 13,500.

(iii) On 1.1.2014, his employer company has given him a CD player for domestic use and a laptop for office and personal use. Ownership of both the assets have not been transferred. The cost of CD player is ₹ 26,000 and that of laptop is ₹ 52,000.

(iv) He invested ₹ 60,000 during the previous year in PPF:

(v) He has paid tuition fees of his sons on 17.12.2013 of ₹ 54,000.

(vi) He has deposited ₹ 12,000 in Five Year Time Deposit Scheme in Post Office on 25.3.2014.

(vii) His agricultural income during the year is ₹ 3,05,000.

(viii) He has received gift of ₹ 28,000 from his grandfather on 10.6.2013.

(ix) He has gifted his car to his wife on 15.5.2013. She has earned income of ₹ 32,000 from the business of hiring the same during the previous year.

Compute the total income and tax payable of Mr. Rakesh for the A.Y. 2014-15. *(10 Marks)*

(b) Super Stable Bank Ltd. furnishes the following information relating to services provided and the gross amount received (excluding service tax):

Particulars	**Amount (₹)**
Commission charged for preparing pay orders	50,000
Administrative charges (over and above interest) on loans, advances and deposits	6,00,000
Interest on overdraft	5,00,000
Commission charged for sale of foreign exchange to general public	9,00,000
Interest on loans with a collateral security	6,00,000
Interest on corporate deposits	11,00,000

Compute the value of taxable service and the service tax liability of Super Stable Bank Ltd. considering the service tax @ 12%.

Note: Super Stable Bank Ltd. is not eligible for small service providers' exemption under *Notification No. 33/2012 – ST dated 20.06.2012.* *(5 Marks)*

(c) Dolphin Enterprises is a dealer in Gujarat and deals in consumer goods. It submits the following information pertaining to the month of January, 2014:

(i) Exempt goods 'X' purchased for ₹ 4,00,000 and sold for ₹ 4,50,000.

(ii) Goods 'Y' purchased for ₹ 3,00,000 (excluding VAT) and sold at a margin of 10% profit on purchase value (Input and output VAT rate is 12.5%).

(iii) Goods 'Z' purchased for ₹ 5,00,000 (excluding VAT) and sold for ₹ 7,00,000 (Input and output VAT rate is 4%);

(iv) His unutilized balance of VAT credit on 01.01.2014 was ₹ 6,000.

Compute the turnover, input VAT, output VAT and net VAT payable by Dolphin Enterprises. *(5 Marks)*

2. (a) Raghu Ltd., engaged in manufacture of medicines (pharmaceuticals), furnishes the following information for the year ended 31.03.2014:

(i) Municipal tax relating to office building ₹ 45,000 not paid till 30.09.2014.

(ii) Patent acquired for ₹ 25,00,000 on 01.06.2013 and used from the same month.

(iii) Capital expenditure on in-house scientific research ₹ 12,00,000 which includes cost of land ₹ 2,00,000.

(iv) Amount due from customer Raja, outstanding for more than 4 years, written off as bad debt in the books ₹ 4,00,000.

(v) Income-tax paid ₹ 1,10,000 by the company in respect of non-monetary perquisites provided to its employees.

(vi) Expenditure towards advertisement in souvenir of a political party ₹ 2,50,000.

(vii) Refund of sales tax ₹ 85,000 received during the year, which was claimed as expenditure in an earlier year.

State with reasons the taxability or deductibility of the items given above under the Income-tax Act, 1961. *(8 Marks)*

Note: *Computation of total income is not required.*

(b) ABC 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 March, 2014 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	50,000
Security deposits forfeited for damages done by service receiver owing to his negligence in the course of receiving a service	4,00,000

Besides, the above receipts, one of the clients-AVB Ltd. made a payment of ₹ 1,50,000 (out of which ₹ 35,000 were paid extra by mistake). However, ABC Private Limited refused to return the excess payment received.

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

(c) How can an auditor play a role to ensure that the tax payers discharge their tax liability properly under the VAT system? *(4 Marks)*

3. (a) Mr. Kamlesh borrowed a sum of ₹ 55 lakhs from the National Housing Bank towards purchase of a residential flat. The loan amount was disbursed directly to the flat promoter by the bank. Though the construction was completed in June, 2014, repayments towards principal and interest had been made during the year ended 31.3.2014.

In the light of the above facts, state:

(i) Whether Mr. Kamlesh can claim deduction under Section 24 in respect of interest for the assessment year 2014-15;

(ii) Whether deduction under Section 80C can be claimed for the above assessment year, even though the construction was completed only after the closure of the year? *(4 Marks)*

(b) State with reasons whether the following statements are true or false having regard to the provisions of the Income-tax Act, 1961:

(i) Capital gain of ₹ 65 lakh arising from transfer of long term capital assets on 11.6.2013 will be fully exempted from tax if such capital gain is invested in the bonds redeemable after three years, issued by NHAI under section 54EC.

(ii) As per section 49(2A), read with section 47(xa) of the Income-tax Act, 1961, no capital gains would arise on conversion of foreign currency exchangeable bonds into shares or debentures, for facilitating the issue of FCEBs by companies. *(4 Marks)*

(c) ABC Consultancy Ltd. provides management consultancy services to its client Vibhuti Industries for agreed consideration of ₹ 12,50,000. Vibhuti Industries makes the payment on 15th February, 2014. However, the date of completion of service is 5th February, 2014. Determine the point of taxation if the relevant invoice for ₹ 12,50,000 is raised by ABC Consultancy Ltd. on:

CASE I 20th February, 2014

CASE II 8th March, 2014

CASE III 10th February, 2014 *(4 Marks)*

(d) VAT chain is broken when a purchasing dealer opts for VAT composition scheme. Discuss the validity of the statement. What is the loss to the seller and buyer opting for the composition scheme, and the subsequent buyers? *(4 Marks)*

4. (a) Avinash, engaged in manufacture and wholesale trade, furnishes you the following information:

Total turnover for the financial year

Particulars	**₹**
2012-13	1,08,00,000
2013-14	95,00,000

State whether tax deduction at source provisions are attracted for the following expenses incurred during the financial year 2013-14:

Particulars	**₹**
Interest paid to SBI	47,000
Contract payment to Bala (2 contracts of ₹ 14,000 each)	28,000
Shop rent paid (one payee)	2,24,000
Commission paid to Lalu	9,500

(4 Marks)

(b) State with reasons whether you agree or disagree with the following statements:

(i) Return of income of Limited Liability Partnership (LLP) could be signed by any partner.

(ii) Time limit for filing return under section 139(1) in the case of Mr. Sameer having total turnover of ₹ 75 lakhs for the year ended 31.03.2014, whether or not opting to offer presumptive income under section 44AD, is 30th September 2014. *(4 Marks)*

(c) Mr. Jai, a service provider has collected service tax from a client, but is unable to perform the service. Briefly explain the conditions subject to which he can adjust the service tax so collected, against his forthcoming service tax liability. *(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	Blast Ltd. sold the crackers manufactured by it to the distributors of crackers- Bonanza Ltd. - at ₹ 60,000.	--
II	Bonanza Ltd. sold the crackers to the wholesalers – Pimpom Ltd.	20%
II	Pimpom Ltd. sold the crackers to the retailers - Fit Ltd.	25%
IV	Fit Ltd. sold the crackers to the ultimate consumers	30%

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

5. (a) Ms. Neena, a resident individual, provides the following details of her income/losses for the year ended 31.3.2014:

(i) Salary received as a partner from a partnership firm ₹ 8,37,000. The same was allowed as deduction in the hands of the firm.

(ii) Loss on sale of shares listed in BSE ₹ 2,50,000. Shares were held for 15 months and STT paid on sale.

(iii) Long-term capital gain on sale of land ₹ 5,75,000.

(iv) ₹ 53,000 received in cash from friends in party.

(v) ₹ 68,000, received towards dividend on listed equity shares of domestic companies.

(vi) Brought forward business loss of assessment year 2013-14 ₹ 10,39,000.

The return for assessment year 2013-14 was filed in time.

Compute gross total income of Ms. Neena for the Assessment Year 2014 -15 and ascertain the amount of loss that can be carried forward. *(6 Marks)*

(b) Under the Income Tax Act, 1961, is citizenship a criterion for determining the residential status of an individual? *(2 Marks)*

(c) A customer gets US \$ 2,00,000 converted into UK £ 1,00,000. RBI reference rate at that time for US \$ is ₹ 60 per US dollar and for UK £ is ₹ 100 per UK pound. Compute the value of taxable service as per rule 2B of the Service Tax (Determination of Value) Rules, 2006. *(4 Marks)*

(d) State the eligibility of purchases for input tax credit in the following cases:-

(i) Aggarwal & Co. purchased goods for using them in the execution of a works contract.

(ii) Sandeep purchased goods from Mandeep. Mandeep has not shown the amount of VAT paid by him separately in the invoice. *(4 Marks)*

6. (a) Mr. Aakash and Mr. Binoy constructed their houses on a piece of land purchased by them at Baroda. The built up area of each house was 1,500 sq.ft. ground floor and an equal area in the first floor. Aakash started construction on 1-04-2012 and completed on 1-04-2013. Binoy started the construction on 1-04-2012 and completed the construction on 30-06-2013. Aakash occupied the entire house on 01-04-2013. Binoy occupied the ground floor on 01-07-2013 and let out the first floor for a rent of ₹ 20,000 per month. However, the tenant vacated the house on 31-12-2013 and Binoy occupied the entire house during the period 01-01-2014 to 31-03-2014.

Following are the other information

(i)	Fair rental value of each unit (ground floor /first floor)	₹ 1,50,000 per annum
(ii)	Municipal value of each unit (ground floor / first floor)	₹ 80,000 per annum
(iii)	Municipal taxes paid by	Aakash – ₹ 10,000 Binoy – ₹ 10,000
(iv)	Repair and maintenance charges paid by	Aakash –₹ 35,000 Binoy – ₹ 40,000

Aakash has availed a housing loan of ₹ 25 lakhs @ 12% p.a. on 01-04-2012. Binoy has availed a housing loan of ₹ 15 lakhs @ 10% p.a. on 01-07-2012. No repayment was made by either of them till 31-03-2014. Compute income from house property for Aakash and Binoy for the previous year 2013-14 (A.Y. 2014-15). *(8 Marks)*

(b) 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 by RBI are not chargeable to service tax.

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

(iv) Duties performed by Members of Parliament and State Legislatures are liable to service tax. *(4 Marks)*

(c) State with reasons whether the following are true or false in the context of VAT:

(i) Taxpayer's Identification Number (TIN) is a 10 digit alpha numeral.

(ii) Self assessment concept on deemed basis is one of the important features of VAT. *(4 Marks)*

7. (a) Mr. Arnab is an individual carrying on business. His stock and machinery were damaged and destroyed in a fire accident.

The value of stock lost (total damaged) was ₹ 7,30,000. Certain portion of the machinery could be salvaged. The opening WDV of the block as on 1-4-2013 was ₹ 12,35,000.

During the process of safeguarding machinery and in the fire fighting operations, Mr. Arnab lost his gold chain and a diamond ring, which he had purchased in July, 2003 for ₹ 1,45,000. The market value of these two items as on the date of fire accident was ₹ 2,05,000.

Mr. Arnab received the following amounts from the insurance company:

(i)	Towards loss of stock	₹ 5,15,000
(ii)	Towards damage of machinery	₹ 8,07,000
(iii)	Towards gold chain and diamond ring	₹ 2,05,000

The salvaged machinery was taken over by the Insurance Company and there was no fresh addition of machinery during the year.

You are requested to briefly comment on the tax treatment of the above three items under the provisions of the Income-tax Act, 1961. *(6 Marks)*

(b) Discuss the tax implications arising consequent to conversion of a capital asset into stock-in-trade of business and its subsequent sale. *(2 Marks)*

(c) Miss Shruti, a wedding planner, has rendered services to Mr. Aakash kapoor in relation to marriage of his son. Miss Shruti, being a close relative of Mr. Aakash kapoor, has not charged any fee from him. Is service tax payable on such free, but taxable service? *(4 Marks)*

(d) Samrat & Co. purchased raw material 'X' for ₹ 30,00,000 plus VAT at 12.5%. Out of such raw material 80% was used for manufacture of taxable goods and the balance for the manufacture of exempted goods.

Another raw material 'Y' was purchased for ₹ 40,00,000 on which VAT was paid @1%. Out of the raw material 'Y', 50% was used for manufacture of taxable goods and the balance for the manufacture of exempted goods.

The entire taxable goods were sold for ₹ 60,00,000 plus VAT at 12.5%. There was no opening or closing inventory of taxable goods or raw materials.

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

Test Series: April, 2014

MOCK TEST PAPER – 2

INTERMEDIATE (IPC) – GROUP – I

PAPER – 4: TAXATION

SUGGESTED ANSWERS/HINTS

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

Particulars	**₹**
Income from salary (as per note 3)	5,23,901
Business Income (assuming that his wife carries on the business of hiring of cars) [Income of wife from hiring of car clubbed under section 64(1)(iv)]	32,000
Gross Total Income	**5,55,901**
Less: Deduction under section 80C (as per note 5)	1,00,000
Total income	**4,55,901**
Total income (rounded off)	**4,55,900**

Computation of tax liability of Mr. Rakesh for the A.Y.2014-15

	₹	₹
Step 1		
Add: Agricultural income and Non-agricultural income (₹ 3,05,000 +₹ 4,55,900)		
Tax on ₹ 7,60,900	**82,180**	
Step 2		
Add: Basic exemption limit to agricultural income (₹ 2,00,000 + ₹ 3,05,000)		
Tax on ₹ 5,05,000	**31,000**	
Step 3		
Tax on non-agricultural income (Tax under step 1 – Tax under step 2) (₹ 82,180 – ₹ 31,000)		51,180
Less: Rebate under section 87A (since total income < ₹ 5 lakhs)		2,000
		49,180

Add: Education cess @2% and Secondary and higher education cess @ 1%		1,475
Total tax liability		**50,655**
Total tax liability (rounded off)		**50,660**

Notes:

1. Valuation of rent free house

Particulars	**₹**
Basic salary	2,25,000
D.A. (not to be considered as it is not forming part of salary)	Nil
Commission on extra production	15,000
Bonus	12,000
Special allowance	14,000
Education allowance (See Note 4)	8,400
Medical allowance	8,000
Salary for the purpose of valuation of rent-free house	**2,82,400**
Value of rent-free house = 15% of ₹ 2,82,400	42,360

2. Valuation of perquisite of CD Player given for use to the employee

Taxable value of this perquisite is 10% p.a. of cost of the CD player w.e.f. 1.1.2014 (i.e. for 90 days)

10% of ₹ 26,000 = 2,600 x 90/365 = ₹ 641

Provision of laptop by the employer is a tax-free perquisite.

3. Income from salary

Particulars	**₹**	**₹**
Basic salary		2,25,000
D.A.		1,85,000
Bonus		12,000
Commission		15,000
Special Allowance		14,000
Taxable education allowance (See Note-4 below)		8,400
Medical Allowance		8,000
Total		**4,67,400**

Add : Taxable perquisites :		
1. Rent free accommodation (Note 1)	42,360	
2. Electricity Bill paid by employer	13,500	
3. CD Player given by employer (Note 2)	641	56,501
Taxable salary		**5,23,901**

4. Education allowance exempt under section 10(14)

Education allowance of ₹ 100 per month per child for a maximum of 2 children plus hostel allowance of ₹ 300 per month per child for a maximum of 2 children is exempt.

i.e. (₹ 100×2×12) + (₹ 300×2×12) =₹ 2,400 + ₹ 7,200 = ₹ 9,600

Therefore, taxable education allowance would be ₹ 18,000 – ₹ 9,600 = ₹ 8,400.

5. Investments/payments deductible under section 80C

Particulars	₹
Investment in PPF	60,000
Investment in 5 year Time Deposit in Post Office	12,000
Tuition fees of children (assumed to be paid to an eligible educational institution – hence qualifies for deduction under section 80C)	54,000
	1,26,000

However, the total deduction under section 80C cannot exceed ₹ 1,00,000. This restriction is contained in section 80CCE.

Therefore, the permissible deduction under section 80C would be ₹ 1,00,000

6. Taxability of gift received from grandfather

Gift from a relative is not taxable under section 56(2)(vii). Grandfather is a relative as per the definition of "relative" given in the Explanation to section 56(2)(vii) and hence ₹ 28,000, being gift received from grandfather, is not taxable.

(b) Computation of service tax liability of Super Stable Bank Ltd.:-

Particulars	Amount (₹)
Commission charged for preparing pay orders (Note-1)	50,000
Administrative charges (over and above interest) on loans, advances and deposits (Note-2)	6,00,000

Interest on overdraft (Note-3)	Nil
Commission charged for sale of foreign exchange to general public (Note-4)	9,00,000
Interest on loans with a collateral security (Note-3)	Nil
Interest on corporate deposits (Note-3)	Nil
Value of taxable service	15,50,000
Service tax @ 12% [₹ 15,50,000×12%]	1,86,000
Education cess @ 2% [₹ 1,86,000×2%]	3,720
Secondary and higher education cess @ 1% [₹1,86,000×1%]	1,860
Service tax liability	1,91,580

Notes:

1. The transaction in money is specifically excluded from the definition of service. However, making of a pay order by a bank is not a transaction in money since the bank charges a commission for preparation of a pay order. Hence, it is taxable.
2. Administrative charges or amounts collected over and above the interest or discount amounts on loans, advances and deposits would not be part of the negative list and thus would represent taxable consideration.
3. Following services are included in the negative list and hence not taxable:-
   - Overdraft facility provided in consideration for payment of interest.
   - Loans with a collateral security to the extent that the consideration for advancing such loans or advances are represented by way of interest.
   - Corporate deposits to the extent that the consideration for advancing such loans or advances are represented by way of interest or discount.
4. Services by way of sale of foreign exchange between banks or authorized dealers of foreign exchange or between banks and such dealers are included in the negative list. However, services provided by banks by way of sale of foreign exchange to general public would not be so covered and hence taxable.

(c) Computation of total turnover, input VAT and output VAT:-

Goods	Purchases	Input VAT credit	Sales	Output VAT
	₹	₹	₹	₹
X	4,00,000	Nil (since exempt)	4,50,000	Nil (since exempt)
Y (Refer Note below)	3,00,000	37,500	3,30,000	41,250

Z	5,00,000	20,000	7,00,000	28,000
Total	12,00,000	57,500	14,80,000	69,250

Hence, the total turnover is ₹14,80,000, input VAT is ₹57,500 and output VAT is ₹69,250.

Computation of VAT payable for the month of January, 2014:-

Particulars	**₹**	**₹**
Opening balance of Input VAT credit		6,000
Add: Input VAT credit for January, 2014		57,500
Total Input VAT credit available		63,500
Less: Output VAT payable on taxable turnover		69,250
Net VAT payable		5,750
Note: Purchase value of Goods Y (excluding VAT)		3,00,000
Add: Profit on cost @ 10%		30,000
Selling price before VAT		3,30,000
VAT @ 12.5% on selling price (rounded off)		41,250

2. **(a)** (i) As per section 43B, municipal tax is not deductible for A.Y. 2014-15 since it is not paid on or before 30.09.2014, being the due date of filing the return for A.Y. 2014-15.

Note – It is assumed that the company has not undertaken any international transaction during the year, and therefore, does not have to file a transfer pricing report under section 92E. Therefore, the due date of filing of return of the company would be 30th September, 2014.

(ii) Patent is an intangible asset eligible for depreciation@25%, as per section 32(1)(ii). Since it has been acquired and put to use for more than 180 days during the previous year 2013-14, full depreciation of ₹ 6,25,000 (i.e. 25% of ₹ 25,00,000) is allowable as deduction.

(iii) 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 is not eligible for deduction.

Deduction under section 35(2AB) = 200% of ₹ 10 lakhs = ₹ 20,00,000.

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).

(iv) Bad debts i.e. ₹ 4,00,000 written off in the books of account as irrecoverable is deductible under section 36(1)(vii), provided the debt has been taken into account in computing the income of the company in the current previous year or any of the earlier previous years.

(v) As per section 40(a)(v), income-tax of ₹ 1,10,000 paid by the company in respect of non-monetary perquisites provided to its employees, exempt in the employee's hands under section 10(10CC), is not deductible while computing business income of the employer–company.

(vi) Expenditure towards advertisement in souvenir of a political party is disallowed under section 37(2B) while computing business incomes.

However, the same is deductible under section 80GGB from gross total income provided the payment is made by any mode other than cash.

(vii) Refund of a trading liability is taxable under section 41(1), if a deduction was allowed in respect of the same to the taxpayer in an earlier year.

Since sales tax was claimed as expenditure in an earlier year, refund of the same during the year would attract the provisions of section 41(1).

(b) 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)	50,000
Security deposits forfeited for damages done by service receiver owing to his negligence in the course of receiving a service (Note-2)	4,00,000
Payment received from SBS Ltd. (Note-3)	1,50,000
Total	15,00,000
Value of taxable service=₹ 15,00,000× $\frac{100}{112.36}$	13,34,995
Service tax liability = =₹ 15,00,000× $\frac{12.36}{112.36}$	1,65,005

Notes:

1. Advances received in March, 2014 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. 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 ₹ 1,50,000 would form part of taxable value.

(c) 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 not be also 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.

3. (a) (i) Interest on borrowed capital is allowed as deduction under section 24(b)

As per section 24(b), Interest payable on loans borrowed for the purpose of acquisition, construction, repairs, renewal or reconstruction of house property can be claimed as deduction. Interest payable on borrowed capital for the period prior to the previous year in which the property has been acquired or constructed, can be claimed as deduction over a period of 5 years in equal annual installments commencing from the year of acquisition or completion of construction.

It is stated that the construction is completed only in June, 2014. Hence, deduction in respect of interest on housing loan cannot be claimed in the assessment year 2014-15.

(ii) Clause (xviii) of section 80C is attracted where there is any payment for the purpose of purchase or construction of a residential house property, the income from which is chargeable to tax under the head ‘Income from house property’. Such payment covers repayment of any amount borrowed from the National Housing Bank.

However, deduction is *prima facie* eligible only if the income from such property is chargeable to tax under the head "Income from House Property". During the assessment year 2014-15, there is no such income chargeable under this head. Hence, deduction under section 80C cannot be claimed for A.Y. 2014-15.

(b) (i) False : The exemption under section 54EC has been restricted, by limiting the maximum investment in long term specified assets (i.e. bonds of NHAI or RECL, redeemable after 3 years) to ₹ 50 lakh during any financial year. Therefore, in this case, the exemption under section 54EC can be availed only to the extent of ₹ 50 lakh, provided the investment is made within six months from the date of transfer.

(ii) True : As per section 47(xa), any transfer by way of conversion of bonds referred to in section 115AC into shares and debentures of any company is not regarded as transfer. Therefore, there will be no capital gains on conversion of foreign currency exchangeable bonds into shares or debentures.

(c) As per rule 3 of the Point of Taxation Rules, 2011, point of taxation would be determined as follows:-

1. Date of invoice or payment, whichever is earlier, if the invoice is issued within 30 days from the date of completion of service.
2. Date of completion of provision of service or payment, if the invoice is not issued within 30 days from the date of completion of service.

Point of taxation in each of the three given cases will be as under:

CASE I-The point of taxation is date of payment [15th February, 2014] as date of payment falls before date of issuance of invoice [20.02.2014] and invoice has been issued within 30 days of completion of service.

CASE II- The point of taxation is date of completion of service [5th February, 2014] as date of completion of service falls before date of payment [15.02.2014] and invoice [08.03.2014] has not been issued within 30 days of completion of service.

CASE III- The point of taxation is 10th February, 2014 as date of invoice [10.02.2014] falls before date of payment [15.02.2014] and invoice has been issued within 30 days of completion of service.

(d) The statement is valid. As soon as the dealer opts for the composition scheme, the VAT chain is broken. When a composition scheme is availed by a seller or buyer, he cannot claim input credit of the tax paid on the purchases.

Loss to the seller: If the composition scheme is availed by a dealer then such dealer cannot avail input tax credit in respect of input tax paid. Hence the dealer will be loosing the input tax credit on purchases made by him. He will not be able to pass on the benefit of input tax credit, which will add to the cost of the goods.

Loss to the purchaser: The purchaser shall not get any tax credit for the purchases made by him from the dealer operating under the composition scheme. Therefore, as soon as a dealer opts for the composition scheme, the VAT chain will be broken, and the benefit of tax paid earlier will not be passed on to the subsequent buyers.

4. (a) As the turnover of Avinash for F.Y.2012-13, i.e. ₹ 108 lakh, has exceeded the monetary limit of ₹ 100 lakh prescribed under section 44AB, he has to comply with the tax deduction provisions during the financial year 2013-14, subject to, however, the exemptions provided for under the relevant sections for applicability of TDS provisions.

Interest paid to SBI

TDS under section 194A is not attracted in respect of interest paid to a banking company.

Contract payment of ₹ 28,000 to Bala for 2 contracts of ₹ 14,000 each

TDS provisions under section 194C would not be attracted if the amount paid to a contractor does not exceed ₹ 30,000 in a single payment or ₹ 75,000 in the aggregate during the financial year. Therefore, TDS provisions under section 194C are not attracted in this case.

Shop Rent paid to one payee – Tax has to be deducted under section 194-I as the rental payment exceeds ₹ 1,80,000.

Commission paid to Lalu – Tax has to be deducted under section 194-H as the commission exceeds ₹ 5,000.

(b) (i) Disagree

The return of income of LLP should be signed by a designated partner.

Any other partner can sign the Return of Income of LLP **only in** the following cases:-

(a) where for any unavoidable reason such designated partner is not able to sign and verify the return, or,

(b) where there is no designated partner.

(ii) Disagree

In case Mr. Sameer opts to offer his income as per the presumptive taxation provisions of section 44AD, then, the due date under section 139(1) for filing of return of income for the year ended 31.03.2014, shall be 31st July, 2014.

It is only in case Mr. Sameer does not opt for presumptive taxation provisions under section 44AD and offers income to be lower than 8% of total turnover and his total income exceeds the basic exemption limit, he has to keep books of account as per section 44AA and get his accounts audited under section 44AB, in which case the due date for filing return would be 30th September, 2014.

(c) Where an assessee has issued an invoice, or received any payment, against a service to be provided which is not so provided by him either wholly or partially for any reason or where the amount of invoice is renegotiated due to deficient provision of service, or any terms contained in a contract, the assessee may take the credit of such excess service tax paid by him, if the assessee:

(i) has refunded the payment or part thereof, so received for the service provided to the person from whom it was received; or

(ii) has issued a credit note for the value of the service not so provided to the person to whom such an invoice had been issued.

(d) Computation of VAT payable:-

Stage	Particulars	VAT Liability	Less VAT Credit	Tax to Government
I	Crackers sold by Blast Ltd. to Bonanza Ltd. at ₹ 60,000	=60,000 × 4% =2,400	--	2,400
II	Crackers sold by Bonanza Ltd to Pimpom Ltd. at ₹ 72,000 (₹ 60,000 × 120%)	=72,000 × 4% =2,880	2,400	480
III	Crackers sold by Pimpom Ltd. to Fit Ltd. at ₹ 90,000 (₹ 72,000 × 125%)	=90,000 × 4% =3,600	2,880	720
IV	Crackers sold by Fit Ltd. to ultimate consumers at ₹ 1,17,000 (₹ 90,000 ×130%)	=1,17,000 × 4% =4,680	3,600	1,080

5. (a) Computation of Gross Total Income of Ms. Neena for the Assessment Year 2014-15

Particulars	₹
Profits and gains of business and profession	
Salary received as a partner from a partnership firm is taxable under the head "Profits and gains of business and profession"	8,37,000
Less: Brought forward business loss of Assessment Year 2013-14 to be set-off against business income	8,37,000

		Nil
Capital Gains		
Long term capital gain on sale of land (See Note 2)		5,75,000
Income from other sources		
Cash gift received from friends - since the value of cash gift exceeds ₹ 50,000, the entire sum is taxable	53,000	
Dividend received from a domestic company is exempt under section 10(34)	Nil	53,000
Gross Total Income		**6,28,000**

Notes :

1. Balance brought forward business loss of assessment year 2013-14 of ₹ 2,02,000 has to be carried forward to the next year.
2. Long-term capital loss on sale of shares cannot be set-off against long-term capital gain on sale of land since loss from an exempt source cannot be set-off against profit from a taxable source. Since long-term capital gain on sale of listed shares on which STT is paid is exempt under section 10(38), loss on sale of listed shares is a loss from an exempt source. So, it cannot be set-off against long-term capital gain on sale of land, which is a profit from a taxable source.

(b) Citizenship of a country and residential status of that country are separate concepts. A person may be an Indian national /citizen, but may not be a resident in India. On the other hand, a person may be a foreign national /citizen, but may be a resident in India. The citizenship of an individual has no role in determining the residential status of an individual.

The residential status of resident, non-resident, etc. is determined on the basis of number of days an individual actually stays in India during the previous year.

The provisions of section 6 of the Income-tax Act, 1961 are the determining factor of residential status of an individual.

(c) 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 = \$ 2,00,000 × ₹ 60

= ₹ 1,20,00,000

(b) UK pound converted into Indian rupees = £ 1,00,000 × ₹ 100

= ₹ 1,00,00,000

Value of taxable service = 1% of ₹ 1,00,00,000 = ₹ 1,00,000

(d) **(i)** Purchases made by Aggarwal & Co are eligible for input tax credit as purchases for use in the execution of works contract are eligible for input tax credit.

(ii) Purchases made by Sandeep are not eligible for input tax credit as the purchases where invoice does not show the amount of tax separately are not eligible for input tax credit.

6. (a) Computation of income from house property of Mr. Aakash for A.Y. 2014-15

Particulars	**₹**	**₹**
Annual value is nil (since house is self occupied)		Nil
Less : Deduction under section 24(b)		
Interest paid on borrowed capital ₹ 25,00,000 @ 12%	3,00,000	
Pre-construction interest ₹ 3,00,000 / 5	60,000	
	3,60,000	
As per second proviso to section 24(b), interest deduction restricted to		1,50,000
Loss under the head "income from house property" of Mr. Aakash		(1,50,000)

Computation of income from house property of Mr. Binoy for A.Y. 2014-15

Particulars		**Ground floor (Self occupied)**	**First floor**
Gross annual value (See note below)		Nil	1,20,000
Less :Municipal taxes (for first floor)			5,000
Net annual value	(A)	Nil	1,15,000
Less : Deduction under section 24			
(a) 30% of net annual value			34,500
(b) interest on borrowed capital			
Current year interest			
₹15,00,000 x 10% = ₹ 1,50,000		75,000	75,000
Pre-construction interest			
₹ 15,00,000 x 10% x 9/12 = ₹ 1,12,500			
₹ 1,12,500 allowed in 5 equal installments			

₹ 1,12,500 / 5 = ₹ 22,500 per annum		11,250	11,250
Total deduction under section 24	(B)	86,250	1,20,750
Income from house property (A)-(B)		(86,250)	(5,750)
Loss under the head "income from house property" of Mr. Binoy (both ground floor and first floor)		(92,000)	

Note : Computation of Gross Annual Value (GAV) of first floor of Binoy's house

If a single unit of property (in this case the first floor of Binoy's house) is let out for some months and self-occupied for the other months, then the annual letting value (ALV) of the property shall be taken into account for determining the annual value. The ALV shall be compared with the actual rent and whichever is higher shall be adopted as the annual value. In this case, the actual rent shall be the rent for the period for which the property was let out during the previous year.

The Annual Letting Value (ALV) is the higher of fair rent and municipal value. This should be considered for 9 months since the construction of property was completed only on 30.6.2013.

Annual letting value	= ₹ 1,12,500 being higher of -
	Fair rent = ₹ 1,50,000 x 9 /12 = ₹ 1,12,500 Municipal value = 80,000 x 9/12 = ₹ 60,000
Actual rent =	₹ 1,20,000 (₹ 20,000 p.m. for 6 months from July to December, 2013)

Gross annual value = ₹ 1,20,000 (being higher of ALV of ₹ 1,12,500 and actual rent of ₹ 1,20,000)

(b) **(i)** **The statement is false.** 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 true.** Services provided by RBI are not chargeable to service tax as they are included in the negative list of services.

(iii) **The statement is true.** Provision of service by an employee to the employer 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.** Explanation to the definition of service clarifies that the term 'service' does not cover duties performed by Members of Parliament and State Legislatures. Hence, they are not liable to service tax.

(c) **(i)** The statement is false. Taxpayer's Identification Number (TIN) is a 11 digit numeral. The first two characters represent State Code as used by the Union Ministry of Home Affairs and the next nine characters will be different in different states.

(ii) The statement is true. Under VAT, a dealer assesses the VAT liability on his own and submits the return. The dealer is deemed to be self-assessed on the basis of the return filed by him if he does not receive any notice proposing departmental audit of his books of account within the time-limit specified in the VAT Act of the respective State.

7. (a) (i) Compensation towards loss of stock: Any compensation received from the insurance company towards loss/damage to stock in trade is to be construed as a trading receipt. Hence, ₹ 5,15,000 received as insurance claim for loss of stock has to be assessed under the head "Profit and gains of business or profession".

Note - The assessee can claim the value of stock destroyed by fire as revenue loss, eligible for deduction while computing income under the head "Profits and gains of business or profession".

(ii) Compensation towards damage to machinery: Since the salvaged machinery was taken over by the Insurance Company, and there was no fresh addition of machinery during the year, the block of machinery will cease to exist. Therefore, ₹ 4,28,000 being the excess of written down value (i.e ₹ 12,35,000) over the insurance compensation (i.e. ₹ 8,07,000) will be assessable as a short-term capital loss.

Note – If new machinery is purchased in the next year, it will constitute the new block of machinery, on which depreciation can be claimed for that year.

(iii) Compensation towards loss of gold chain and diamond ring: Gold chain and diamond ring are capital assets as envisaged by section 2(14). They are not "personal effects", which alone are to be excluded. As per section 45(1A), if any profit or gain arises in a previous year owing to receipt of insurance claim, the same shall be chargeable to tax as capital gains. The capital gains has to be computed by reducing the indexed cost of acquisition of jewellery from the insurance compensation of ₹ 2,05,000.

(b) The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade. However, as per section 45(2), the profits or gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold. For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset. Indexation benefit is available upto the year of conversion of capital asset in stock-in-trade.

On subsequent sale of such stock-in-trade, business profits would arise. The business income chargeable to tax would be the difference between the price at which the stock-in-trade is sold and the fair market value on the date of conversion of the capital asset into stock-in-trade.

(c) Section 67(1)(iii) and Service Tax (Determination of Value) Rules, 2006 make provisions for valuation even when consideration is not ascertainable. However, these provisions apply only when there is consideration. If there is no consideration i.e., in case of free service, section 67 and Service Tax (Determination of Value) Rules, 2006 cannot apply.

Thus, no service tax is payable when value of service is zero. In other words, if the value is zero, the tax will also be zero even though the service may be taxable. However, this principle applies only when there is really a 'free service' and not when its cost is recovered through other means.

Therefore, in the light of the aforesaid discussion, it may be inferred that, the service tax is not payable on service rendered by Miss Shruti to Mr. Aakash Kapoor as Miss Shruti has not charged any fee from Mr. Aakash Kapoor.

(d) Computation of VAT liability of Samrat & Co.

Particulars	**₹**	**₹**
Output VAT (60,00,000 x 12.5%) (A)		7,50,000
Input VAT (B)		
Raw material 'X' (30,00,000 x 80% x 12.5%) (Refer Note 1)	3,00,000	
Raw material 'Y' (40,00,000 x 50% x 1%) (Refer Note 2)	20,000	3,20,000
Net VAT payable by Samrat & Co. (A) – (B)		4,30,000

Notes:

(1) In respect of the raw material 'X', input tax credit is allowed only to the extent raw material 'X' is used in manufacture of taxable goods and hence the same is restricted to the extent of 80%.

(2) In respect of the raw material 'Y', input tax credit is allowed only to the extent raw material 'Y' is used in manufacture of taxable goods and hence the same is restricted to the extent of 50%.